

Tencent 腾讯

Tencent Holdings Limited

Incorporated in the Cayman Islands with limited liability

騰訊控股有限公司

於開曼群島註冊成立的有限公司

(Stock Code 股份代號 : 700)



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Interim Report 2012

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Financial Performance Highlights

FIRST HALF OF 2012

	Unaudited Six months ended		Year- on-year change
	30 June 2012	30 June 2011	
	<i>(RMB in millions, unless specified)</i>		
Revenues	20,175.1	13,077.5	54.3%
Operating profit	7,629.0	6,170.4	23.6%
Profit for the period	6,072.9	5,227.5	16.2%
Profit attributable to equity holders of the Company	6,049.6	5,219.6	15.9%
Non-GAAP profit attributable to equity holders of the Company	6,667.3	5,271.5	26.5%
EPS (RMB per share)			
– basic	3.316	2.863	15.8%
– diluted	3.252	2.800	16.1%

SECOND QUARTER OF 2012

	Unaudited Three months ended			Year- on-year change
	30 June 2012	31 March 2012	Quarter- on-quarter change	
	<i>(RMB in millions, unless specified)</i>			
Revenues	10,527.2	9,647.9	9.1%	56.2%
Operating profit	3,937.6	3,691.4	6.7%	41.4%
Profit for the period	3,110.6	2,962.3	5.0%	32.7%
Profit attributable to equity holders of the Company	3,100.1	2,949.5	5.1%	32.0%
Non-GAAP profit attributable to equity holders of the Company	3,386.3	3,281.1	3.2%	26.0%
EPS (RMB per share)				
– basic	1.698	1.618	4.9%	31.7%
– diluted	1.665	1.587	4.9%	32.1%

Chairman's Statement

I am pleased to present our interim report for the three and six months ended 30 June 2012 to the shareholders.

RESULTS

The Group's unaudited profit attributable to equity holders of the Company for the three and six months ended 30 June 2012 increased by 32.0% and 15.9% on a year-on-year basis to RMB3,100 million and RMB6,050 million respectively. Basic EPS for the three and six months ended 30 June 2012 were RMB1.698 and RMB3.316 respectively. Diluted EPS for the three and six months ended 30 June 2012 were RMB1.665 and RMB3.252 respectively.

BUSINESS REVIEW AND OUTLOOK

Overall Financial Performance

Despite maturing Internet user growth and decelerating economic growth, we sustained healthy year-on-year improvements in our revenues, earnings, and cash flow during the second quarter of 2012. Our IVAS business continued to expand year-on-year as our existing and new games added users, and as we generated more revenue from applications on our open platforms. Our MVAS business experienced modest growth during the quarter, thanks primarily to our bundled SMS packages and mobile games. Our online advertising business achieved a significant year-on-year growth rate, due to new platform contributions and market share gains in key advertiser categories. Revenue of our e-Commerce transactions business increased sequentially, benefiting from growth in GMV of principal transactions and, to a lesser extent, commission fees derived from transactions on our marketplace.

Strategic Highlights

In May 2012, we announced a reorganisation of our business units into six new business groups. In addition, a wholly-owned subsidiary has been formed for managing our e-Commerce transactions business. This reorganisation is intended to help us capture new opportunities in the evolving Internet industry, by better allocating our resources toward the core technologies and platforms that may support our future business growth.

We believe establishment of the new business groups will reinforce our entrepreneurial spirit, execution and innovation, and will sharpen each group's focus on addressing its target users' needs. Simultaneously, under the principle of "One Tencent", the business groups will continue to enjoy company-wide synergies by sharing technical infrastructure and by integrating certain services, where we believe such integration brings value to users.

Chairman's Statement

Divisional and Product Highlights

IM Platform

MAUs of QQ IM increased by 12% on a year-on-year basis to 784 million at the end of the second quarter of 2012. Such growth rate was broadly in line with the user growth of the overall Internet market in China. PCU for the quarter was 167 million, representing 22% growth as compared to the same period last year. Per user engagement continued to improve, as evidenced by the year-on-year growth rates of PCU and daily user hours exceeding that of MAUs. We believe QQ IM's PCU growth rate may slow in future as increased mobile usage creates more dispersion of time spent on QQ IM through different day parts.

Media Platforms

We believe we are uniquely positioned in the China Internet market because of our leadership across multiple media platforms, and our ability to provide cross-platform integration and user benefits. During the second quarter of 2012, we expanded our platforms and deepened our media influence. QQ.com continued to lead amongst Internet portals in China in terms of traffic and unique visitors. Recently, we have revamped QQ.com's front page and certain major channels to help users find and share news, video, and microblog content more easily. Tencent Microblog further expanded its user base, with 469 million registered users and 82 million DAUs at the end of the second quarter of 2012. Tencent Video achieved solid user growth as we continued to enrich our content and improve our user experience.

IVAS

In the second quarter of 2012, our online communities registered continued growth in user base. Qzone maintained its position as the leading social network in China, with MAUs increasing by 12% on a year-on-year basis to 598 million at the end of the second quarter of 2012. MAUs of Pengyou reached 248 million at the end of the quarter, representing year-on-year growth of 31%. For our IVAS subscription services, we introduced more stringent measures during the quarter to clean up free-riders who subscribed through telecommunications operators, in order to enhance the quality of our subscriber base. As a result of these measures, our IVAS registered subscriptions declined and our overall collection rates improved. Given these measures mostly affected non-paying users, they had limited impact on our revenues. As for our open platforms, we continued to introduce more third-party and first-party applications to users during the second quarter. Consequently, item-based sales within applications grew strongly. Recently, we have introduced a streamlined process for third-party developers to launch their applications across our range of services more efficiently.

Our online game business continued to grow in terms of users and revenues. Contributions from international markets, whose seasonality may differ from that of China, continued to climb as we broadened our user base in different regions. Our QQ Game Platform enjoyed a healthy growth rate, with its PCU increasing by 17% on a year-on-year basis to 8.8 million for the second quarter of 2012.

We continued to develop our game pipeline, putting new titles such as Legend of Yulong and NBA2K Online into closed beta testing during the second quarter. In July, we announced an exclusive strategic partnership with Activision Blizzard to bring its Call of Duty Online title to China. We believe that our game platform and operational expertise will support the delivery of what we expect to be an immersive and highly interactive game experience.

Chairman's Statement

MVAS

In the second quarter of 2012, our MVAS business registered stable year-on-year revenue growth and modest sequential revenue growth, primarily from our bundled SMS packages and mobile games. We continued to market our smartphone applications, such as mobile security and mobile browser, to further expand our user base on the mobile Internet. The regulatory environment for MVAS remains uncertain, and we will continue to position for the mobile Internet future.

Online Advertising

Driven by new platform contributions and market share gains in key advertiser categories, we achieved a robust year-on-year revenue growth rate in the second quarter of 2012. Our sequential revenue growth was mainly driven by positive seasonality and improved monetisation on our new platforms. Within brand display advertising, our strong traffic and high ROI enabled us to sustain growth despite a more challenging macro environment, and revenues from our online video platform more than doubled sequentially. Within performance-based display advertising, we achieved strong revenue growth on our social networks during the quarter, reflecting more inventory and thus impressions made available to advertisers, as well as improved click-through rates on the back of enhancements to our targeted advertising system. Within search advertising, we grew revenues from desktop search, mobile search, and e-Commerce search, while continuing to improve our search results quality, mobile search experience, and search integration with upstream properties, such as our portal and mobile browser.

e-Commerce Transactions

Despite an intensively competitive market environment, GMV of our principal transactions increased sequentially during the second quarter of 2012. Commission fees derived from transactions on our marketplace also increased, albeit from a low base. We will continue our efforts to leverage our significant user base to build an e-Commerce open platform and a healthy industry value chain.

DIVIDEND

The Board did not propose any interim dividend for the six months ended 30 June 2012 (for the six months ended 30 June 2011: Nil).

APPRECIATION

With our employees' and management's unwavering dedication, we have successfully better served our user community. The Board would like to take this opportunity to thank them, as well as the shareholders and stakeholders of the Company, for their continuous support, contribution and commitment going forward.

Ma Huateng

Chairman

Hong Kong, 15 August 2012

Management Discussion and Analysis

SECOND QUARTER OF 2012 COMPARED TO FIRST QUARTER OF 2012

The following table sets forth the comparative figures for the second quarter of 2012 and the first quarter of 2012:

	Unaudited	
	Three months ended	
	30 June	31 March
	2012	2012
	RMB'000	<i>RMB'000</i>
Revenues	10,527,244	9,647,858
Cost of revenues	(4,311,379)	(3,836,317)
Gross profit	6,215,865	5,811,541
Interest income	196,806	166,733
Other losses, net	(3,219)	(63,642)
Selling and marketing expenses	(609,672)	(469,200)
General and administrative expenses	(1,862,165)	(1,754,074)
Operating profit	3,937,615	3,691,358
Finance costs, net	(115,256)	(69,982)
Share of profit/(losses) of associates	5,411	(9,753)
Share of (losses)/profit of jointly controlled entities	(9,375)	1,380
Profit before income tax	3,818,395	3,613,003
Income tax expense	(707,824)	(650,673)
Profit for the period	3,110,571	2,962,330
Attributable to:		
Equity holders of the Company	3,100,075	2,949,510
Non-controlling interests	10,496	12,820
	3,110,571	2,962,330
Non-GAAP profit attributable to equity holders of the Company	3,386,266	3,281,064

Management Discussion and Analysis

Revenues. Revenues increased by 9% to RMB10,527 million for the second quarter of 2012 from RMB9,648 million for the first quarter of 2012. The following table sets forth our revenues by line of business for the second quarter of 2012 and the first quarter of 2012:

	Unaudited			
	Three months ended			
	30 June 2012		31 March 2012	
	Amount	% of total revenues	Amount	% of total revenues
	<i>(RMB in thousands, unless specified)</i>			
IVAS	7,786,625	74.0%	7,381,621	76.5%
MVAS	929,007	8.8%	913,842	9.5%
Online advertising	879,691	8.4%	540,113	5.6%
e-Commerce transactions	857,526	8.1%	752,817	7.8%
Others	74,395	0.7%	59,465	0.6%
Total revenues	<u>10,527,244</u>	<u>100.0%</u>	<u>9,647,858</u>	<u>100.0%</u>

- Revenues from our IVAS increased by 5% to RMB7,787 million for the second quarter of 2012 from RMB7,382 million for the first quarter of 2012. Online game revenues increased by 5% to RMB5,565 million. Game revenues from China registered modest growth during the quarter with weaker seasonality due to school examinations, while contributions from international markets, whose seasonality may differ from that of China, continued to climb. Revenues from our community and open platforms increased by 8% to RMB2,222 million, riding on growth in item-based sales within applications, including those on our SNS platforms. QQ Membership subscriptions revenue also contributed to the increase.
- Revenues from our MVAS increased by 2% to RMB929 million for the second quarter of 2012 from RMB914 million for the first quarter of 2012. This was mainly attributable to growth in our bundled SMS packages and mobile games.
- Revenues from our online advertising business increased by 63% to RMB880 million for the second quarter of 2012 from RMB540 million for the first quarter of 2012. In addition to more favourable seasonality in the second quarter, our online advertising business benefited from the rapid revenue growth of performance advertising on our social networks, and brand display advertising on our online video platform.
- Revenues from our e-Commerce transactions business increased by 14% to RMB858 million for the second quarter of 2012 from RMB753 million for the first quarter of 2012. This primarily reflected growth in GMV of principal e-Commerce transactions. Commission fees generated from transactions on our marketplace also contributed to the growth of our e-Commerce transactions business.

Management Discussion and Analysis

Cost of revenues. Cost of revenues increased by 12% to RMB4,311 million for the second quarter of 2012 from RMB3,836 million for the first quarter of 2012. This mainly reflected an increase in sharing costs, cost of merchandise sold, staff costs and bandwidth and server custody fees. As a percentage of revenues, cost of revenues increased to 41% for the second quarter of 2012 from 40% for the first quarter of 2012. The following table sets forth our cost of revenues by line of business for the second quarter of 2012 and the first quarter of 2012:

	Unaudited			
	Three months ended			
	30 June 2012		31 March 2012	
	Amount	% of segment revenues	Amount	% of segment revenues
<i>(RMB in thousands, unless specified)</i>				
IVAS	2,645,374	34.0%	2,408,823	32.6%
MVAS	358,935	38.6%	338,839	37.1%
Online advertising	421,288	47.9%	316,183	58.5%
e-Commerce transactions	836,005	97.5%	732,051	97.2%
Others	49,777	66.9%	40,421	68.0%
Total cost of revenues	<u>4,311,379</u>		<u>3,836,317</u>	

- Cost of revenues for our IVAS increased by 10% to RMB2,645 million for the second quarter of 2012 from RMB2,409 million for the first quarter of 2012. This was mainly driven by an increase in sharing costs as a result of revenue growth of certain licensed games. Bandwidth and server custody fees also increased along with the expansion of our business.
- Cost of revenues for our MVAS increased by 6% to RMB359 million for the second quarter of 2012 from RMB339 million for the first quarter of 2012. This primarily reflected higher staff costs. Bandwidth and server custody fees and sharing costs also contributed to the increase.
- Cost of revenues for our online advertising business increased by 33% to RMB421 million for the second quarter of 2012 from RMB316 million for the first quarter of 2012. This primarily reflected greater commissions payable to advertising agencies and increased sharing costs for our search business. Content costs related to our online video platform and staff costs also rose.
- Cost of revenues for our e-Commerce transactions business increased by 14% to RMB836 million for the second quarter of 2012 from RMB732 million for the first quarter of 2012, primarily driven by greater cost of merchandise sold as a result of growth in GMV of principal transactions.

Management Discussion and Analysis

Other losses, net. Other losses, net decreased by 95% to RMB3 million for the second quarter of 2012 from RMB64 million for the first quarter of 2012. This mainly reflected no donation being made to the Tencent Charity Fund in the second quarter of 2012, whereas RMB60 million was made to the fund in the first quarter of 2012.

Selling and marketing expenses. Selling and marketing expenses increased by 30% to RMB610 million for the second quarter of 2012 from RMB469 million for the first quarter of 2012. This primarily reflected an increase in promotion and advertising expenses related to our products and platforms such as new online games and online security products. Staff costs also contributed to the increase in selling and marketing expenses. As a percentage of revenues, selling and marketing expenses increased to 6% for the second quarter of 2012 from 5% for the first quarter of 2012.

General and administrative expenses. General and administrative expenses increased by 6% to RMB1,862 million for the second quarter of 2012 from RMB1,754 million for the first quarter of 2012. This mainly reflected an increase in research and development expenses and staff costs due to the growth of our business scale, partly offset by a decrease in intangible asset amortisation as certain intangible assets acquired through acquisition were fully amortised in the first quarter of 2012. As a percentage of revenues, general and administrative expenses was 18% for the second quarter of 2012, stable compared to the first quarter of 2012.

Finance costs, net. Finance costs, net increased by 65% to RMB115 million for the second quarter of 2012 from RMB70 million for the first quarter of 2012. This mainly reflected the recognition of exchange losses on our foreign currency denominated debts resulting from exchange rate movements in the second quarter of 2012.

Income tax expense. Income tax expense increased by 9% to RMB708 million for the second quarter of 2012 from RMB651 million for the first quarter of 2012. This primarily reflected an increase in profit before tax and the absence of deferred tax liabilities reversal arising from the Riot Games Acquisition.

Profit attributable to equity holders of the Company. Profit attributable to equity holders of the Company increased by 5% to RMB3,100 million for the second quarter of 2012 from RMB2,950 million for the first quarter of 2012. Non-GAAP profit attributable to equity holders of the Company increased by 3% to RMB3,386 million for the second quarter of 2012 from RMB3,281 million for the first quarter of 2012.

Management Discussion and Analysis

SECOND QUARTER OF 2012 COMPARED TO SECOND QUARTER OF 2011

The following table sets forth the comparative figures for the second quarter of 2012 and the second quarter of 2011:

	Unaudited	
	Three months ended	
	30 June	30 June
	2012	2011
	RMB'000	RMB'000
Revenues	10,527,244	6,739,044
Cost of revenues	(4,311,379)	(2,331,637)
Gross profit	6,215,865	4,407,407
Interest income	196,806	106,546
Other (losses)/gains, net	(3,219)	2,809
Selling and marketing expenses	(609,672)	(369,491)
General and administrative expenses	(1,862,165)	(1,363,372)
Operating profit	3,937,615	2,783,899
Finance (costs)/income, net	(115,256)	1,771
Share of profit of associates	5,411	23,454
Share of losses of jointly controlled entities	(9,375)	(60,689)
Profit before income tax	3,818,395	2,748,435
Income tax expense	(707,824)	(405,163)
Profit for the period	3,110,571	2,343,272
Attributable to:		
Equity holders of the Company	3,100,075	2,349,246
Non-controlling interests	10,496	(5,974)
	3,110,571	2,343,272
Non-GAAP profit attributable to equity holders of the Company	3,386,266	2,686,757

Management Discussion and Analysis

Revenues. Revenues increased by 56% to RMB10,527 million for the second quarter of 2012 from RMB6,739 million for the second quarter of 2011. The following table sets forth our revenues by line of business for the second quarter of 2012 and the second quarter of 2011:

	Unaudited			
	Three months ended			
	30 June 2012		30 June 2011	
	Amount	% of total revenues	Amount	% of total revenues
	<i>(RMB in thousands, unless specified)</i>			
IVAS	7,786,625	74.0%	5,386,578	79.9%
MVAS	929,007	8.8%	793,839	11.8%
Online advertising	879,691	8.4%	512,312	7.6%
e-Commerce transactions	857,526	8.1%	–	–
Others	74,395	0.7%	46,315	0.7%
Total revenues	<u>10,527,244</u>	<u>100.0%</u>	<u>6,739,044</u>	<u>100.0%</u>

- Revenues from our IVAS increased by 45% to RMB7,787 million for the second quarter of 2012 from RMB5,387 million for the second quarter of 2011. Online game revenues increased by 53% to RMB5,565 million. This mainly reflected the increased popularity of our major titles such as Cross Fire, QQ Dancer, DNF, and QQ Speed in the China market, the growth of our mini casual games, as well as contributions from new titles and international markets. Revenues from our community and open platforms increased by 27% to RMB2,222 million, primarily attributable to growth in our open platforms and QQ Membership. Revenues from our open platforms grew on the back of a significant increase in item-based sales within applications, including those on our SNS platforms. The growth in QQ Membership mainly reflected an expanded subscriber base driven by enhanced privileges and value-added functions.
- Revenues from our MVAS increased by 17% to RMB929 million for the second quarter of 2012 from RMB794 million for the second quarter of 2011. This was primarily driven by an increase in revenues from our bundled SMS packages and mobile games.
- Revenues from our online advertising business increased by 72% to RMB880 million for the second quarter of 2012 from RMB512 million for the second quarter of 2011. This mainly reflected the revenue contributions from performance advertising on our social networks, the rapid growth of brand display advertising on our online video platform, and search advertising. Traditional brand display advertising also contributed to our business growth.
- Revenues from our e-Commerce transactions business, which primarily consist of revenues from merchandise sales in principal transactions and commission fees generated from transactions on our marketplace, amounted to RMB858 million for the second quarter of 2012.

Management Discussion and Analysis

Cost of revenues. Cost of revenues increased by 85% to RMB4,311 million for the second quarter of 2012 from RMB2,332 million for the second quarter of 2011. This mainly reflected the recognition of cost of merchandise sold relating to our e-Commerce transactions business as well as an increase in sharing costs and staff costs. As a percentage of revenues, cost of revenues increased to 41% for the second quarter of 2012 from 35% for the second quarter of 2011. The following table sets forth our cost of revenues by line of business for the second quarter of 2012 and the second quarter of 2011:

	Unaudited			
	Three months ended			
	30 June 2012		30 June 2011	
	Amount	% of segment revenues	Amount	% of segment revenues
	<i>(RMB in thousands, unless specified)</i>			
IVAS	2,645,374	34.0%	1,788,240	33.2%
MVAS	358,935	38.6%	322,454	40.6%
Online advertising	421,288	47.9%	168,624	32.9%
e-Commerce transactions	836,005	97.5%	–	–
Others	49,777	66.9%	52,319	113.0%
Total cost of revenues	<u>4,311,379</u>		<u>2,331,637</u>	

- Cost of revenues for our IVAS increased by 48% to RMB2,645 million for the second quarter of 2012 from RMB1,788 million for the second quarter of 2011. This mainly reflected growth in sharing costs driven by increased revenues from licensed games. Staff costs also increased as our business grew.
- Cost of revenues for our MVAS increased by 11% to RMB359 million for the second quarter of 2012 from RMB322 million for the second quarter of 2011. This primarily reflected higher bandwidth and server custody fees as well as an increase in mobile and telecommunications revenue sharing costs.
- Cost of revenues for our online advertising business increased by 150% to RMB421 million for the second quarter of 2012 from RMB169 million for the second quarter of 2011. The increase was primarily driven by the allocation of a significant proportion of costs related to our online video platform, which include content costs as well as bandwidth and server custody fees, to the online advertising segment since the fourth quarter of 2011. It was also driven by an increase in staff costs, sales commissions payable to advertising agencies and sharing costs for our search advertising business as our business expanded.
- Cost of revenues for our e-Commerce transactions business, which primarily consists of cost of merchandise sold, amounted to RMB836 million for the second quarter of 2012.

Management Discussion and Analysis

Other (losses)/gains, net. We recorded other losses, net of RMB3 million for the second quarter of 2012, compared to other gains, net of RMB3 million for the second quarter of 2011.

Selling and marketing expenses. Selling and marketing expenses increased by 65% to RMB610 million for the second quarter of 2012 from RMB369 million for the second quarter of 2011. This primarily reflected an increase in promotion and advertising expenses related to products and platforms such as online games, online security products and mobile applications. Staff costs also increased as our business expanded. As a percentage of revenues, selling and marketing expenses increased to 6% for the second quarter of 2012 from 5% for the second quarter of 2011.

General and administrative expenses. General and administrative expenses increased by 37% to RMB1,862 million for the second quarter of 2012 from RMB1,363 million for the second quarter of 2011. This was mainly driven by an increase in research and development expenses and staff costs, partly offset by a decrease in intangible asset amortisation as certain intangible assets acquired through acquisition were fully amortised in the first quarter of 2012. As a percentage of revenues, general and administrative expenses decreased to 18% for the second quarter of 2012 from 20% for the second quarter of 2011.

Finance (costs)/income, net. We recorded finance costs, net of RMB115 million for the second quarter of 2012, compared to finance income, net of RMB2 million for the second quarter of 2011. The change primarily reflected an increase in interest-bearing debts and the recognition of exchange losses on our foreign currency denominated debts resulting from exchange rate movements in the second quarter of 2012.

Income tax expense. Income tax expense increased by 75% to RMB708 million for the second quarter of 2012 from RMB405 million for the second quarter of 2011. This was primarily driven by an increase in profit before tax. The increase also reflected the absence of deferred tax liabilities reversal arising from the Riot Games Acquisition and lower income tax expense reversal as a result of the finalisation of our corporate income tax assessment.

Profit attributable to equity holders of the Company. Profit attributable to equity holders of the Company increased by 32% to RMB3,100 million for the second quarter of 2012 from RMB2,349 million for the second quarter of 2011. Non-GAAP profit attributable to equity holders of the Company increased by 26% to RMB3,386 million for the second quarter of 2012 from RMB2,687 million for the second quarter of 2011.

Management Discussion and Analysis

OTHER FINANCIAL INFORMATION

	Unaudited		Unaudited		
	Six months ended		Three months ended		
	30 June 2012	30 June 2011	30 June 2012	31 March 2012	30 June 2011
	<i>(RMB in thousands, unless specified)</i>				
EBITDA (a)	8,585,869	6,392,021	4,331,322	4,254,547	3,171,308
Adjusted EBITDA (a)	9,020,172	6,726,473	4,558,963	4,461,209	3,361,637
Adjusted EBITDA margin (b)	44.7%	51.4%	43.3%	46.2%	49.9%
Interest expense	136,922	29,817	69,344	67,578	13,132
Net cash (c)	19,631,631	15,749,917	19,631,631	20,818,507	15,749,917
Capital expenditures (d)	1,577,286	1,663,863	915,156	662,130	943,047

Note:

- (a) EBITDA consists of operating profit less interest income, and plus other losses/(gains), net, depreciation of fixed assets and investment properties and amortisation of intangible assets. Adjusted EBITDA consists of EBITDA plus equity-settled share-based compensation expenses.
- (b) Adjusted EBITDA margin is calculated by dividing Adjusted EBITDA by revenues.
- (c) Net cash is calculated as cash and cash equivalents, term deposits with initial term of over three months, and restricted cash pledged for secured bank borrowings, minus total borrowings and long-term notes payable.
- (d) Capital expenditures consist of additions (excluding business combination) to fixed assets, construction in progress, land use rights and intangible assets (excluding game and other content licences).

Management Discussion and Analysis

The following table reconciles our operating profit to our EBITDA and Adjusted EBITDA for the periods indicated:

	Unaudited		Unaudited		
	Six months ended		Three months ended		
	30 June	30 June	30 June	31 March	30 June
	2012	2011	2012	2012	2011
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Operating profit	7,628,973	6,170,402	3,937,615	3,691,358	2,783,899
Less: Interest income	(363,539)	(207,208)	(196,806)	(166,733)	(106,546)
Add: Other losses/(gains), net	66,861	(341,878)	3,219	63,642	(2,809)
Add: Depreciation of fixed assets and investment properties	869,000	494,844	444,830	424,170	274,113
Add: Amortisation of intangible assets	384,574	275,861	142,464	242,110	222,651
EBITDA	8,585,869	6,392,021	4,331,322	4,254,547	3,171,308
Equity-settled share-based compensation	434,303	334,452	227,641	206,662	190,329
Adjusted EBITDA	9,020,172	6,726,473	4,558,963	4,461,209	3,361,637

NON-GAAP FINANCIAL MEASURES

To supplement the consolidated results of the Group prepared in accordance with IFRS, certain non-GAAP financial measures, including non-GAAP operating profit, non-GAAP operating margin, non-GAAP profit for the period, non-GAAP net margin and non-GAAP profit attributable to equity holders of the Company, have been presented in this interim report. These unaudited non-GAAP financial measures should be considered in addition to, not as a substitute for, measures of the Company's financial performance prepared in accordance with IFRS. In addition, these non-GAAP financial measures may be defined differently from similar terms used by other companies.

Management Discussion and Analysis

The Company's management believes that the non-GAAP financial measures provide investors with useful supplementary information to assess the performance of the Group's core operations by excluding certain non-cash items and certain impact of acquisitions. The following tables set forth the reconciliations of the Company's non-GAAP financial measures for the first half of 2012 and 2011, the second quarter of 2012 and 2011, and the first quarter of 2012 to the nearest measures prepared in accordance with IFRS:

	Unaudited six months ended 30 June 2012								
	As reported	Adjustments				Non-GAAP			
		Equity-settled share-based compensation	Cash-settled share-based compensation	Gain on deemed disposal	Amortisation of intangible assets				
							(a)	(b)	(c)
							(RMB in thousands, unless specified)		
Operating profit	7,628,973	434,303	57,975	–	168,511	8,289,762			
Profit for the period	6,072,901	434,303	57,975	–	155,752	6,720,931			
Profit attributable to equity holders of the Company	6,049,585	425,609	51,130	–	141,006	6,667,330			
Operating margin	37.8%					41.1%			
Net margin	30.1%					33.3%			

	Unaudited six months ended 30 June 2011								
	As reported	Adjustments				Non-GAAP			
		Equity-settled share-based compensation	Cash-settled share-based compensation	Gain on deemed disposal	Amortisation of intangible assets				
							(a)	(b)	(c)
							(RMB in thousands, unless specified)		
Operating profit	6,170,402	334,452	33,537	(459,037)	238,445	6,317,799			
Profit for the period	5,227,480	334,452	33,537	(459,037)	159,669	5,296,101			
Profit attributable to equity holders of the Company	5,219,620	330,373	31,053	(459,037)	149,468	5,271,477			
Operating margin	47.2%					48.3%			
Net margin	40.0%					40.5%			

Management Discussion and Analysis

Unaudited three months ended 30 June 2011						
	As reported	Adjustments			Non-GAAP	
		Equity-settled share-based compensation	Cash-settled share-based compensation (a)	Gain on deemed disposal (b)		Amortisation of intangible assets (c)
<i>(RMB in thousands, unless specified)</i>						
Operating profit	2,783,899	190,329	24,446	–	199,215	3,197,889
Profit for the period	2,343,272	190,329	24,446	–	136,440	2,694,487
Profit attributable to equity holders of the Company	2,349,246	187,252	22,618	–	127,641	2,686,757
Operating margin	41.3%					47.5%
Net margin	34.8%					40.0%

Note:

- (a) Including put options granted to employees of investees on their shares and shares to be issued under investees' share-based incentive plans which can be acquired by the Group, and other incentives
- (b) Gain on deemed disposal of previously held interest in associates
- (c) Amortisation of intangible assets resulting from acquisitions, net of related deferred tax

Management Discussion and Analysis

LIQUIDITY AND FINANCIAL RESOURCES

Our net cash positions as at 30 June 2012 and 31 March 2012 are as follows:

	Unaudited 30 June 2012 RMB'000	Unaudited 31 March 2012 RMB'000
Cash and cash equivalents	10,602,451	13,348,679
Term deposits with initial term of over three months	17,014,730	15,909,027
Restricted cash pledged for secured bank borrowings	324,347	968,675
	27,941,528	30,226,381
Long-term notes payable	(3,751,839)	(3,731,549)
Long-term borrowings	(948,735)	–
Short-term borrowings	(3,609,323)	(5,676,325)
Net cash	19,631,631	20,818,507

As at 30 June 2012, RMB5,343 million of our financial resources (31 March 2012: RMB6,020 million) were held in deposits and investments denominated in non-RMB currencies. Since there are no cost-effective hedges against the fluctuation of RMB and no effective manner to generally convert a significant amount of non-RMB currencies into RMB, which is not a freely exchangeable currency, there is a risk that we may experience a loss as a result of any foreign currency exchange rate fluctuations in connection with our deposits and investments.

Report on Review of Interim Financial Information

TO THE BOARD OF DIRECTORS OF TENCENT HOLDINGS LIMITED

(Incorporated in the Cayman Islands with limited liability)

INTRODUCTION

We have reviewed the interim financial information set out on pages 22 to 59, which comprises the consolidated statement of financial position of Tencent Holdings Limited (the “Company”) and its subsidiaries (together, the “Group”) as at 30 June 2012 and the related consolidated income statement, the consolidated statement of comprehensive income for the three and six months then ended, the consolidated statement of changes in equity and the condensed consolidated statement of cash flows for the six months then ended, and a summary of significant accounting policies and other explanatory notes (collectively defined as the “Interim Financial Information”). The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and International Accounting Standard 34 ‘Interim Financial Reporting’. The directors of the Company are responsible for the preparation and presentation of this interim financial information in accordance with International Accounting Standard 34 ‘Interim Financial Reporting’. Our responsibility is to express a conclusion on this Interim Financial Information based on our review and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

SCOPE OF REVIEW

We conducted our review in accordance with International Standard on Review Engagement 2410 ‘Review of interim financial information performed by the independent auditor of the entity’. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

CONCLUSION

Based on our review, nothing has come to our attention that causes us to believe that the Interim Financial Information is not properly prepared, in all material respects, in accordance with International Accounting Standard 34 ‘Interim Financial Reporting’.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 15 August 2012

Consolidated Statement of Financial Position

As at 30 June 2012

	Note	Unaudited 30 June 2012 RMB'000	Audited 31 December 2011 RMB'000
ASSETS			
Non-current assets			
Fixed assets	7	6,201,179	5,884,952
Construction in progress	7	323,786	158,656
Investment properties	7	21,643	21,871
Land use rights	7	348,509	230,915
Intangible assets	7	4,194,417	3,779,976
Interests in associates	8	5,292,559	4,338,075
Investment in jointly controlled entities		53,908	61,903
Deferred income tax assets	19	184,608	198,058
Available-for-sale financial assets	9	5,320,869	4,343,602
Prepayments, deposits and other assets	11	3,877,451	2,282,869
		25,818,929	21,300,877
Current assets			
Inventories		202,106	–
Accounts receivable	10	2,500,207	2,020,796
Prepayments, deposits and other assets	11	3,275,968	2,211,917
Term deposits with initial term of over three months		17,014,730	13,716,040
Restricted cash		2,317,431	4,942,595
Cash and cash equivalents		10,602,451	12,612,140
		35,912,893	35,503,488
Total assets		61,731,822	56,804,365
EQUITY			
Equity attributable to the Company's equity holders			
Share capital	12	198	198
Share premium	12	2,488,779	2,058,051
Shares held for share award scheme	12	(609,657)	(606,874)
Other reserves		532,264	302,091
Retained earnings		31,652,090	26,710,368
		34,063,674	28,463,834
Non-controlling interests		650,698	624,510
Total equity		34,714,372	29,088,344

Consolidated Statement of Financial Position

As at 30 June 2012

	Note	Unaudited 30 June 2012 RMB'000	Audited 31 December 2011 RMB'000
LIABILITIES			
Non-current liabilities			
Borrowings	17	948,735	–
Long-term notes payable	18	3,751,839	3,733,331
Deferred income tax liabilities	19	893,822	939,534
Long-term payables	16	1,441,920	1,859,808
		<u>7,036,316</u>	<u>6,532,673</u>
Current liabilities			
Accounts payable	14	3,368,438	2,244,114
Other payables and accruals	15	4,872,613	5,014,281
Derivative financial instruments		14,680	20,993
Borrowings	17	3,609,323	7,999,440
Current income tax liabilities		998,523	708,725
Other tax liabilities		256,781	179,499
Deferred revenue		6,860,776	5,016,296
		<u>19,981,134</u>	<u>21,183,348</u>
Total liabilities		<u>27,017,450</u>	<u>27,716,021</u>
Total equity and liabilities		<u>61,731,822</u>	<u>56,804,365</u>
Net current assets		<u>15,931,759</u>	<u>14,320,140</u>
Total assets less current liabilities		<u>41,750,688</u>	<u>35,621,017</u>

The accompanying notes on pages 29 to 59 form an integral part of this Interim Financial Information.

On behalf of the Board

Ma Huateng
Director

Zhang Zhidong
Director

Consolidated Income Statement

For the three and six months ended 30 June 2012

	Note	Unaudited		Unaudited	
		Three months ended 30 June		Six months ended 30 June	
		2012 RMB'000	2011 RMB'000	2012 RMB'000	2011 RMB'000
Revenues					
Internet value-added services		7,786,625	5,386,578	15,168,246	10,637,860
Mobile and telecommunications value-added services		929,007	793,839	1,842,849	1,571,631
Online advertising		879,691	512,312	1,419,804	793,206
e-Commerce transactions		857,526	–	1,610,343	–
Others		74,395	46,315	133,860	74,767
		10,527,244	6,739,044	20,175,102	13,077,464
Cost of revenues	21	(4,311,379)	(2,331,637)	(8,147,696)	(4,525,366)
Gross profit		6,215,865	4,407,407	12,027,406	8,552,098
Interest income		196,806	106,546	363,539	207,208
Other (losses)/gains, net	20	(3,219)	2,809	(66,861)	341,878
Selling and marketing expenses	21	(609,672)	(369,491)	(1,078,872)	(669,944)
General and administrative expenses	21	(1,862,165)	(1,363,372)	(3,616,239)	(2,260,838)
Operating profit		3,937,615	2,783,899	7,628,973	6,170,402
Finance (costs)/income, net	22	(115,256)	1,771	(185,238)	(2,098)
Share of profit/(losses) of associates	8	5,411	23,454	(4,342)	61,308
Share of losses of jointly controlled entities		(9,375)	(60,689)	(7,995)	(64,986)
Profit before income tax		3,818,395	2,748,435	7,431,398	6,164,626
Income tax expense	23	(707,824)	(405,163)	(1,358,497)	(937,146)
Profit for the period		3,110,571	2,343,272	6,072,901	5,227,480
Attributable to:					
Equity holders of the Company		3,100,075	2,349,246	6,049,585	5,219,620
Non-controlling interests		10,496	(5,974)	23,316	7,860
		3,110,571	2,343,272	6,072,901	5,227,480
Earnings per share for profit attributable to equity holders of the Company (expressed in RMB per share)					
– basic	24	1.698	1.289	3.316	2.863
– diluted	24	1.665	1.260	3.252	2.800

The accompanying notes on pages 29 to 59 form an integral part of this Interim Financial Information.

Consolidated Statement of Comprehensive Income

For the three and six months ended 30 June 2012

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2012	2011	2012	2011
	RMB'000	RMB'000	RMB'000	RMB'000
Profit for the period	3,110,571	2,343,272	6,072,901	5,227,480
Other comprehensive income, net of tax:				
Net (losses)/gains from changes in fair value of available-for-sale financial assets	(530,203)	264,280	758,711	(418,156)
Currency translation differences	7,743	(74)	13,819	133
	(522,460)	264,206	772,530	(418,023)
Total comprehensive income for the period	2,588,111	2,607,478	6,845,431	4,809,457
Attributable to:				
Equity holders of the Company	2,576,886	2,613,452	6,821,375	4,801,597
Non-controlling interests	11,225	(5,974)	24,056	7,860
	2,588,111	2,607,478	6,845,431	4,809,457

The accompanying notes on pages 29 to 59 form an integral part of this Interim Financial Information.

Consolidated Statement of Changes in Equity

For the six months ended 30 June 2012

	Unaudited							Total equity RMB'000
	Attributable to equity holders of the Company							
	Share capital RMB'000	Share premium RMB'000	Shares held for share award scheme RMB'000	Other reserves RMB'000	Retained earnings RMB'000	Total RMB'000	Non- controlling interests RMB'000	
Balance at 1 January 2012	198	2,058,051	(606,874)	302,091	26,710,368	28,463,834	624,510	29,088,344
Comprehensive income								
Profit for the period	-	-	-	-	6,049,585	6,049,585	23,316	6,072,901
Other comprehensive income:								
- net gains from changes in fair value of available-for-sale financial assets	-	-	-	758,711	-	758,711	-	758,711
- currency translation differences	-	-	-	13,079	-	13,079	740	13,819
Total comprehensive income for the period	-	-	-	771,790	6,049,585	6,821,375	24,056	6,845,431
Transaction with owners								
Capital injection	-	-	-	-	-	-	7,220	7,220
Employee share option schemes:								
- value of employee services	-	55,669	-	34,432	-	90,101	18,182	108,283
- proceeds from shares issued	-	113,640	-	-	-	113,640	-	113,640
Employee share award scheme:								
- value of employee services	-	295,814	-	25,792	-	321,606	4,415	326,021
- shares purchased for share award scheme	-	-	(16,946)	-	-	(16,946)	-	(16,946)
- vesting of awarded shares	-	(14,163)	14,163	-	-	-	-	-
Profit appropriations to statutory reserves	-	-	-	(26)	26	-	-	-
Repurchase and cancellation of shares	-	(20,232)	-	-	-	(20,232)	-	(20,232)
Dividend (Note 25)	-	-	-	-	(1,107,889)	(1,107,889)	(18,180)	(1,126,069)
Total contributions by and distributions to owners for the period	-	430,728	(2,783)	60,198	(1,107,863)	(619,720)	11,637	(608,083)
Non-controlling interests arising from business combinations (Note 26)	-	-	-	-	-	-	(2,455)	(2,455)
Acquisition of additional equity interests in non-wholly owned subsidiaries	-	-	-	(244,197)	-	(244,197)	(7,050)	(251,247)
Recognition of financial liabilities in respect of the put options granted to non-controlling interests	-	-	-	(357,618)	-	(357,618)	-	(357,618)
Total transactions with owners for the period	-	430,728	(2,783)	(541,617)	(1,107,863)	(1,221,535)	2,132	(1,219,403)
Balance at 30 June 2012	198	2,488,779	(609,657)	532,264	31,652,090	34,063,674	650,698	34,714,372

The accompanying notes on pages 29 to 59 form an integral part of this Interim Financial Information.

Consolidated Statement of Changes in Equity

For the six months ended 30 June 2012

	Unaudited							
	Attributable to equity holders of the Company							
	Share capital RMB'000	Share premium RMB'000	Shares held for share award scheme RMB'000	Other reserves RMB'000	Retained earnings RMB'000	Total RMB'000	Non- controlling interests RMB'000	Total equity RMB'000
Balance at 1 January 2011	198	2,299,965	(258,137)	1,919,695	17,795,225	21,756,946	83,912	21,840,858
Comprehensive income								
Profit for the period	-	-	-	-	5,219,620	5,219,620	7,860	5,227,480
Other comprehensive income:								
- net losses from changes in fair value of available-for-sale financial assets	-	-	-	(418,156)	-	(418,156)	-	(418,156)
- currency translation differences	-	-	-	133	-	133	-	133
Total comprehensive income for the period	-	-	-	(418,023)	5,219,620	4,801,597	7,860	4,809,457
Transaction with owners								
Employee share option schemes:								
- value of employee services	-	93,102	-	-	-	93,102	-	93,102
- proceeds from shares issued	-	80,689	-	-	-	80,689	-	80,689
Employee share award scheme:								
- value of employee services	-	242,477	-	-	-	242,477	-	242,477
- shares purchased for share award scheme	-	-	(247,777)	-	-	(247,777)	-	(247,777)
- vesting of awarded shares	-	(29,574)	29,574	-	-	-	-	-
Repurchase and cancellation of shares	-	(97,586)	-	-	-	(97,586)	-	(97,586)
Dividends (Note 25)	-	-	-	-	(838,290)	(838,290)	(56,531)	(894,821)
Transfer to reserve	-	-	-	10,000	(10,000)	-	-	-
Total contributions by and distributions to owners for the period	-	289,108	(218,203)	10,000	(848,290)	(767,385)	(56,531)	(823,916)
Non-controlling interests arising from business combinations	-	-	-	-	-	-	187,092	187,092
Recognition of the financial liabilities in respect of the put option granted to non-controlling interests	-	-	-	(670,985)	-	(670,985)	-	(670,985)
Total transactions with owners for the period	-	289,108	(218,203)	(660,985)	(848,290)	(1,438,370)	130,561	(1,307,809)
Balance at 30 June 2011	198	2,589,073	(476,340)	840,687	22,166,555	25,120,173	222,333	25,342,506

The accompanying notes on pages 29 to 59 form an integral part of this Interim Financial Information.

Condensed Consolidated Statement of Cash Flows

For the six months ended 30 June 2012

	Unaudited	
	Six months ended	
	30 June	
	2012	2011
	RMB'000	RMB'000
Net cash flows generated from operating activities	8,945,857	5,434,115
Net cash flows used in investing activities	(6,455,778)	(9,547,558)
Net cash flows (used in)/generated from financing activities	(4,506,408)	1,741,476
Net decrease in cash and cash equivalents	(2,016,329)	(2,371,967)
Cash and cash equivalents at beginning of period	12,612,140	10,408,257
Exchange gains/(losses) on cash and cash equivalents	6,640	(73,200)
Cash and cash equivalents at end of period	10,602,451	7,963,090
Analysis of balances of cash and cash equivalents:		
Bank balances and cash	6,699,446	6,381,618
Term deposits and highly liquid investments with initial term within three months	3,903,005	1,581,472
	10,602,451	7,963,090

The accompanying notes on pages 29 to 59 form an integral part of this Interim Financial Information.

Notes to the Interim Financial Information

1 GENERAL INFORMATION

Tencent Holdings Limited (the “Company”) was incorporated in the Cayman Islands. The address of its registered office is Cricket Square, Hutchins Drive, P.O. Box 2681, Grand Cayman KY 1-1111, Cayman Islands. The shares of the Company have been listed on the Main Board of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) since 16 June 2004.

The Company is an investment holding company. The Company and its subsidiaries (collectively, the “Group”) are principally engaged in the provision of Internet value-added services (“IVAS”), mobile and telecommunications value-added services (“MVAS”), online advertising services and e-Commerce transactions services to users in the People’s Republic of China (the “PRC”).

The consolidated statement of financial position as at 30 June 2012, the related consolidated income statement and the consolidated statement of comprehensive income for the three and six months then ended, the consolidated statement of changes in equity and the condensed consolidated statement of cash flows for the six months then ended, and a summary of significant accounting policies and other explanatory notes (collectively defined as the “Interim Financial Information”) of the Group have been approved by the Board on 15 August 2012.

This Interim Financial Information has not been audited.

2 BASIS OF PREPARATION AND PRESENTATION

The Interim Financial Information is prepared in accordance with International Accounting Standards (“IAS”) 34 ‘Interim Financial Reporting’ issued by the International Accounting Standards Board.

The Interim Financial Information should be read in conjunction with the annual consolidated financial statements of the Group for the year ended 31 December 2011 as set out in the 2011 annual report of the Company dated 14 March 2012 (the “2011 Financial Statements”).

3 SIGNIFICANT ACCOUNTING POLICIES

Except as described below, the accounting policies and method of computation used in the preparation of the Interim Financial Information are consistent with those used in the 2011 Financial Statements, which have been prepared in accordance with International Financial Reporting Standards (“IFRS”) under the historical cost convention, as modified by the revaluation of available-for-sale financial assets and derivative financial instruments.

Taxes on income for the interim period are accrued using the tax rates that would be applicable to expected total annual assessable profits.

The new or revised standards and amendments to the existing standards, which are mandatory for the financial year of the Company beginning 1 January 2012, are either not currently relevant or have no impact on the Group’s Interim Financial Information.

Because of the growth in related business during the six months ended 30 June 2012, the Group disclosed the following accounting policies in this Interim Financial Information, which were not included in the principal accounting policies in the 2011 Financial Statements:

Notes to the Interim Financial Information

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

(a) Revenue recognition in third-party developed games/applications hosted by the developers

In 2012, the Group entered into cooperation agreements with third-party game/application developers, pursuant to which the games/applications designed, developed and hosted by third-party developers are available to the users on the Group's Internet platforms. The respective third-party game/application developers are responsible for the users' experiences. Under the terms of the cooperation agreements, the Group pays the third-party developers a stated percentage of the fees paid by and collected from end users for the virtual products/items utilised in these games/applications. The Group recognises revenue at the net amount it retains because the Group acts as an agent in the arrangement.

The Group issues prepaid cards and tokens (represent a specific amount of payment unit) through various channels to end users of the games/applications. The end users can register these prepaid cards and tokens to their user accounts on the Group's Internet platforms and then gain access to the respective games/applications hosted by the third-party developers. The users can use the Group's prepaid cards and tokens to purchase virtual products/items in the games/applications. The Group defers the related revenue over an estimated period of the respective products/items as there is an implicit obligation of the Group to maintain and allow access of the users of the games/applications through its platforms.

Revenue derived from games/applications hosted by third-party developers on the Group's Internet platforms is presented within revenues from IVAS.

(b) Revenue recognition in relation to e-Commerce transactions business

e-Commerce transactions revenues are primarily derived from sales of merchandise through the Group's Internet platforms. The Group recognises revenues from merchandise sales and related costs on a gross basis when it acts as a principal. Whether the Group acts as a principal is based on several criteria, including whether it is a primary obligor, whether it is subject to inventory risk, whether it has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, in a transaction. When the Group is not a principal and is instead acting as an agent, revenues are recognised on a net basis based on a pre-determined percentage.

For merchandise sold under e-Commerce transactions, the customers place their orders online with a commitment made at a fixed selling price. Payment for the purchased merchandise is made either before delivery or upon delivery. When the Group is acting as a principal, revenues, net of discounts and return allowances and value-added tax, are recognised when the merchandise is physically delivered to the respective customers. Return allowances, which reduce the gross amount of revenues, are estimated based on historical experience.

Notes to the Interim Financial Information

4 ESTIMATES

The preparation of the Interim Financial Information requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

In preparing the Interim Financial Information, the significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those applied to the 2011 Financial Statements.

5 FINANCIAL RISK MANAGEMENT

(a) Financial risk factors

The Group is subject to a variety of financial risks: market risk (including foreign exchange risk, price risk and interest rate risk), credit risk and liquidity risk.

The Interim Financial Information does not include all financial risk management information and disclosures required in the annual financial statements, and should be read in conjunction with the 2011 Financial Statements.

There were no changes in any risk management policies during the six months ended 30 June 2012.

(b) Foreign exchange risk

Listed below are the Group's major non-RMB monetary assets and liabilities as at 30 June 2012, which are exposed to foreign exchange risk:

	Denomination currency	Unaudited 30 June 2012 RMB'000	Audited 31 December 2011 RMB'000
Monetary assets			
Current assets	USD	5,245,878	5,645,223
Current assets	HKD	274,086	304,835
Current assets	EUR	259,706	194,705
Monetary liabilities			
Non-current liabilities	USD	5,722,494	5,529,637
Current liabilities	USD	3,789,364	6,600,412
Current liabilities	HKD	38,329	52,086

During the three and six months ended 30 June 2012, the Group reported exchange losses of RMB45,912,000 and RMB48,316,000, respectively (for the three and six months ended 30 June 2011: exchange gains of RMB14,903,000 and RMB27,719,000, respectively) (Note 22). The losses were recorded in "Finance (costs)/income, net" in the consolidated income statements for the three and six months ended 30 June 2012.

Notes to the Interim Financial Information

5 FINANCIAL RISK MANAGEMENT (continued)

(c) Capital risk management

The Group monitors capital by regularly reviewing the gearing ratio. The gearing ratio is calculated as total liabilities divided by total assets. The total capital is the “total equity” of the Group as shown in the consolidated statement of financial position, which is also equal to total assets less total liabilities.

As at 30 June 2012, the gearing ratio of the Group was 44% (31 December 2011: 49%).

(d) Fair value estimation

The Group’s main financial instruments carried at fair value are available-for-sale financial assets and derivative financial instruments, and the valuation method is the same as that applied in the 2011 Financial Statements.

During the three and six months ended 30 June 2012, the Group reported a net loss (net of tax) of RMB530,203,000 and a net gain (net of tax) of RMB758,711,000 respectively, for available-for-sale financial assets in other comprehensive income, which mainly resulted from the change in fair value of available-for-sale financial assets which have quoted prices (unadjusted) in active markets.

There were no reclassifications of financial assets during the three and six months ended 30 June 2011 and 2012.

6 SEGMENT INFORMATION

The chief operating decision-makers mainly include the executive directors of the Company. They review the Group’s internal reports in order to determine the operating segments, assess performance and allocate resources based on these reports.

During the three and six months ended 30 June 2012, the scale of e-Commerce transactions business of the Group increased significantly and the executive directors of the Company treated e-Commerce transactions business as a separate segment of the Group’s operations. As a result, a new line of segment information has been presented since 1 January 2012. No comparative figures of the comparative quarters of 2011 is presented since the amounts involved were insignificant.

The Group has the following reportable segments for the three and six months ended 30 June 2012:

- IVAS;
- MVAS;
- Online advertising;
- e-Commerce transactions; and
- Others.

Other segments of the Group are mainly comprised of the provision of trademark licensing, software development services and software sales.

Notes to the Interim Financial Information

6 SEGMENT INFORMATION (continued)

The chief operating decision-makers assess the performance of the operating segments mainly based on segment revenue and gross profit/(losses) of each operating segment. The selling and marketing expenses and general and administrative expenses are common costs incurred for the operating segments as a whole and, therefore, they are not included in the measure of the segments' performance which is used by the chief operating decision-makers as a basis for the purpose of resource allocation and assessment of segment performance. Interest income, other (losses)/gains, net, finance (costs)/income, net and income tax expense are not allocated to individual operating segment either.

There were no material inter-segment sales during the three and six months ended 30 June 2012 and 2011. The revenues from external customers reported to the chief operating decision-makers are measured in a manner consistent with that applied in the consolidated income statement.

Other information, together with the segment information, provided to the chief operating decision-makers, is measured in a manner consistent with that applied in the Interim Financial Information. There were no segment assets and segment liabilities information provided to the chief operating decision-makers.

The segment information provided to the chief operating decision-makers for the reportable segments for the three and six months ended 30 June 2012 and 2011 is as follows:

	Unaudited					Total RMB'000
	Three months ended 30 June 2012					
	IVAS RMB'000	MVAS RMB'000	Online advertising RMB'000	e-Commerce transactions RMB'000	Others RMB'000	
Segment revenues	<u>7,786,625</u>	<u>929,007</u>	<u>879,691</u>	<u>857,526</u>	<u>74,395</u>	<u>10,527,244</u>
Gross profit	<u>5,141,251</u>	<u>570,072</u>	<u>458,403</u>	<u>21,521</u>	<u>24,618</u>	<u>6,215,865</u>
Depreciation	263,625	26,350	24,899	1,940	4,397	321,211
Amortisation	48,315	–	44,756	–	–	93,071
Share of profit/(losses) of associates	7,358	527	–	(8,338)	5,864	5,411
Share of losses of jointly controlled entities	<u>(9,375)</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>(9,375)</u>

Notes to the Interim Financial Information

6 SEGMENT INFORMATION (continued)

	Unaudited				
	Three months ended 30 June 2011				
	IVAS	MVAS	Online advertising	Others	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Segment revenues	<u>5,386,578</u>	<u>793,839</u>	<u>512,312</u>	<u>46,315</u>	<u>6,739,044</u>
Gross profit/(losses)	<u>3,598,338</u>	<u>471,385</u>	<u>343,688</u>	<u>(6,004)</u>	<u>4,407,407</u>
Depreciation	166,973	14,134	13,487	7,559	202,153
Amortisation	10,585	–	–	–	10,585
Share of profit/(losses) of associates	25,158	(1,704)	–	–	23,454
Share of losses of jointly controlled entities	<u>(60,689)</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>(60,689)</u>

	Unaudited					
	Six months ended 30 June 2012					
	IVAS	MVAS	Online advertising	e-Commerce transactions	Others	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Segment revenues	<u>15,168,246</u>	<u>1,842,849</u>	<u>1,419,804</u>	<u>1,610,343</u>	<u>133,860</u>	<u>20,175,102</u>
Gross profit	<u>10,114,049</u>	<u>1,145,075</u>	<u>682,333</u>	<u>42,287</u>	<u>43,662</u>	<u>12,027,406</u>
Depreciation	511,545	52,124	48,633	3,697	8,680	624,679
Amortisation	90,206	–	85,577	–	–	175,783
Share of profit/(losses) of associates	6,698	(4,128)	–	(20,100)	13,188	(4,342)
Share of losses of jointly controlled entities	<u>(7,995)</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>(7,995)</u>

Notes to the Interim Financial Information

6 SEGMENT INFORMATION (continued)

	Unaudited				
	Six months ended 30 June 2011				
	IVAS	MVAS	Online advertising	Others	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Segment revenues	<u>10,637,860</u>	<u>1,571,631</u>	<u>793,206</u>	<u>74,767</u>	<u>13,077,464</u>
Gross profit/(losses)	<u>7,107,472</u>	<u>951,677</u>	<u>506,478</u>	<u>(13,529)</u>	<u>8,552,098</u>
Depreciation	300,905	25,312	24,106	12,008	362,331
Amortisation	13,597	–	–	–	13,597
Share of profit/(losses) of associates	62,300	(992)	–	–	61,308
Share of losses of jointly controlled entities	<u>(64,986)</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>(64,986)</u>

The reconciliation of gross profit to profit before tax is shown in the consolidated income statement.

The Company is domiciled in the Cayman Islands while the Group mainly operates its businesses in the PRC. Revenues derived from external customers in mainland China for the three and six months ended 30 June 2012 were RMB10,097,850,000 and RMB19,391,349,000, respectively (for the three and six months ended 30 June 2011: RMB6,706,925,000 and RMB12,996,547,000, respectively), and revenues derived from external customers in other regions were RMB429,394,000 and RMB783,753,000, respectively (for the three and six months ended 30 June 2011: RMB32,119,000 and RMB80,917,000, respectively).

As at 30 June 2012, the total non-current assets, excluding financial instruments and deferred income tax assets, located in mainland China and other regions were RMB16,738,557,000 and RMB3,574,895,000, respectively (31 December 2011: RMB13,620,472,000 and RMB3,138,745,000, respectively).

Revenues derived from any single external customer were less than 10% of the Group's total revenues for the three and six months ended 30 June 2012.

Notes to the Interim Financial Information

7 FIXED ASSETS, CONSTRUCTION IN PROGRESS, INVESTMENT PROPERTIES, LAND USE RIGHTS AND INTANGIBLE ASSETS

		Unaudited			
	Fixed assets	Construction in progress	Investment properties	Land use rights	Intangible assets
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Net book amount at 1 January 2011	3,292,828	386,943	37,229	229,890	572,981
Business combinations	14,781	–	–	–	2,644,502
Other additions	1,380,752	198,149	–	–	539,376
Transfers	472,126	(457,297)	(14,829)	–	–
Disposals	(317)	–	–	–	–
Depreciation/amortisation	(494,544)	–	(300)	(2,358)	(275,861)
Net book amount at 30 June 2011	<u>4,665,626</u>	<u>127,795</u>	<u>22,100</u>	<u>227,532</u>	<u>3,480,998</u>
Net book amount at 1 January 2012	5,884,952	158,656	21,871	230,915	3,779,976
Business combinations	503	–	–	–	84,906
Other additions	1,041,695	315,119	–	120,760	706,834
Transfers	149,989	(149,989)	–	–	–
Disposals	(1,298)	–	–	–	–
Depreciation/amortisation	(868,772)	–	(228)	(3,166)	(384,574)
Exchange difference	(5,890)	–	–	–	7,275
Net book amount at 30 June 2012	<u>6,201,179</u>	<u>323,786</u>	<u>21,643</u>	<u>348,509</u>	<u>4,194,417</u>

Non-financial assets that have an indefinite life are not subject to amortisation, but are tested for impairment annually at year-end (31 December) or whenever there is any indication of impairment. Non-financial assets that are subject to amortisation and depreciation are reviewed for impairment whenever events or changes in circumstance indicate that the carrying amount may not be recoverable.

There was no indication of impairment for fixed assets, construction in progress, investment properties, land use rights and intangible assets during the three and six months ended 30 June 2012.

Notes to the Interim Financial Information

8 INTERESTS IN ASSOCIATES

	Unaudited	
	Six months ended	
	30 June	
	2012	2011
	RMB'000	RMB'000
At beginning of period	4,338,075	1,070,633
Additions ((a), (b) and (c))	1,017,698	1,789,296
Transfer from available-for-sale financial assets	31,139	–
Transfer out as a result of step-up business combination	–	(117,502)
Share of (losses)/profit of associates	(4,342)	61,308
Dividends received from associates	(21,748)	(20,000)
Disposal of an associate	(68,263)	–
	5,292,559	2,783,735
At end of period	5,292,559	2,783,735

Note:

- (a) On 31 January 2012, the Group acquired 619,400,000 ordinary shares of ChinaVision Media Group Limited (“ChinaVision”), representing approximately 8% of its total outstanding shares, for a cash consideration of HKD247,760,000. ChinaVision is a company listed on the Main Board of the Stock Exchange, and principally engaged in production and licensing of film and television programmes, and printed media and television advertising businesses. Since the Group has the right to nominate a director to the board of ChinaVision, the investment in ChinaVision is accounted for as an investment in associate of the Group.
- (b) In April 2012, the Group acquired 3,600,000 preference shares of Kakao Corp. (“Kakao”), a company principally engaged in developing and operating mobile chat applications, representing approximately 13.84% of its issued share capital, for a cash consideration of KRW72,000,000,000. Since the Group has significant influence in Kakao through its representative of the board, the investment in Kakao is accounted for as an investment in associate of the Group.
- (c) In addition to the above, the Group acquired some other associates for an aggregate consideration of RMB221,843,000 during the six months ended 30 June 2012. They are principally engaged in online community service, online game development and other Internet related businesses. The Group also made additional investments in existing investees for an aggregate consideration of RMB193,224,000 during the six months ended 30 June 2012. They are principally engaged in game development.

As at 30 June 2012 and 2011, there were certain call or conversion options embedded in interests in associates. The directors of the Company considered that the fair values of such options were insignificant and accordingly, the Group did not separately recognise these options in the Interim Financial Information.

Notes to the Interim Financial Information

9 AVAILABLE-FOR-SALE FINANCIAL ASSETS

	Unaudited	
	Six months ended	
	30 June	
	2012	2011
	RMB'000	RMB'000
At beginning of period	4,343,602	4,126,878
Additions	252,063	953,535
Transfer to interests in associates	(31,139)	–
Gains/(losses) from changes in fair value	756,343	(424,846)
	5,320,869	4,655,567
At end of period	5,320,869	4,655,567
Market value of listed securities	4,075,137	3,889,122

As at 30 June 2012, there were certain call or conversion options embedded in available-for-sale financial assets. The directors of the Company considered that the fair values of such options were insignificant and accordingly, the Group did not separately recognise these options in the Interim Financial Information.

10 ACCOUNTS RECEIVABLE

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
0 - 30 days	1,502,110	1,103,261
31 - 60 days	363,831	443,555
61 - 90 days	324,424	246,501
Over 90 days	309,842	227,479
	2,500,207	2,020,796

Accounts receivable was mainly denominated in RMB.

Receivable balances as at 30 June 2012 mainly represented amounts due from telecommunication operators, including China Mobile Communications Corporation, China United Telecommunications Co. Ltd., China Telecommunications Corporation and their respective branches, subsidiaries and affiliates, as well as online advertising customers mainly located in the PRC.

Notes to the Interim Financial Information

10 ACCOUNTS RECEIVABLE (continued)

While there are no contractual requirements for the telecommunication operators to pay amounts owed to the Group within a specified period of time, they usually settle the amounts due by them within a period of 30 to 120 days. Online advertising customers, which are mainly advertising agencies, are usually granted a credit period of 90 days after full execution of the contracted advertisement orders.

The directors of the Company considered that the carrying amounts of the receivable balances approximated to their fair value as at 30 June 2012.

11 PREPAYMENTS, DEPOSITS AND OTHER ASSETS

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Included in non-current assets:		
Prepayment for interests in associates	2,118,925	–
Prepayment for purchase of buildings	743,379	510,425
Prepayment for online game licences	423,764	350,668
Prepayment for land use rights	258,237	258,237
Loans to associates and jointly controlled entities	184,133	111,063
Non-current portion of running royalty fees for online games	132,103	945,135
Prepaid expenses	16,910	107,341
	3,877,451	2,282,869
Included in current assets:		
Current portion of running royalty fees for online games	1,527,516	405,915
Prepaid expenses	575,694	483,592
Interest receivables	249,858	143,370
Refundable value-added tax	280,322	270,028
Rental deposits and other deposits	117,288	112,714
Loans to associates	36,075	6,052
Others	489,215	790,246
	3,275,968	2,211,917
	7,153,419	4,494,786

Notes to the Interim Financial Information

11 PREPAYMENTS, DEPOSITS AND OTHER ASSETS (continued)

The directors of the Company considered that the carrying amounts of the prepayments, deposits and other assets approximated to their fair values as at 30 June 2012.

Prepayments, deposits and other assets were neither past due nor impaired. Their recoverability was assessed with reference made to the credit status of the respective recipients.

12 SHARE CAPITAL, SHARE PREMIUM AND SHARES HELD FOR SHARE AWARD SCHEME

As at 30 June 2012, the total authorised number of ordinary shares is 10,000,000,000 shares (31 December 2011: 10,000,000,000 shares) with par value of HKD0.0001 per share (31 December 2011: HKD0.0001 per share).

As at 30 June 2012, all issued shares were fully paid.

	Unaudited				Total RMB'000
	Number of ordinary shares	Share capital RMB'000	Share premium RMB'000	Shares held for share award scheme RMB'000	
At 1 January 2012	1,839,814,008	198	2,058,051	(606,874)	1,451,375
Employee share option schemes:					
Value of employee services	–	–	55,669	–	55,669
Number of shares issued and proceeds received	4,430,528	–	113,640	–	113,640
Employee share award scheme:					
Value of employee services	–	–	295,814	–	295,814
Shares purchased and withheld for share award scheme	–	–	–	(16,946)	(16,946)
Shares vested from share award scheme and transferred to the grantees	–	–	(14,163)	14,163	–
Repurchase and cancellation of shares	(154,400)	–	(20,232)	–	(20,232)
At 30 June 2012	1,844,090,136	198	2,488,779	(609,657)	1,879,320

Notes to the Interim Financial Information

12 SHARE CAPITAL, SHARE PREMIUM AND SHARES HELD FOR SHARE AWARD SCHEME (continued)

	Unaudited				
	Number of ordinary shares	Share capital RMB'000	Share premium RMB'000	Shares held for share award scheme RMB'000	Total RMB'000
At 1 January 2011	1,835,730,235	198	2,299,965	(258,137)	2,042,026
Employee share option schemes:					
Value of employee services	–	–	93,102	–	93,102
Number of shares issued and proceeds received	3,980,713	–	80,689	–	80,689
Employee share award scheme:					
Value of employee services	–	–	242,477	–	242,477
Shares purchased and withheld for share award scheme	–	–	–	(247,777)	(247,777)
Shares vested from share award scheme and transferred to the grantees	–	–	(29,574)	29,574	–
Repurchase and cancellation of shares	(611,300)	–	(97,586)	–	(97,586)
At 30 June 2011	<u>1,839,099,648</u>	<u>198</u>	<u>2,589,073</u>	<u>(476,340)</u>	<u>2,112,931</u>

Note:

- (a) As at 30 June 2012, the total number of issued ordinary shares of the Company was 1,844,090,136 shares (31 December 2011: 1,839,814,008 shares), which included 17,418,292 shares (31 December 2011: 17,809,839 shares) held under the Share Award Scheme (Note 13(b)).
- (b) The Group merged the share-based compensation reserve related to the Company's share option schemes and share award scheme into the Company's share premium during the six months ended 30 June 2012. The comparative figures have been reclassified to conform to the presentation of the current period. Such reclassification has no impact on the Group's net profit for the comparative period, as well as on the Group's net assets as at 31 December 2011.

Notes to the Interim Financial Information

13 SHARE-BASED PAYMENTS

(a) Share option schemes

The Company has adopted four share option schemes, namely, the Pre-IPO Option Scheme, the Post-IPO Option Scheme I, the Post-IPO Option Scheme II and Post-IPO Option Scheme III, under which the directors may, at their discretion, grant options to any qualifying participants to subscribe for shares in the Company, subject to the terms and conditions stipulated therein. No further options will be granted under the Pre-IPO Option Scheme and the Post-IPO Option Scheme I.

In respect of Post-IPO Option Scheme II and Post-IPO Option Scheme III, the exercise price must be at least the higher of: (i) the closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheet on the date of grant, which must be a business day; (ii) the average closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's shares. In addition, the option vesting period is determined by the Board provided that it is not later than the last day of a 7-year or 10-year period after the date of grant of option.

(i) Movements in share options

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

	Pre-IPO Option Scheme		Post-IPO Option Scheme I		Post-IPO Option Scheme II		Post-IPO Option Scheme III		Total
	Average exercise price	No. of options	Average exercise price	No. of options	Average exercise price	No. of options	Average exercise price	No. of options	No. of options
At 1 January 2011	USD0.0935	563,193	HKD12.8579	12,805,763	HKD54.9391	28,795,168	HKD158.5000	1,000,000	43,164,124
Granted	-	-	-	-	HKD194.4000	312,550	-	-	312,550
Exercised	USD0.0709	(464,420)	HKD12.7643	(1,866,215)	HKD43.6137	(1,650,078)	-	-	(3,980,713)
Lapsed	-	-	HKD4.4850	(33)	HKD58.0532	(96,556)	-	-	(96,589)
At 30 June 2011	USD0.1998	98,773	HKD12.8739	10,939,515	HKD57.2042	27,361,084	HKD158.5000	1,000,000	39,399,372
Exercisable as at									
30 June 2011	USD0.1998	98,773	HKD11.6643	9,671,095	HKD 41.1057	7,512,924	-	-	17,282,792
At 1 January 2012	-	-	HKD12.3871	8,761,937	HKD59.9665	26,156,088	HKD158.5000	1,000,000	35,918,025
Exercised	-	-	HKD15.6453	(2,026,139)	HKD45.0567	(2,404,389)	-	-	(4,430,528)
Lapsed	-	-	HKD8.1734	(157)	HKD47.3139	(85,024)	-	-	(85,181)
At 30 June 2012	-	-	HKD11.4071	6,735,641	HKD61.5267	23,666,675	HKD158.5000	1,000,000	31,402,316
Exercisable as at									
30 June 2012	-	-	HKD11.1559	6,615,641	HKD40.8706	9,526,152	-	-	16,141,793

Notes to the Interim Financial Information

13 SHARE-BASED PAYMENTS (continued)

(a) Share option schemes (continued)

(i) Movements in share options (continued)

During the six months ended 30 June 2012, no share option (during the six months ended 30 June 2011: Nil) was granted to the directors of the Company.

As a result of options exercised during the six months ended 30 June 2012, 4,430,528 ordinary shares (during the six months ended 30 June 2011: 3,980,713 ordinary shares) were issued by the Company (Note 12). The weighted average price of the shares at the time these options were exercised was HKD213.57 per share (for the six months ended 30 June 2011: HKD202.01 per share).

(ii) Outstanding share options

Details of the expiry dates, exercise prices and the respective numbers of share options which remained outstanding as at 30 June 2012 and 31 December 2011 are as follows:

Expiry Date	Range of exercise price	Number of share options	
		30 June 2012	31 December 2011
10 years commencing from the adoption date of 24 March 2004 (Post-IPO Option Scheme I)	HKD3.66-HKD8.35	3,509,751	4,164,319
	HKD11.55-HKD25.26	3,225,890	4,597,618
		6,735,641	8,761,937
7 years commencing from the date of grant of options (Post-IPO Option Scheme II)	HKD31.75-HKD43.50	11,689,738	12,715,582
	HKD45.50-HKD90.30	8,271,812	9,733,781
	HKD128.40-HKD194.40	3,705,125	3,706,725
	23,666,675	26,156,088	
10 years commencing from the date of grant of options (Post-IPO Option Scheme III)	HKD158.50	1,000,000	1,000,000
		31,402,316	35,918,025

Notes to the Interim Financial Information

13 SHARE-BASED PAYMENTS (continued)

(b) Share award scheme

The Company has adopted a share award scheme (the “Share Award Scheme”), which is managed by an independent trustee appointed by the Group (the “Trustee”). The vesting period of the awarded share is determined by the Board.

Movements in the number of shares held for the Share Award Scheme and awarded shares for the six months ended 30 June 2012 and 2011 are as follows:

	Number of shares held for the Share Award Scheme	Number of awarded shares
At 1 January 2011	80	13,562,734
Purchased for awards	1,437,320	–
Shares to be allotted to the Share Award Scheme	535,170	–
Granted	(1,972,570)	1,972,570
Vested and exercised	–	(238,616)
At 30 June 2011	<u>–</u>	<u>15,296,688</u>
Exercisable as at 30 June 2011		<u>72,117</u>
At 1 January 2012	1,970,840	15,838,999
Purchased and withheld for award	107,981	–
Granted	(759,400)	759,400
Lapsed	321,925	(321,925)
Vested and exercised	–	(499,528)
At 30 June 2012	<u>1,641,346</u>	<u>15,776,946</u>
Exercisable as at 30 June 2012		<u>3,005</u>

During the six months ended 30 June 2012, no awarded share (during the six months ended 30 June 2011: 35,000) was granted to the directors of the Company.

Notes to the Interim Financial Information

13 SHARE-BASED PAYMENTS (continued)

(b) Share award scheme (continued)

The fair value of the awarded shares was calculated based on the market price of the Company's shares at the respective grant date. The expected dividends during the vesting period have been taken into account when assessing the fair value of these awarded shares.

The weighted average fair value of awarded shares granted during the six months ended 30 June 2012 was HKD 215.62 per share (during the six months ended 30 June 2011: HKD208.32 per share). In addition, such awarded shares are divided into one to five tranches on an equal basis. The first tranche can be exercised immediately or after a specified period ranging from three months to five years from the grant dates, and the remaining tranches will become exercisable in each subsequent year.

(c) Employee incentive scheme

In 2011, the Group established an employee incentive scheme in a form of limited liability partnership (the "EIS") for incentive purpose pursuant to a shareholders' resolution passed at the 2011 annual general meeting of the Company held on 11 May 2011. The Board may, at its absolute discretion, select any employees of the Group to participate in the EIS by subscribing for partnership interest at cash consideration. The initial total cash contribution by selected employees is limited to approximately RMB80,000,000. The participating employees are entitled to all the economic benefits generated by the EIS (if any) after a specified vesting period under the EIS, ranging from 4 to 7 years. A wholly-owned subsidiary of the Company which acts as a general partner of the EIS manages and in essence, controls it. The EIS is therefore consolidated by the Company. In addition, because certain continuous service conditions are attached to the partnership interest subscribed by the employees, the EIS is accounted for as an equity-settled share-based payment transaction.

During the six months ended 30 June 2012, there was no partnership interest of EIS granted to the employees of the Group.

(d) Share options and restricted share award schemes adopted by non-wholly owned subsidiaries

Other than the above, certain non-wholly owned subsidiaries of the Company operate their own share-based compensation plans (share option and/or restricted share award schemes). The exercise prices of the share options, as well as the vesting periods of the share options and restricted shares are determined by the board of directors of these subsidiaries at their sole discretion in accordance with the relevant plans. Similar to the share option/award schemes adopted by the Company, the share options or restricted shares of the subsidiaries so granted are normally vested in several tranches.

The directors of the Company considered that the fair value of share options/restricted shares granted under the share-based compensation plans of the non-wholly owned subsidiaries, and the relevant share-based compensation expense charged to the income statement of the Group for the three and six months ended 30 June 2012, are not significant to the Group.

Notes to the Interim Financial Information

13 SHARE-BASED PAYMENTS (continued)

(e) Expected retention rate of grantees

The Group has to estimate the expected yearly percentage of grantees that will stay within the Group at the end of vesting periods of the options and awarded shares (the “Expected Retention Rate”) in order to determine the amount of share-based compensation expenses charged to the income statement. As at 30 June 2012, the Expected Retention Rate was assessed to be 91% (31 December 2011: 91%).

14 ACCOUNTS PAYABLE

Accounts payable and their ageing analysis are as follows:

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
0 - 30 days	2,169,560	1,514,155
31 - 60 days	962,739	351,587
61 - 90 days	54,185	108,337
Over 90 days	181,954	270,035
	<u>3,368,438</u>	<u>2,244,114</u>

15 OTHER PAYABLES AND ACCRUALS

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Prepayments received from customers and e-Commerce business	2,003,263	1,840,947
Staff costs and welfare accruals	1,504,655	1,478,391
Marketing and administrative expense accruals	683,071	731,571
Purchase consideration payables for business combinations and associates	266,489	252,952
Current portion of running royalty fee for online games	44,274	315,045
Others	370,861	395,375
	<u>4,872,613</u>	<u>5,014,281</u>

Notes to the Interim Financial Information

16 LONG-TERM PAYABLES

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Present value of non-current portion of running royalty fee for online games	132,103	945,135
Present value of liabilities in relation to put options granted to non-controlling interests	1,028,603	670,985
Present value of purchase consideration payable for certain business combination	137,344	131,180
Others	143,870	112,508
	<u>1,441,920</u>	<u>1,859,808</u>

17 BORROWINGS

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Included in non-current liabilities:		
USD bank borrowing		
Unsecured (a)	948,735	–
Included in current liabilities:		
RMB bank borrowings		
Secured (b)	320,375	2,958,720
USD bank borrowings		
Unsecured (c)	3,288,948	4,410,630
Bonds		
Unsecured	–	630,090
	<u>3,609,323</u>	<u>7,999,440</u>
	<u>4,558,058</u>	<u>7,999,440</u>

Notes to the Interim Financial Information

17 BORROWINGS (continued)

Movement in the borrowings is analysed as follows:

	Unaudited	
	Six months ended	
	30 June	
	2012	2011
	RMB'000	RMB'000
At beginning of period	7,999,440	5,298,947
Additions of bank borrowings	1,893,240	4,778,230
Issuance of bonds	–	657,520
Repayments of bonds	(629,190)	–
Repayments of bank borrowings	(4,729,060)	(2,493,119)
Exchange difference	23,628	(91,513)
	<u>4,558,058</u>	<u>8,150,065</u>
At end of period		

Note:

- (a) Unsecured long-term bank borrowing of carrying amount of RMB948,735,000 as at 30 June 2012 was denominated in USD. The aggregate principal amount was USD150,000,000 with an interest rate of LIBOR plus 2.44% per annum. Such bank borrowing shall be repaid by installments.
- (b) Bank borrowings of carrying amount of RMB320,375,000 were secured by pledge of bank deposits of RMB324,347,000.
- (c) Unsecured bank borrowings of carrying amount of RMB3,288,948,000 as at 30 June 2012 were denominated in USD. The aggregate principal amount was USD520,000,000 with interest rates of LIBOR plus 0.85% to 1.75% per annum. In addition, the Group entered into foreign exchange forward contracts to purchase the required amount of USD with RMB for settling some of the bank borrowings with an aggregate principal amount of USD45,000,000 upon the respective borrowing due dates. As the Group did not adopt hedge accounting, these bank borrowings and the relevant foreign exchange forward contracts were accounted for separately. The bank borrowings were accounted for as USD denominated bank borrowings and stated at amortised cost, while the forward contracts were accounted for as derivative financial instruments stated at fair value with their gains or losses recorded in "Other (losses)/gains, net" in the consolidated income statement.

18 LONG-TERM NOTES PAYABLE

On 12 December 2011, the Company issued long-term notes (the "Notes") with an initial aggregate principal amount of USD600,000,000 for general corporate purposes. The Notes bear an interest at 4.625% per annum from 12 December 2011, payable semi-annually in arrears on 12 June and 12 December of each year, beginning on 12 June 2012. The Notes are listed on Singapore Exchange Securities Trading Limited and will mature on 12 December 2016.

As at 30 June 2012, the carrying amount of the Notes was RMB3,751,839,000.

Notes to the Interim Financial Information

19 DEFERRED INCOME TAXES

The movements of the deferred income tax assets/liabilities account were as follows:

	Deferred income tax assets RMB'000	Deferred income tax liabilities RMB'000	Deferred income tax, net RMB'000
At 1 January 2011	219,019	(967,211)	(748,192)
Charge to consolidated income statement	(28,136)	(48,775)	(76,911)
Credit to other comprehensive income	6,690	–	6,690
Temporary differences arising from a business combination	–	(269,793)	(269,793)
Withholding tax paid in relation to the remittance of dividends from the PRC to foreign investors	–	339,946	339,946
At 30 June 2011	<u>197,573</u>	<u>(945,833)</u>	<u>(748,260)</u>
At 1 January 2012	198,058	(939,534)	(741,476)
Charge to consolidated income statement	(15,818)	(105,714)	(121,532)
Credit to other comprehensive income	2,368	–	2,368
Temporary differences arising from a business combination (Note 26)	–	(3,082)	(3,082)
Withholding tax paid in relation to the remittance of dividends from the PRC to foreign investors	–	156,968	156,968
Exchange difference	–	(2,460)	(2,460)
At 30 June 2012	<u>184,608</u>	<u>(893,822)</u>	<u>(709,214)</u>

Notes to the Interim Financial Information

20 OTHER (LOSSES)/GAINS, NET

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2012	2011	2012	2011
	RMB'000	RMB'000	RMB'000	RMB'000
Gains on disposal/deemed disposal of associates	–	–	11,543	459,037
Government subsidies	13,258	9,699	32,836	14,988
Gains/(losses) from derivative financial instruments	18	(23,495)	(19,842)	(44,869)
Donation to Tencent Charity Fund	–	–	(60,000)	(100,000)
Others	(16,495)	16,605	(31,398)	12,722
	<u>(3,219)</u>	<u>2,809</u>	<u>(66,861)</u>	<u>341,878</u>

21 EXPENSES BY NATURE

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2012	2011	2012	2011
	RMB'000	RMB'000	RMB'000	RMB'000
Employee benefit expenses (Note)	1,908,491	1,249,702	3,597,857	2,209,952
Content costs and agency fees	1,697,518	1,103,048	3,140,491	2,236,777
Mobile and telecom charges and bandwidth and server custody fees	817,869	620,745	1,593,286	1,212,068
Cost of merchandise sold	810,273	–	1,524,365	–
Depreciation of fixed assets (Note)	444,716	273,999	868,772	494,544
Promotion and advertising expenses	386,383	240,817	663,444	447,004
Amortisation of intangible assets	142,464	222,651	384,574	275,861
Operating lease rentals in respect of office buildings	145,827	80,339	288,674	139,350
Travelling and entertainment expenses	73,669	48,380	131,113	77,549
Other expenses	356,006	224,819	650,231	363,043
	<u>6,783,216</u>	<u>4,064,500</u>	<u>12,842,807</u>	<u>7,456,148</u>

Notes to the Interim Financial Information

21 EXPENSES BY NATURE (continued)

Note:

Research and development expenses for the three and six months ended 30 June 2012 were RMB1,042,440,000 and RMB1,983,203,000, respectively (for the three and six months ended 30 June 2011: RMB671,791,000 and RMB1,184,978,000, respectively) which included employee benefit expenses of RMB842,449,000 and depreciation of fixed assets of RMB109,412,000 for the three months ended 30 June 2012 (for the three months ended 30 June 2011: RMB582,534,000 and RMB63,088,000, respectively) and employee benefit expenses of RMB1,617,522,000 and depreciation of fixed assets of RMB217,176,000 for the six months ended 30 June 2012 (for the six months ended 30 June 2011: RMB1,022,103,000 and RMB116,291,000, respectively). No research and development expenses were capitalised as at 30 June 2012.

22 FINANCE (COSTS)/INCOME, NET

	Unaudited Three months ended 30 June		Unaudited Six months ended 30 June	
	2012 RMB'000	2011 RMB'000	2012 RMB'000	2011 RMB'000
Exchange (losses)/gains	(45,912)	14,903	(48,316)	27,719
Interest expenses	(69,344)	(13,132)	(136,922)	(29,817)
	<u>(115,256)</u>	<u>1,771</u>	<u>(185,238)</u>	<u>(2,098)</u>

Interest expenses mainly arose from the borrowings (Note 17) and long-term notes payable (Note 18).

Notes to the Interim Financial Information

23 TAX EXPENSE

(a) Income tax expense

- (i) Cayman Islands and British Virgin Islands profits tax

The Group was not subject to any taxation in the Cayman Islands and British Virgin Islands for the three and six months ended 30 June 2012 and 2011.

- (ii) Hong Kong profits tax

Hong Kong profits tax provision has been provided at the rate of 16.5% on the estimated assessable profits for the three and six months ended 30 June 2012. No such provision was provided for the three and six months ended 30 June 2011.

- (iii) PRC Corporate Income Tax ("CIT")

CIT provision was made on the assessable profits of entities within the Group incorporated in the PRC, calculated in accordance with the relevant regulations of the PRC after considering the available tax benefits from refunds and allowances.

Pursuant to the PRC Corporate Income Tax Law passed by the Tenth National People's Congress on 16 March 2007 (the "CIT Law"), the CIT rate for domestic and foreign enterprises has been unified at 25%, effective from 1 January 2008.

The CIT Law also provides a five-year transitional period starting from its effective date for those enterprises which were established before the promulgation of the CIT Law and which were entitled to preferential income tax rates under the then effective tax laws or regulations.

On 26 December 2007, the State Council issued the "Circular to Implementation of the Transitional Preferential Policies for the Corporate Income Tax". Pursuant to this circular, the transitional CIT rates for the Group's subsidiaries established in the Shenzhen Special Economic Zone or the Beijing High Technology Zone before 16 March 2007 are 18%, 20%, 22%, 24% and 25% for 2008, 2009, 2010, 2011 and 2012, respectively. Other tax preferential treatments such as reduction of 50% in income tax rates shall be based on the above transitional income tax rates for the respective years.

In 2011, certain subsidiaries of the Company in the PRC were approved as High and New Technology Enterprise, and accordingly, they were subject to a reduced preferential CIT rate of 15% for a 3-year period from 2011 to 2013 according to the applicable CIT Law.

In addition, according to relevant tax circulars issued by the PRC tax authorities, certain subsidiaries of the Company are exempt from CIT for two years, followed by a 50% reduction in the applicable tax rates for the next three years, commencing either from the first year of commercial operation or from the first year of profitable operation after offsetting tax losses generated in prior years.

Notes to the Interim Financial Information

23 TAX EXPENSE (continued)

(a) Income tax expense (continued)

- (iv) United States corporate income tax

United States corporate income tax provision was provided during the three and six months ended 30 June 2012 for the entities within the Group which were incorporated in the United States. No such provision was provided for the three and six months ended 30 June 2011.

- (v) PRC withholding tax

According to applicable PRC tax regulations, dividends distributed by a company established in the PRC to a foreign investor with respect to profits derived after 1 January 2008 are generally subject to a 10% withholding tax. If a foreign investor is incorporated in Hong Kong and meets the conditions or requirements under the double taxation arrangement entered into between the PRC and Hong Kong, the relevant withholding tax rate will be reduced from 10% to 5%.

The income tax expense of the Group for the three and six months ended 30 June 2012 and 2011 are analysed as follows:

	Unaudited Three months ended 30 June		Unaudited Six months ended 30 June	
	2012 RMB'000	2011 RMB'000	2012 RMB'000	2011 RMB'000
Current tax	631,810	432,561	1,236,965	860,235
Deferred tax	76,014	(27,398)	121,532	76,911
	<u>707,824</u>	<u>405,163</u>	<u>1,358,497</u>	<u>937,146</u>

Notes to the Interim Financial Information

23 TAX EXPENSE (continued)

(a) Income tax expense (continued)

The tax on the Group's profit before income tax differs from the theoretical amount that would arise using the tax rate of 25% for the three and six months ended 30 June 2012 (for the three and six months ended 30 June 2011: 24%), being the tax rate of the major subsidiaries of the Company before preferential tax treatments. The difference is analysed as follows:

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2012	2011	2012	2011
	RMB'000	RMB'000	RMB'000	RMB'000
Profit before income tax	3,818,395	2,748,435	7,431,398	6,164,626
Add: Share of losses/(profit) of associates and jointly controlled entities	3,964	37,235	12,337	3,678
	3,822,359	2,785,670	7,443,735	6,168,304
Tax calculated at a tax rate of 25% (for the three and six months ended 30 June 2011: 24%)	955,590	668,561	1,860,934	1,480,393
Effects of different tax rates applicable to different subsidiaries	(308,254)	(227,458)	(672,381)	(533,220)
Effects of tax holiday on assessable profit of subsidiaries	(67,650)	(125,882)	(135,057)	(249,576)
Income not subject to tax	(27,478)	(1,900)	(46,456)	(11,663)
Expenses not deductible for tax purposes	60,843	79,318	120,092	113,879
Withholding tax on earnings expected to be remitted by PRC subsidiaries	78,603	50,000	171,603	141,500
Unrecognised deferred income tax assets	29,588	22,019	73,180	55,328
Adjustments in respect of CIT filing	(13,418)	(59,495)	(13,418)	(59,495)
Income tax expense	707,824	405,163	1,358,497	937,146

Notes to the Interim Financial Information

23 TAX EXPENSE (continued)

(b) Value-added tax, business tax and related taxes and surcharges

The operations of the Group are also subject to the following taxes and surcharges in the PRC:

Category	Tax rate	Basis of levy
Value-added tax ("VAT")	6-17%	Sales value of goods sold, offsetting by VAT on purchases
	3%	Sales value of goods sold
Business tax ("BT")	3-5%	Services fee income
City construction tax	1-7%	Net VAT and BT payable amount
Construction fee for cultural undertakings	3%	Advertising income
Educational surcharge	3-5%	Net VAT and BT payable amount

24 EARNINGS PER SHARE

(a) Basic

Basic earnings per share ("EPS") are calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the period.

	Unaudited Three months ended 30 June		Unaudited Six months ended 30 June	
	2012	2011	2012	2011
Profit attributable to equity holders of the Company for the period (RMB'000)	3,100,075	2,349,246	6,049,585	5,219,620
Weighted average number of ordinary shares in issue (thousand shares)	1,826,071	1,823,051	1,824,501	1,822,866
Basic EPS (RMB per share)	1.698	1.289	3.316	2.863

Notes to the Interim Financial Information

24 EARNINGS PER SHARE (continued)

(b) Diluted

The share options and awarded shares granted by the Company have potential dilutive effect on the EPS. Diluted EPS is calculated by adjusting the weighted average number of ordinary shares outstanding by the assumption of the conversion of all potential dilutive ordinary shares arising from share options and awarded shares granted by the Company (collectively forming the denominator for computing the diluted EPS). No adjustment is made to earnings (numerator).

In addition, the share options and restricted shares granted by the Company's non-wholly owned subsidiaries and associates should also have potential dilutive effect on the EPS. During the three and six months ended 30 June 2012, these share options and restricted shares either had anti-dilutive effect or their dilutive effect was insignificant to the Group.

	Unaudited Three months ended 30 June		Unaudited Six months ended 30 June	
	2012	2011	2012	2011
Profit attributable to equity holders of the Company for the period (RMB'000)	3,100,075	2,349,246	6,049,585	5,219,620
Weighted average number of ordinary shares in issue (thousand shares)	1,826,071	1,823,051	1,824,501	1,822,866
Adjustments for share options (thousand shares)	23,766	30,626	24,406	31,160
Adjustments for awarded shares (thousand shares)	11,496	10,160	11,515	10,061
Weighted average number of ordinary shares for the calculation of diluted EPS (thousand shares)	1,861,333	1,863,837	1,860,422	1,864,087
Diluted EPS (RMB per share)	1.665	1.260	3.252	2.800

Notes to the Interim Financial Information

25 DIVIDEND

A final dividend in respect of the year ended 31 December 2011 of HKD0.75 per share (2010: HKD0.55 per share) was proposed pursuant to a resolution passed by the Board on 14 March 2012 and approved by shareholders at the 2012 annual general meeting of the Company held on 16 May 2012. Such dividend, amounted to HKD1,369,117,000 (equivalent to approximately RMB1,107,889,000) (final dividend for 2010: HKD1,010,294,000 (equivalent to approximately RMB838,290,000)), had been paid as at 30 June 2012.

The Board did not propose any interim dividend for the six months ended 30 June 2012 (for the six months ended 30 June 2011: Nil).

26 BUSINESS COMBINATIONS

During the six months ended 30 June 2012, the Group acquired 51% equity interest in a company engaged in publication and online reading services and 100% equity interest in a company engaged in providing massively multi-player online game information.

The considerations and the allocation of such considerations to the fair value of the net assets acquired and goodwill recognised as at the respective dates of these acquisitions are as follows:

	RMB'000
Purchase considerations	75,846
Carrying amount of the non-controlling interests	(2,455)
	73,391
	73,391
Fair value of net assets acquired	7,544
Goodwill	65,847
	73,391

The revenues and net profit contributed by these subsidiaries from their respective acquisition dates to 30 June 2012 to the Group were not material.

27 CONTINGENCIES

The Group had no material contingent liabilities outstanding as at 30 June 2012.

Notes to the Interim Financial Information

28 COMMITMENTS

(a) Capital commitments

Capital commitments as at 30 June 2012 and 2011 are analysed as follows:

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Contracted:		
Construction/purchase of buildings and purchase of land use rights	589,375	463,046
Purchase of other fixed assets	149,685	132,260
Capital investment in investees	1,075,357	816,910
	1,814,417	1,412,216
Authorised but not contracted:		
Construction/purchase of buildings and purchase of land use rights	1,049,033	1,186,867
Capital investment in investees	450,772	651,927
	1,499,805	1,838,794
	3,314,222	3,251,010

(b) Operating lease commitments

The future aggregate minimum lease payments under non-cancellable operating leases in respect of buildings are as follows:

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Contracted:		
Not later than one year	505,969	520,396
Later than one year and not later than five years	1,301,742	1,462,788
Later than five years	255,295	286,135
	2,063,006	2,269,319

Notes to the Interim Financial Information

28 COMMITMENTS (continued)

(c) Other commitments

The future aggregate minimum payments under non-cancellable bandwidth and server custody leases, online game licensing and contents agreements are as follows:

	Unaudited	Audited
	30 June	31 December
	2012	2011
	RMB'000	RMB'000
Contracted:		
Not later than one year	1,024,238	596,031
Later than one year and not later than five years	1,333,948	768,291
	<u>2,358,186</u>	<u>1,364,322</u>

29 RELATED PARTIES TRANSACTIONS

Save as disclosed in “Loans to associates and jointly controlled entities” in Note 11 (Prepayments, deposits and other assets) and Note 13 (Share-based payments) to this Interim Financial Information, the Group had no other material transactions with related parties for the three and six months ended 30 June 2012, and no other material related parties’ balances as at 30 June 2012.

30 SUBSEQUENT EVENTS

- (a) In July 2012, the Group purchased 49% issued share capital of Level Up! International Holdings Pte. Ltd. (“Level Up”) from a related party (the “Level Up Acquisition”). In addition, the Group has an option to acquire, within a two-year period after closing, certain additional number of shares in Level Up that, together with the shares acquired in the Level Up Acquisition, will represent 67% of the issued share capital of Level Up as at the date when the option is fully exercised. Level Up is principally engaged in online game publishing and game magazine publication. As of the date of this report, the Group is in the process of assessing and quantifying the fair value of the net identifiable assets acquired and not in a position to complete its initial accounting because of time constraint.
- (b) In May 2012, the Group entered into sales and purchase agreement, pursuant to which, the Group agreed to purchase certain equity interest of Epic Games, Inc. (“Epic”). This acquisition was completed in July 2012. Epic is principally engaged in developing game engine technology, as well as game titles for PC, consoles and mobile devices. Upon completion of the acquisition, Epic has been accounted for as an associate of the Group.

31 SEASONALITY

The Group’s online advertising business is subject to seasonal fluctuations as advertisers usually reduce their advertising spending around the Chinese New Year holiday period (the first quarter of the year).

Other Information

DIRECTORS' INTERESTS IN SECURITIES

As at 30 June 2012, the interests and short positions of the directors and the chief executive of the Company in the shares, underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) which (a) were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they have taken, or are deemed to have taken, under such provisions of the SFO); or (b) were required, pursuant to section 352 of the SFO, to be recorded in the register required to be kept by the Company; or (c) were required, pursuant to the Model Code, to be notified to the Company and the Stock Exchange were as follows:

(A) LONG AND SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES OF THE COMPANY

Name of director	Long/short position	Nature of interest	Number of shares/ underlying shares held	Percentage of issued share capital
Ma Huateng	Long position	Corporate (Note 1)	189,892,880	10.30%
Zhang Zhidong	Long position	Corporate (Note 2)	66,750,000	3.62%
Lau Chi Ping Martin	Long position	Personal	9,903,600 (Note 3)	0.54%
Li Dong Sheng	Long position	Personal	40,000 (Note 4)	0.002%
Iain Ferguson Bruce	Long position	Personal	105,000 (Note 5)	0.006%
Ian Charles Stone	Long position	Personal	75,000 (Note 6)	0.004%

Other Information

Notes:

1. These shares are held by Advance Data Services Limited, a British Virgin Islands company wholly owned by Ma Huateng.
2. These shares are held by Best Update International Limited, a British Virgin Islands company wholly owned by Zhang Zhidong.
3. The interest comprises 4,103,600 shares and 5,800,000 underlying shares in respect of the share options granted pursuant to the Post-IPO Option Scheme II and the Post-IPO Option Scheme III. Details of the share options granted to this director are set out below under “Share Option Schemes”.
4. The interest represents the underlying shares in respect of the share options granted pursuant to the Post-IPO Option Scheme I. Details of the share options granted to this director are set out below under “Share Option Schemes”.
5. The interest comprises 49,000 shares and 56,000 underlying shares in respect of the 40,000 share options granted pursuant to Post-IPO Option Scheme I and 16,000 awarded shares granted pursuant to the Share Award Scheme. Details of the share options and awarded shares granted to this director are set out below under “Share Option Schemes” and “Share Award Scheme” respectively.
6. The interest comprises 3,000 shares and 72,000 underlying shares in respect of the 60,000 share options granted pursuant to Post-IPO Option Scheme I and the 12,000 awarded shares granted pursuant to the Share Award Scheme. Details of the share options and awarded shares granted to this director are set out below under “Share Option Schemes” and “Share Award Scheme” respectively.

(B) LONG POSITION IN THE SHARES OF ASSOCIATED CORPORATIONS

Name of director	Name of associated corporation	Nature of interest	Number of shares and class of shares held	Percentage of issued share capital
Ma Huateng	Tencent Computer	Personal	RMB16,285,710 (registered capital)	54.29%
	Shiji Kaixuan	Personal	RMB5,971,427 (registered capital)	54.29%
Zhang Zhidong	Tencent Computer	Personal	RMB6,857,130 (registered capital)	22.86%
	Shiji Kaixuan	Personal	RMB2,514,281 (registered capital)	22.86%

Save as disclosed above, none of the directors or chief executive of the Company and their associates, had interests or short positions in any shares, underlying shares or debentures of the Company and its associated corporations as at 30 June 2012.

Other Information

SHARE OPTION SCHEMES

The Company has adopted four share option schemes, namely, the Pre-IPO Option Scheme, the Post-IPO Option Scheme I, the Post-IPO Option Scheme II and Post-IPO Option Scheme III, under which the directors may, at their discretion, grant options to any qualifying participants to subscribe for shares in the Company, subject to the terms and conditions stipulated therein. No further options will be granted under the Pre-IPO Option Scheme and the Post-IPO Option Scheme I. Movements of the options under the Pre-IPO Option Scheme, the Post-IPO Option Scheme I, the Post-IPO Option Scheme II and the Post-IPO Option Scheme III are detailed in Note 13 to the Interim Financial Information as included in this interim report.

As at 30 June 2012, there were a total of 5,940,000 outstanding share options granted to the directors of the Company, details of which are as follows:

Name of director	Date of grant	Exercise price (HKD)	Number of share options			As at 30 June 2012	Exercise period
			As at 1 January 2012	Granted during the period	Exercised during the period		
Lau Chi Ping Martin	4 April 2007	25.26	600,000	–	600,000 (Note 5)	–	4 April 2008 to 23 March 2014 (Note 1)
	5 July 2007	33.05	2,000,000	–	200,000 (Note 5)	1,800,000	5 July 2009 to 4 July 2014 (Note 2)
	5 July 2007	33.05	3,000,000	–	–	3,000,000	5 July 2010 to 4 July 2014 (Note 3)
	24 March 2010	158.50	1,000,000	–	–	1,000,000	24 March 2015 to 23 March 2020 (Note 4)
	Total:		6,600,000	–	800,000	5,800,000	
Li Dong Sheng	4 April 2007	25.26	40,000	–	–	40,000	4 April 2008 to 23 March 2014 (Note 1)
Iain Ferguson Bruce	4 April 2007	25.26	60,000	–	20,000 (Note 5)	40,000	4 April 2008 to 23 March 2014 (Note 1)
Ian Charles Stone	4 April 2007	25.26	60,000	–	–	60,000	4 April 2008 to 23 March 2014 (Note 1)
	Grand Total:		6,760,000	–	820,000	5,940,000	

Other Information

Notes:

- For options granted with exercisable date determined based on the grant date of options, the first 20% of the option can be exercised one year after the grant date, and 20% each of the total options will become exercisable in each subsequent year.
- For options granted with exercisable date determined based on the grant date of options, the first 20% of the option can be exercised two years after the grant date, and 20% each of the total options will become exercisable in each subsequent year.
- For options granted with exercisable date determined based on the grant date of options, the first 20% of the option can be exercised three years after the grant date, and 20% each of the total options will become exercisable in each subsequent year, except the last 20% of the total options which will become exercisable in the eleventh month after the fourth 20% of the total options become exercisable.
- For options granted with exercisable date determined based on the grant date of options, the first 25% of the option can be exercised five years after the grant date, and 25% each of the total options will become exercisable in each subsequent year.
- The closing prices immediately before the dates on which the options were exercised by each of the directors were as follows:

Name of director	Closing prices (HKD)
Lau Chi Ping Martin	222.80
Iain Ferguson Bruce	221.40

- No options were granted, cancelled or lapsed during the period.

SHARE AWARD SCHEME

The Company adopted the Share Award Scheme in which eligible persons (including any director) of the Group will be entitled to participate. Unless early terminated by the Board, the Share Award Scheme shall be valid and effective for a term of 15 years commencing on the adoption date. The maximum number of shares which can be awarded under the Share Award Scheme and to an Awarded Person are limited to two percent (i.e. 35,755,232 shares) and one percent (i.e. 17,877,616 shares) of the issued share capital of the Company respectively as at the date of adoption.

Pursuant to the Share Award Scheme, the Board shall select the eligible persons for participation in the Share Award Scheme and determine the number of shares to be awarded. Shares will be acquired by an independent trustee at the cost of the Company or shares will be allotted to the independent trustee under the general mandate granted or to be granted by the shareholders of the Company at general meetings from time to time and be held in trust for the Awarded Persons, excluding the directors and substantial shareholders of the Group, until the end of each vesting period.

Vested shares will be transferred at no cost to the Awarded Persons. The Company shall comply with the relevant Listing Rules when granting the Awarded Shares. If awards are made to the directors or substantial shareholders of the Group, such awards shall constitute connected transaction under Chapter 14A of the Listing Rules and the Company shall comply with the relevant requirements under the Listing Rules.

Other Information

The Awarded Shares and the related income derived therefrom are subject to a vesting scale to be determined by the Board at the date of the grant of the award. Vesting of the Awarded Shares will be conditional on the Awarded Persons satisfying all vesting conditions specified by the Board at the time of making the award and, for the majority of the Awarded Persons, the relevant Awarded Shares will be transferred to the Awarded Persons on or about the relevant vesting dates.

During the six months ended 30 June 2012, a total of 759,400 Awarded Shares were granted and no Awarded Shares was granted to the directors of the Company. Details of the movements in the Share Award Scheme during the six months ended 30 June 2012 are set out in Note 13 to the Interim Financial Information as included in this interim report.

As at 30 June 2012, there were a total of 28,000 outstanding Awarded Shares granted to the directors of the Company, details of which are as follows:

Name of director	Date of grant	Number of Awarded Shares				As at 30 June 2012	Vesting period
		As at 1 January 2012	Granted during the period	Vested during the period	As at 30 June 2012		
Iain Ferguson Bruce	17 March 2011	20,000	–	4,000	16,000	17 March 2012 to 17 March 2016	
Ian Charles Stone	17 March 2011	15,000	–	3,000	12,000	17 March 2012 to 17 March 2016	
	Total:	<u>35,000</u>	<u>–</u>	<u>7,000</u>	<u>28,000</u>		

INFORMATION OF DIRECTORS

Pursuant to Rule 13.51B(1) of the Listing Rules, the amounts of emoluments of certain directors have been changed during the period of this interim report and the detailed changes are shown under the biographical details of each director, if applicable, as follows:

Ma Huateng, age 40, is an executive director, Chairman of the Board and CEO of the Company. Mr Ma has overall responsibilities for strategic planning and positioning and management of the Group. Mr Ma is one of the core founders and has been employed by the Group since 1999. Prior to his current employment, Mr Ma was in charge of research and development for Internet paging system development at China Motion Telecom Development Limited, a supplier of telecommunications services and products in China. Mr Ma is a member of the 5th Shenzhen Municipal People's Congress. Mr Ma has a Bachelor of Science degree specialising in Computer and its Application obtained in 1993 from Shenzhen University and more than 18 years of experience in the telecommunications and Internet industries. He is also a director of Advance Data Services Limited which holds shares of the Company. Mr Ma is entitled to an annual base salary of RMB4,245,800 in 2012 which was covered by the current service contract with the Company and the basis of determining his emoluments including the base salary and bonus as set out in the service contract remained the same.

Other Information

Lau Chi Ping Martin, age 39, is an executive director with effect from 21 March 2007. Mr Lau was appointed as the President of the Company in February 2006 to assist Mr Ma, Chairman of the Board and CEO, in managing the day-to-day operation of the Company. In February 2005, he joined the Company as the Chief Strategy and Investment Officer of the Company, and was responsible for corporate strategies, investments, merger and acquisitions and investor relations. Prior to joining the Company, Mr Lau was an executive director at Goldman Sachs (Asia) LLC's investment banking division and the Chief Operating Officer of its Telecom, Media and Technology Group. Prior to that, he worked at McKinsey & Company, Inc. as a management consultant. Mr Lau received a Bachelor of Science Degree in Electrical Engineering from the University of Michigan, a Master of Science Degree in Electrical Engineering from Stanford University and a MBA from Kellogg Graduate School of Management, Northwestern University. On 28 July 2011, Mr Lau was appointed as a non-executive director of Kingsoft Corporation Limited, an Internet based software developer, distributor and software service provider listed in Hong Kong. The annual base salary of Mr Lau has been changed to USD571,300 in 2012 which was covered by the current service contract with the Company and the basis of determining his emoluments including the base salary and bonus as set out in the service contract remained the same.

Zhang Zhidong, age 40, is an executive director and Chief Technology Officer of the Company. Mr Zhang has overall responsibilities for the development of our proprietary technologies, including the basic IM platform and massive-scale online application systems. Mr Zhang is one of the core founders and has been employed by the Group since 1999. Prior to his current employment, Mr Zhang worked at Liming Network Group focusing on software and network application systems research and development. Mr Zhang has a Bachelor of Science degree specialising in Computer & its Application obtained in 1993 from Shenzhen University and a Master's degree in Computer Application and System Structure from South China University of Technology obtained in 1996. Mr Zhang has more than 15 years of experience in the telecommunications and Internet industries. He is also a director of Best Update International Limited which holds shares of the Company. Mr Zhang is entitled to an annual base salary of RMB2,971,800 in 2012 which was covered by the current service contract with the Company and the basis of determining his emoluments including the base salary and bonus as set out in the service contract remained the same.

Charles St Leger Searle, age 48, has been a non-executive director since 5 June 2001. Mr Searle is currently the Chief Investment Officer of MIH Internet group companies. Prior to joining the MIH group companies, he held various corporate finance positions at Cable & Wireless plc and Hong Kong Telecom. Prior to joining Cable & Wireless plc, he was a senior corporate finance manager at Deloitte & Touche in London and Sydney. Currently, Mr Searle serves on the boards of directors of a number of companies that are subsidiaries of or associated companies with MIH. Mr Searle graduated from the University of Cape Town in 1987 with a Bachelor of Commerce degree and is a member of the Institute of Chartered Accountants in Australia (1992). Mr Searle has more than 18 years of experience in the telecommunications and Internet industries. Mr Searle as a non-executive director is not entitled to any director's fee or emoluments.

Li Dong Sheng, age 55, has been an independent non-executive director since April 2004. Mr Li is the Chairman and CEO of TCL Corporation, the Chairman of the Hong Kong listed TCL Multimedia Technology Holdings Limited and the Chairman of the Hong Kong listed TCL Communication Technology Holdings Limited, all of which produce consumer electronic products. Mr Li graduated from South China University of Technology in 1982 with a Bachelor degree in radio technology and has more than 17 years of experience in the information technology field. Mr Li is entitled to a director's fee of HKD450,000 per annum for the year 2012, which is determined with reference to his duties and responsibilities with the Company.

Other Information

Iain Ferguson Bruce, age 71, has been an independent non-executive director since April 2004. Mr Bruce joined KPMG in Hong Kong in 1964 and was elected to its partnership in 1971. He was the Senior Partner of KPMG from 1991 until his retirement in 1996 and served as Chairman of KPMG Asia Pacific from 1993 to 1997. Since 1964, Mr Bruce has been a member of the Institute of Chartered Accountants of Scotland and is a fellow of the Hong Kong Institute of Certified Public Accountants, with over 47 years' experience in the accounting profession. He is also a fellow of The Hong Kong Institute of Directors and a member of The Hong Kong Securities Institute. Mr Bruce is currently an independent non-executive director of Goodbaby International Holdings Limited, a manufacturer of durable juvenile products, Paul Y. Engineering Group Limited, a construction and engineering services company, Sands China Ltd., an operator of integrated resorts and casinos, Vitasoy International Holdings Limited, a beverage manufacturing company, and Wing On Company International Limited, a department store operating and real property investment company; all of these companies are publicly listed companies in Hong Kong. Mr Bruce is also a non-executive director of Noble Group Limited, a commodity trading company that is publicly listed in Singapore, of China Medical Technologies, Inc., a China-based medical device company that is listed on NASDAQ, and of Yingli Green Energy Holding Company Limited, a China-based vertically integrated photovoltaic product manufacturer that is listed on the New York Stock Exchange. Mr Bruce is an independent non-executive director of Citibank (Hong Kong) Limited and is the Chairman of KCS Limited. The director's fee of Mr Bruce has been changed to HKD800,000 per annum for the year 2012, which is determined with reference to his duties and responsibilities with the Company.

Ian Charles Stone, age 61, has been an independent non-executive director since April 2004. Mr Stone is currently an Advisor on International Projects for PCCW Limited and CEO of SITC (a PCCW joint venture) in Saudi Arabia. Since 2001 in PCCW he has been CEO of UK Broadband in UK and then PCCW Mobile in Hong Kong, followed by being the Managing Director of the International Projects business. Mr Stone has more than 41 years of experience in the telecom and mobile industries. He was the CEO of SmarTone between 1999 and 2001 prior to which held various senior positions in telecom businesses of the First Pacific Group in Hong Kong and Philippines. Mr Stone has also held senior positions at Cable & Wireless plc and Hong Kong Telecom, including as Managing Director of CSL and Commercial Director of Hong Kong Telecom. Mr Stone is a fellow member of the Hong Kong Institute of Directors. The director's fee of Mr Stone has been changed to HKD550,000 per annum for the year 2012, which is determined with reference to his duties and responsibilities with the Company.

Other Information

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2012, the following persons, other than the directors or chief executive of the Company, had an interest or short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO as recorded in the register required to be kept by the Company under section 336 of the SFO, or who was, directly or indirectly, interested in 5% or more of the issued share capital of the Company:

LONG AND SHORT POSITIONS IN THE SHARES OF THE COMPANY

Name of shareholder	Long/short position	Nature of interest	Number of shares held	Percentage of issued share capital
MIH TC	Long position	Corporate (Note 1)	630,240,380	34.18%
Advance Data Services Limited	Long position	Corporate (Note 2)	189,892,880	10.30%
JPMorgan Chase & Co.	Long position	Beneficial owner	13,276,638	
		Investment manager	20,153,213	
		Custodian corporation/ Approved lending agent	<u>58,797,939</u>	
		Total (Note 3(i))	92,227,790	5.00%
	Short position	Beneficial owner (Note 3(ii))	7,100,066	0.39%

Notes:

- As MIH TC is controlled by Naspers Limited through its wholly-owned intermediary companies, MIH (Mauritius) Limited and MIH Holdings Limited. Naspers Limited, MIH (Mauritius) Limited and MIH Holdings Limited are deemed to be interested in the same block of 630,240,380 shares under Part XV of the SFO.
- As Advance Data Services Limited is wholly owned by Ma Huateng, Mr Ma has interest in these shares as disclosed under the section of "Directors' Interests in Securities".
- Such long position includes derivative interests in 4,998,986 underlying shares of the Company of which (a) 1,402,400 underlying shares are derived from listed and physically settled derivatives; (b) 1,634,000 underlying shares are derived from listed and cash settled derivatives; (c) 1,317,800 underlying shares are derived from unlisted and physically settled derivatives; and (d) 644,786 underlying shares are derived from unlisted and cash settled derivatives. It also includes 58,797,939 shares in lending pool.
 - Such short position includes derivative interests in 3,385,066 underlying shares of the Company of which (a) 507,700 underlying shares are derived from listed and physically settled derivatives; (b) 721,500 underlying shares are derived from listed and cash settled derivatives; (c) 1,870,250 underlying shares are derived from unlisted and physically settled derivatives; and (d) 285,616 underlying shares are derived from unlisted and cash settled derivatives.

Other Information

Save as disclosed above, the Company had not been notified of any other persons (other than a director or chief executive of the Company) who, as at 30 June 2012, had an interest or short position in the shares and underlying shares in the Company as recorded in the register required to be kept under section 336 of the SFO.

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

During the six months ended 30 June 2012, the Company repurchased 154,400 shares on the Stock Exchange for an aggregate consideration of approximately HKD25 million before expenses. The repurchased shares were subsequently cancelled. The repurchases were effected by the Board for the enhancement of shareholder value in the long term. Details of the shares repurchased are as follows:

Month of purchase in the six months ended 30 June 2012	No. of shares purchased	Purchase consideration per share		Aggregate consideration paid HKD
		Highest price paid HKD	Lowest price paid HKD	
		January	128,400	
May	26,000	205.0	204.4	5,326,269
Total:	154,400			24,909,067

Save as disclosed above, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares during the six months ended 30 June 2012.

EMPLOYEE AND REMUNERATION POLICIES

As at 30 June 2012, the Group had 20,000 employees (30 June 2011: 12,904). The number of employees employed by the Group varies from time to time depending on needs and employees are remunerated based on industry practice.

The remuneration policy and package of the Group's employees are periodically reviewed. Apart from pension funds and in-house training programs, discretionary bonuses, share awards and share options may be awarded to employees according to the assessment of individual performance.

The total remuneration cost (including capitalised remuneration cost) incurred by the Group for the six months ended 30 June 2012 was RMB3,598 million (for the six months ended 30 June 2011: RMB2,214 million).

Other Information

AUDIT COMMITTEE

The Audit Committee has reviewed the accounting principles and practices adopted by the Company and discussed auditing, internal control and financial reporting matters. The Audit Committee, together with the Auditor, has reviewed the Group's unaudited Interim Financial Information for the three and six months ended 30 June 2012.

ADOPTION OF CODE OF CONDUCT REGARDING DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding directors' securities transactions on terms no less exacting than the required standard set out in the Model Code. The directors of the Company have complied with such code of conduct throughout the accounting periods covered by this interim report.

COMPLIANCE WITH THE CORPORATE GOVERNANCE CODE

Code provision A.4.2 of the CG Code provides that every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years. According to the Articles of Association, one-third of the directors for the time being (or, if their number is not a multiple of three, the number nearest to but not greater than one-third) shall retire from office by rotation, provided that the chairman of the Board shall not, whilst holding such office, be subject to retirement by rotation or be taken into account in determining the number of directors to retire in each year. In compliance with the provisions in the Articles of Association, at the 2012 AGM, two directors retired and were re-elected and the re-election of Ian Charles Stone, who was re-elected in 2009, was not considered at the 2012 AGM and his re-election will be considered at subsequent annual general meeting. Code provision A.4.2 regarding the retirement of director by rotation at least once every three years was deviated.

The Board considered that the continuing compliance with the existing provision of retirement and re-election of director in the Articles of Association, which have been in operation for several years, shall not have a material impact on the operation of the Company as a whole. Notwithstanding the above, the Board will review the current provisions in the Articles of Association from time to time and shall make necessary amendments at the appropriate time.

Save as disclosed above and those disclosed in the 2011 annual report of the Company, none of the directors of the Company is aware of any information which would reasonably indicate that the Company has not complied with the code provisions of the Code on Corporate Governance Practices during the period from 1 January 2012 to 31 March 2012 and the CG Code during the period from 1 April 2012 to 30 June 2012.

As to the deviation from code provisions A.2.1 and A.4.2 of the CG Code, the Board will continue to review the current structure from time to time and shall make necessary changes when appropriate and inform the shareholders accordingly.

Definition

In this interim report, unless the context otherwise requires, the following expressions shall have the following meanings:

Term	Definition
“2012 AGM”	the annual general meeting of the Company held on 16 May 2012
“Articles of Association”	the articles of association of the Company
“Audit Committee”	the audit committee of the Company
“Auditor”	PricewaterhouseCoopers, the auditor of the Company
“Awarded Person”	a person who is eligible to participate in the Share Award Scheme
“Awarded Shares”	the shares of the Company awarded under the Share Award Scheme
“Board”	the board of directors of the Company
“CEO”	chief executive officer
“CG Code”	the Corporate Governance Code set out in Appendix 14 to the Listing Rules
“CIT”	corporate income tax
“Company”	Tencent Holdings Limited, a limited liability company organised and existing under the laws of the Cayman Islands and the shares of which are listed on the Stock Exchange
“DAU”	daily active user accounts
“DNF”	Dungeon and Fighter
“EBITDA”	earnings before interest, tax, depreciation and amortisation
“EPS”	earnings per share
“GAAP”	Generally Accepted Accounting Principles
“GMV”	gross merchandise volume
“Group”	the Company and its subsidiaries
“HKD”	the lawful currency of Hong Kong
“Hong Kong”	the Hong Kong Special Administrative Region, the PRC

Definition

Term	Definition
“IFRS”	International Financial Reporting Standards
“IM”	instant messaging
“IPO”	initial public offering
“IVAS”	Internet value-added services
“LIBOR”	London Interbank Offered Rate
“Listing Rules”	the Rules Governing the Listing of Securities on the Stock Exchange
“Main Board”	the main board of the Stock Exchange
“MAU”	monthly active user accounts
“MIH TC”	MIH TC Holdings Limited
“Model Code”	the Model Code for Securities Transactions by Directors of Listed Companies set out in Appendix 10 to the Listing Rules
“MVAS”	mobile and telecommunications value-added services
“PCU”	peak concurrent user accounts
“Post-IPO Option Scheme I”	the Post-IPO Share Option Scheme adopted by the Company on 24 March 2004
“Post-IPO Option Scheme II”	the Post-IPO Share Option Scheme adopted by the Company on 16 May 2007
“Post-IPO Option Scheme III”	the Post-IPO Share Option Scheme adopted by the Company on 13 May 2009
“PRC” or “China”	the People’s Republic of China
“Pre-IPO Option Scheme”	the Pre-IPO Share Option Scheme adopted by the Company on 27 July 2001
“Riot Games”	Riot Games, Inc.
“Riot Games Acquisition”	the acquisition of a majority interest in Riot Games by the Group from the existing shareholders, including the founders of Riot Games
“RMB”	the lawful currency of the PRC

Definition

Term	Definition
“ROI”	return on investment
“SFO”	the Securities and Futures Ordinance (Cap 571 of the Laws of Hong Kong) as amended, supplemented or otherwise modified from time to time
“Share Award Scheme”	the share award scheme adopted by the Company on 13 December 2007
“Shiji Kaixuan”	Shenzhen Shiji Kaixuan Technology Company Limited
“SMS”	short message service
“SNS”	social networking service
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“Tencent Charity Fund”	a charity fund established by the Group
“Tencent Computer”	Shenzhen Tencent Computer Systems Company Limited
“United States”	the United States of America
“USD”	the lawful currency of the United States

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