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Tencent 腾讯
TENCENT HOLDINGS LIMITED
騰訊控股有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 700)

ANNOUNCEMENT OF THE RESULTS
FOR THE THREE AND SIX MONTHS ENDED 30 JUNE 2010

The board of directors (the “Board”) of Tencent Holdings Limited (the “Company”) is pleased to announce the unaudited consolidated results of the Company and its subsidiaries (collectively, the “Group”) for the three and six months ended 30 June 2010. These interim results have been reviewed by PricewaterhouseCoopers, the auditors of the Company (the “Auditors”), in accordance with International Standard on Review Engagements 2410 “Review of interim financial information performed by the independent auditor of the entity” issued by the International Auditing and Assurance Standards Board, and by the audit committee of the Company (the “Audit Committee”), comprising a majority of the independent non-executive directors of the Company.

FINANCIAL INFORMATION

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2010

		Unaudited 30 June 2010 RMB'000	Audited 31 December 2009 RMB'000
ASSETS			
Non-current assets			
Fixed assets		2,822,058	2,517,202
Construction in progress		179,678	105,771
Investment properties		67,613	68,025
Land use rights		232,248	35,296
Intangible assets		265,961	268,713
Investment in associates		799,982	477,622
Deferred income tax assets		272,708	301,016
Held-to-maturity investments		—	341,410
Available-for-sale financial assets		2,284,894	153,462
Prepayments, deposits and other assets		<u>423,749</u>	<u>80,306</u>
		<u>7,348,891</u>	<u>4,348,823</u>
Current assets			
Accounts receivable	3	1,710,749	1,229,436
Prepayments, deposits and other assets		401,819	373,642
Derivative financial instruments		17,578	—
Term deposits with initial term of over three months		7,422,082	5,310,168
Restricted cash	6(a)	1,214,493	200,000
Cash and cash equivalents		<u>6,486,312</u>	<u>6,043,696</u>
		<u>17,253,033</u>	<u>13,156,942</u>
Total assets		<u><u>24,601,924</u></u>	<u><u>17,505,765</u></u>

		Unaudited	Audited
		30 June	31 December
		2010	2009
	<i>Note</i>	RMB'000	RMB'000
EQUITY			
Equity attributable to the Company's equity holders			
Share capital		198	197
Share premium		1,352,114	1,244,425
Shares held for share award scheme		(236,114)	(123,767)
Share-based compensation reserve		924,309	703,563
Other reserves		90,238	(166,364)
Retained earnings		<u>13,449,624</u>	<u>10,520,453</u>
		15,580,369	12,178,507
Non-controlling interests		<u>60,174</u>	<u>120,146</u>
Total equity		<u>15,640,543</u>	<u>12,298,653</u>
LIABILITIES			
Non-current liabilities			
Deferred income tax liabilities		481,517	369,983
Long-term payables		<u>—</u>	<u>274,050</u>
		<u>481,517</u>	<u>644,033</u>
Current liabilities			
Accounts payable	5	1,028,726	696,511
Other payables and accruals		1,994,316	1,626,051
Short-term bank borrowings	6	2,755,116	202,322
Current income tax liabilities		358,733	85,216
Other tax liabilities		173,308	216,978
Deferred revenue		<u>2,169,665</u>	<u>1,736,001</u>
		<u>8,479,864</u>	<u>4,563,079</u>
Total liabilities		<u>8,961,381</u>	<u>5,207,112</u>
Total equity and liabilities		<u>24,601,924</u>	<u>17,505,765</u>
Net current assets		<u>8,773,169</u>	<u>8,593,863</u>
Total assets less current liabilities		<u>16,122,060</u>	<u>12,942,686</u>

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE THREE AND SIX MONTHS ENDED 30 JUNE 2010**

		Unaudited		Unaudited	
		Three months ended		Six months ended	
		30 June		30 June	
		2010	2009	2010	2009
<i>Note</i>		<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Revenues					
		3,581,976	2,156,468	6,969,353	4,061,031
	Internet value-added services				
	Mobile and telecommunications				
	value-added services	674,120	470,003	1,292,358	909,548
	Online advertising	397,520	243,044	601,854	389,607
	Others	15,564	8,908	31,675	22,602
		4,669,180	2,878,423	8,895,240	5,382,788
	Cost of revenues	8 (1,482,939)	(934,613)	8 (2,811,294)	(1,720,527)
	Gross profit	3,186,241	1,943,810	6,083,946	3,662,261
	Interest income	54,005	27,520	111,196	61,569
	Other gains/(losses), net	7 27,415	(2,192)	7 (7,860)	(37,012)
	Selling and marketing expenses	8 (230,340)	(114,587)	8 (415,757)	(212,692)
	General and administrative expenses	8 (665,961)	(455,629)	8 (1,251,727)	(910,647)
	Operating profit	* 2,371,360	1,398,922	* 4,519,798	2,563,479
	Finance costs	(2,976)	(653)	(4,534)	(405)
	Share of profit of associates	11,334	3,452	24,247	8,824
	Profit before income tax	2,379,718	1,401,721	4,539,511	2,571,898
	Income tax expense	9 (448,525)	(199,973)	9 (805,900)	(316,540)
	Profit/Total comprehensive income for the period	1,931,193	1,201,748	3,733,611	2,255,358
	Attributable to:				
	Equity holders of the Company	1,916,502	1,192,410	3,699,696	2,227,850
	Non-controlling interests	14,691	9,338	33,915	27,508
		1,931,193	1,201,748	3,733,611	2,255,358

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2010	2009	2010	2009
<i>Note</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>

**Earnings per share for profit
attributable to equity holders of
the Company during the period
(expressed in RMB per share)**

- basic	10	<u>1.054</u>	<u>0.662</u>	<u>2.039</u>	<u>1.239</u>
- diluted	10	<u>1.031</u>	<u>0.647</u>	<u>1.990</u>	<u>1.213</u>

* After deduction of share-based compensation charge amounting to RMB119,599,000 for the three months ended 30 June 2010 (for the three months ended 30 June 2009: RMB53,904,000) and RMB220,571,000 for the six months ended 30 June 2010 (for the six months ended 30 June 2009: RMB103,238,000).

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE SIX MONTHS ENDED 30 JUNE 2010

Unaudited									
Attributable to equity holders of the Company									
	Share capital	Share premium	Shares held for share award scheme	Share-based compensation reserve	Other reserves	Retained earnings	Total	Non- controlling interests	Total equity
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Balance at 1 January 2010	197	1,244,425	(123,767)	703,563	(166,364)	10,520,453	12,178,507	120,146	12,298,653
Profit/Total comprehensive income for the period	-	-	-	-	-	3,699,696	3,699,696	33,915	3,733,611
Employee share option schemes:									
- value of employee services	-	-	-	62,689	-	-	62,689	-	62,689
- proceeds from shares issued	1	110,721	-	-	-	-	110,722	-	110,722
Employee share award scheme:									
- value of employee services	-	-	-	158,057	-	-	158,057	-	158,057
- shares purchased for share award scheme	-	-	(115,379)	-	-	-	(115,379)	-	(115,379)
- vesting of awarded shares	-	(3,032)	3,032	-	-	-	-	-	-
Profit appropriations to statutory reserves	-	-	-	-	6,083	(6,083)	-	-	-
Dividends	-	-	-	-	-	(639,264)	(639,264)	(62,792)	(702,056)
Reversal of liabilities in respect of put options granted to non-controlling interests owners	-	-	-	-	94,246	-	94,246	-	94,246
Acquisition of additional interests in a subsidiary	-	-	-	-	156,273	(125,178)	31,095	(31,095)	-
Balance at 30 June 2010	198	1,352,114	(236,114)	924,309	90,238	13,449,624	15,580,369	60,174	15,640,543
Balance at 1 January 2009	195	1,155,209	(21,809)	381,439	(433,038)	5,938,930	7,020,926	98,406	7,119,332
Profit/Total comprehensive income for the period	-	-	-	-	-	2,227,850	2,227,850	27,508	2,255,358
Employee share option schemes:									
- value of employee services	-	-	-	86,674	-	-	86,674	-	86,674
- proceeds from shares issued	1	82,813	-	-	-	-	82,814	-	82,814
Employee share award scheme:									
- value of employee services	-	-	-	17,026	-	-	17,026	-	17,026
- shares purchased for share award scheme	-	-	(24,423)	-	-	-	(24,423)	-	(24,423)
Repurchase and cancellation of shares	-	(74,570)	-	-	-	-	(74,570)	-	(74,570)
Profit appropriations to statutory reserves	-	-	-	-	1,417	(1,417)	-	-	-
Dividends	-	-	-	-	-	(554,604)	(554,604)	(23,020)	(577,624)
Balance at 30 June 2009	196	1,163,452	(46,232)	485,139	(431,621)	7,610,759	8,781,693	102,894	8,884,587

**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE SIX MONTHS ENDED 30 JUNE 2010**

	Unaudited	
	Six months ended 30 June	
	2010	2009
	<i>RMB'000</i>	<i>RMB'000</i>
Net cash flows generated from operating activities	5,027,992	3,531,851
Net cash flows used in investing activities	(6,427,813)	(1,944,788)
Net cash flows from/(used in) financing activities	<u>1,846,080</u>	<u>(593,803)</u>
Net increase in cash and cash equivalents	446,259	993,260
Cash and cash equivalents at beginning of period	6,043,696	3,067,928
Exchange losses on cash and cash equivalents	<u>(3,643)</u>	<u>(166)</u>
Cash and cash equivalents at end of period	<u><u>6,486,312</u></u>	<u><u>4,061,022</u></u>
Analysis of balances of cash and cash equivalents:		
Bank balances and cash	3,255,633	1,742,385
Short-term highly liquid investments with initial term of three months or less	<u>3,230,679</u>	<u>2,318,637</u>
	<u><u>6,486,312</u></u>	<u><u>4,061,022</u></u>

1 General information, basis of preparation and presentation

The Company was incorporated in the 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 Group is principally engaged in the provision of Internet value-added services, mobile and telecommunications value-added services and online advertising services to users in the People’s Republic of China (the “PRC”).

The consolidated statement of financial position as at 30 June 2010, the related 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 11 August 2010.

The Interim Financial Information is prepared in accordance with International Accounting Standard (“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 2009 (the “2009 Financial Statements”) as set out in the 2009 annual report of the Company dated 17 March 2010.

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 2009 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 earnings.

The following new standards and amendments to existing standards have been published and are mandatory for the financial year beginning 1 January 2010, are relevant to the Group:

IAS 27 (Revised)	Consolidated and Separate Financial Statements
IFRS 2 (Amendment)	Group Cash-settled Share-based Payment Transaction
IFRS 3 (Revised)	Business Combinations

The Group has applied IAS 27 (Revised), IFRS 2 (Amendment) and IFRS 3 (Revised) and management has considered that these amendments have no significant impact on the Interim Financial Information.

2 Segment information

The Group has the following reportable segments for the three and six months ended 30 June 2010 and 2009:

- Internet value-added services;
- Mobile and telecommunications value-added services;
- Online advertising; and
- Others.

Other segments of the Group are mainly comprised of the provision of online payment services and trademark licensing.

There were no inter-segment sales during the three and six months ended 30 June 2010 and 2009.

The segment information provided to the executive directors for the reportable segments for the three and six months ended 30 June 2010 and 2009 is as follows:

	Unaudited				
	Three months ended 30 June 2010				
	Internet	Mobile and	Online	Others	Total
	value-added	telecommunications	advertising	Others	Total
	services	value-added	services	advertising	Others
	RMB'000	services	RMB'000	RMB'000	RMB'000
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Segment revenues (revenues from external customers)	<u>3,581,976</u>	<u>674,120</u>	<u>397,520</u>	<u>15,564</u>	<u>4,669,180</u>
Gross profit/(loss)	<u>2,481,944</u>	<u>432,026</u>	<u>280,092</u>	<u>(7,821)</u>	<u>3,186,241</u>
Depreciation	86,361	8,737	4,718	3,346	103,162
Amortisation	13,385	–	–	–	13,385
Share of profit of associates	<u>10,655</u>	<u>679</u>	<u>–</u>	<u>–</u>	<u>11,334</u>

Unaudited					
Three months ended 30 June 2009					
	Internet	Mobile and	Online	Others	Total
	value-added	telecommunications	advertising		
	services	value-added			
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Segment revenues (revenues from external customers)	<u>2,156,468</u>	<u>470,003</u>	<u>243,044</u>	<u>8,908</u>	<u>2,878,423</u>
Gross profit/(loss)	<u>1,491,313</u>	<u>290,422</u>	<u>169,621</u>	<u>(7,546)</u>	<u>1,943,810</u>
Depreciation	28,021	3,786	1,279	1,369	34,455
Amortisation	16,915	—	—	—	16,915
Share of profit of associates	<u>2,415</u>	<u>1,037</u>	<u>—</u>	<u>—</u>	<u>3,452</u>

Unaudited					
Six months ended 30 June 2010					
	Internet	Mobile and	Online	Others	Total
	value-added	telecommunications	advertising		
	services	value-added			
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Segment revenues (revenues from external customers)	<u>6,969,353</u>	<u>1,292,358</u>	<u>601,854</u>	<u>31,675</u>	<u>8,895,240</u>
Gross profit/(loss)	<u>4,856,393</u>	<u>828,918</u>	<u>413,483</u>	<u>(14,848)</u>	<u>6,083,946</u>
Depreciation	153,935	15,224	8,266	6,000	183,425
Amortisation	30,677	—	—	—	30,677
Share of profit of associates	<u>20,361</u>	<u>3,886</u>	<u>—</u>	<u>—</u>	<u>24,247</u>

	Unaudited				
	Six months ended 30 June 2009				
	Internet	Mobile and	Online	Others	Total
	value-added	telecommunications	advertising		
	services	value-added			
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Segment revenues (revenues from external customers)	<u>4,061,031</u>	<u>909,548</u>	<u>389,607</u>	<u>22,602</u>	<u>5,382,788</u>
Gross profit/(loss)	<u>2,851,252</u>	<u>560,907</u>	<u>264,183</u>	<u>(14,081)</u>	<u>3,662,261</u>
Depreciation	53,614	7,576	2,415	2,509	66,114
Amortisation	40,611	—	—	—	40,611
Share of profit of associates	<u>3,899</u>	<u>4,925</u>	<u>—</u>	<u>—</u>	<u>8,824</u>

3 Accounts receivable

	Unaudited	Audited
	30 June	31 December
	2010	2009
	<i>RMB'000</i>	<i>RMB'000</i>
0 - 30 days	981,461	690,858
31 days - 60 days	215,196	173,331
61 days - 90 days	152,200	112,752
Over 90 days but less than a year	<u>361,892</u>	<u>252,495</u>
	<u>1,710,749</u>	<u>1,229,436</u>

Receivable balances as at 30 June 2010 mainly represented amounts due from telecommunication operators, including China Mobile, China Unicom, China Telecom and their respective branches, subsidiaries and affiliates, as well as online advertising customers located in the PRC.

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

4 Share option and share award schemes

(a) Share option schemes

The Company has adopted several share option schemes for the purpose of providing incentives and rewards to its directors, executives or officers, employees, consultants and other eligible persons:

(i) *Pre-IPO Share Option Scheme (the “Pre-IPO Option Scheme”)*

On 27 July 2001, the Pre-IPO Option Scheme was adopted by the Company. As at the listing of the Company on 16 June 2004, all options under the Pre-IPO Option Scheme had been granted.

(ii) *Post-IPO Share Option Scheme I (the “Post-IPO Option Scheme I”)*

On 24 March 2004, the Company adopted the Post-IPO Option Scheme I. This was terminated upon the adoption of the Post-IPO Share Option Scheme II (the “Post-IPO Option Scheme II”) as mentioned below.

(iii) *Post-IPO Option Scheme II*

On 16 May 2007, the Company adopted the Post-IPO Option Scheme II. Pursuant to the Post-IPO Option Scheme II, the Board may, at its discretion, grant options to any eligible person to subscribe for shares in the Company. The Post-IPO Option Scheme II shall be valid and effective for a period of ten years commencing on its date of adoption.

(iv) *Post-IPO Share Option Scheme III (the “Post-IPO Option Scheme III”)*

On 13 May 2009, the Company adopted the Post-IPO Option Scheme III. Pursuant to the Post-IPO Option Scheme III, the Board may, at its discretion, grant options to any eligible person (any senior executive or senior officer, director of any member of the Group or any invested entity and any consultant, advisor or agent of any member of the Board) to subscribe for shares in the Company. The Post-IPO Option Scheme III shall be valid and effective for a period of ten years commencing on its date of adoption.

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 2009	USD0.0964	4,124,083	HKD10.4762	37,615,536	HKD41.2330	28,715,506	–	–	70,455,125
Granted	–	–	–	–	HKD48.0100	380,000	–	–	380,000
Exercised	USD0.1435	(1,375,675)	HKD8.1223	(7,860,636)	HKD37.0514	(771,474)	–	–	(10,007,785)
Lapsed	USD0.0497	<u>(254,080)</u>	HKD8.8487	<u>(329,029)</u>	HKD48.3206	<u>(346,393)</u>	–	–	<u>(929,502)</u>
At 30 June 2009	USD0.0752	<u>2,494,328</u>	HKD11.1232	<u>29,425,871</u>	HKD41.3526	<u>27,977,639</u>	–	–	<u>59,897,838</u>
Currently exercisable as at 30 June 2009	USD0.0752	<u>2,494,328</u>	HKD9.4056	<u>14,952,621</u>	HKD37.0696	<u>2,504,950</u>	–	–	<u>19,951,899</u>
At 1 January 2010	USD0.0812	1,865,068	HKD11.5050	24,941,918	HKD45.1756	28,991,419	–	–	55,798,405
Granted	–	–	–	–	HKD158.5000	750,000	HKD158.5000	1,000,000	1,750,000
Exercised	USD0.0732	(1,068,900)	HKD9.5604	(8,964,204)	HKD40.9064	(968,471)	–	–	(11,001,575)
Lapsed	–	–	HKD17.9514	<u>(210,202)</u>	HKD55.1520	<u>(148,226)</u>	–	–	<u>(358,428)</u>
At 30 June 2010	USD0.0920	<u>796,168</u>	HKD12.5246	<u>15,767,512</u>	HKD48.2376	<u>28,624,722</u>	HKD158.5000	<u>1,000,000</u>	<u>46,188,402</u>
Currently exercisable as at 30 June 2010	USD0.0920	<u>796,168</u>	HKD10.5815	<u>12,450,172</u>	HKD39.1929	<u>5,215,620</u>	–	–	<u>18,461,960</u>

During the six months ended 30 June 2010, 1,000,000 share options (during the six months ended 30 June 2009: Nil) were granted to an executive director of the Company.

(b) **Share award scheme**

On 13 December 2007, the Company adopted a share award scheme (the “Share Scheme”). The Share Scheme was subsequently amended on 31 January 2008 and 13 May 2009, respectively. The Board may, at its absolute discretion, select any eligible person to participate in the Share Scheme.

Movements in the number of shares held for the Share Scheme and awarded shares for the six months ended 30 June 2010 and 2009 are as follows:

	Shares held for the Share Scheme	Awarded shares
At 1 January 2009	132,160	1,349,450
Purchased	383,100	—
Granted	(145,700)	145,700
Cancelled	<u>(132,080)</u>	<u>—</u>
At 30 June 2009	<u>237,480</u>	<u>1,495,150</u>
Currently exercisable as at 30 June 2009		<u>13,542</u>
At 1 January 2010	10	10,411,424
Purchased (<i>Note</i>)	814,283	—
Granted	(802,293)	802,293
Vested	<u>—</u>	<u>(88,910)</u>
At 30 June 2010	<u>12,000</u>	<u>11,124,807</u>
Currently exercisable as at 30 June 2010		<u>206,959</u>

Note:

During the six months ended 30 June 2010, 814,283 shares were acquired through an independent trustee at a consideration of approximately HKD131,250,000 (equivalent to approximately RMB115,379,000).

During the six months ended 30 June 2010, no awarded shares (during the six months ended 30 June 2009: Nil) were granted to any director of the Company.

5 Accounts payable

Accounts payable and their ageing analysis are as follows:

	Unaudited 30 June 2010 RMB'000	Audited 31 December 2009 RMB'000
0 - 30 days	555,754	493,013
31 days - 60 days	178,760	72,554
61 days - 90 days	135,965	82,525
Over 90 days but less than a year	<u>158,247</u>	<u>48,419</u>
	<u>1,028,726</u>	<u>696,511</u>

6 Short-term bank borrowings

	Unaudited 30 June 2010 RMB'000	Audited 31 December 2009 RMB'000
Secured (<i>Note (a)</i>)	1,193,209	202,322
Unsecured (<i>Note (b)</i>)	<u>1,561,907</u>	<u>—</u>
	<u>2,755,116</u>	<u>202,322</u>

Notes:

- (a) Bank borrowings as at 30 June 2010 were secured by a pledge of restricted cash of RMB1,214,493,000. The principal amount of the bank borrowings was USD178,412,000 and the interest rates were fixed at 1.06% to 2.99% per annum. The borrowings will be repaid in full in USD within one year. Concurrently, foreign exchange forward contracts were arranged with the same borrowing banks as at the respective borrowing dates in order to enable the Group to purchase the required amount of USD with RMB for settling the principal amount of the borrowings plus related interest upon the loan due dates. The bank borrowings and the foreign exchange forward contracts are deemed as linked transactions and, accordingly, the bank borrowings have effectively been accounted for as borrowings denominated in RMB.

These bank borrowings and the forward contracts were transacted on the belief that, despite the associated interest expenses, the Group would benefit from the interest income from the restricted cash and the fixed exchange gains arising from the bank borrowings which are calculated as the difference between the forward rate stated in the contracts and the respective spot rates at the borrowing dates.

- (b) These bank borrowings are also denominated in USD. The aggregate principal amount was USD230,000,000 and the interest rates were fixed at 1.63% to 1.90% per annum. In addition, the Group entered into foreign forward contracts to purchase the required amount of USD with RMB for settling the principal amount of the borrowings upon the due dates. However, the Group transacted with different banks for the bank loans and the forward contracts, and the Group did not adopt hedge accounting. As a result, these bank borrowings and relevant foreign forward contracts were accounted for separately (i.e. these 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 gains/(losses), net” of consolidated statement of comprehensive income.

The fair value of the short-term bank borrowings approximate to their carrying amounts as at 30 June 2010.

7 **Other gains/(losses), net**

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2010	2009	2010	2009
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Fair value gains on financial assets held for trading	–	11,929	–	11,929
Gains from derivative financial instruments	17,578	–	17,578	–
Government subsidies	12,871	17,039	13,534	20,580
Donation to a charity fund established by the Group	–	(25,000)	(40,000)	(55,000)
Others	(3,034)	(6,160)	1,028	(14,521)
	<u>27,415</u>	<u>(2,192)</u>	<u>(7,860)</u>	<u>(37,012)</u>

8 Expenses by nature

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2010	2009	2010	2009
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Employee benefit expenses (<i>Note</i>)	750,851	467,386	1,395,899	947,335
Mobile and telecom charges and bandwidth and server custody fees	515,081	395,204	990,204	751,429
Content costs and agency fees	634,080	349,689	1,191,954	573,519
Depreciation of fixed assets (<i>Note</i>)	159,761	94,003	294,592	181,435
Promotion and advertising expenses	132,767	49,730	237,324	95,643
Travelling and entertainment expenses	30,728	26,559	52,864	51,409
Operating lease rentals in respect of office buildings	21,497	24,335	40,549	48,814
Amortisation of intangible assets	30,184	31,196	63,095	69,193
Other expenses	104,291	66,727	212,297	125,089
Total cost of revenues, selling and marketing expenses and general and administrative expenses	<u>2,379,240</u>	<u>1,504,829</u>	<u>4,478,778</u>	<u>2,843,866</u>

Note:

Research and development expenses were RMB407,154,000 and RMB758,430,000 for the three and six months ended 30 June 2010, respectively (for the three and six months ended 30 June 2009: RMB264,582,000 and RMB535,855,000, respectively). The expenses included employee benefit expenses of RMB340,684,000 and depreciation of fixed assets of RMB48,840,000 for the three months ended 30 June 2010 (for the three months ended 30 June 2009: RMB201,278,000 and RMB56,276,000, respectively) and employee benefit expenses of RMB626,250,000 and depreciation of fixed assets of RMB97,509,000 for the six months ended 30 June 2010 (for the six months ended 30 June 2009: RMB414,564,000 and RMB109,357,000, respectively).

The Group did not capitalise any research and development expenses for the three and six months ended 30 June 2010 (for the three and six months ended 30 June 2009: Nil).

9 **Income tax expense**

Income tax expense is recognised based on management's best knowledge of the income tax rates expected for the financial year.

(a) **Cayman Islands and British Virgin Islands profits tax**

The Group has not been subject to any taxation in these jurisdictions for the three and six months ended 30 June 2010 and 2009.

(b) **Hong Kong profits tax**

No Hong Kong profits tax has been provided as the Group had no assessable profit arising in Hong Kong for the three and six months ended 30 June 2010 and 2009.

(c) **PRC corporate income tax ("CIT")**

CIT is provided on the assessable income 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 ("CIT Law"), the CIT for domestic and foreign enterprises has been unified at 25%, effective 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 date of promulgation of the CIT Law and which were entitled to preferential income tax rates under the then effective tax laws or regulations. Pursuant to the "Circular to Implementation of the Transitional Preferential Policies for the Corporate Income Tax", the transitional income tax 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 rate shall be based on the above transitional income tax rates for the respective years.

In 2008, six subsidiaries of the Group were approved as High/New Technology Enterprise, and accordingly, they were subject to a reduced preferential CIT rate of 15% according to the CIT Law. With such status, the above mentioned transitional income tax rates for the period from 2008 to 2010 are no longer applicable to them.

In addition, according to relevant tax circulars issued by PRC tax authorities, certain subsidiaries of the Company are exempt from CIT for either two or three years, in either case followed by a 50% reduction in tax rate for the next three years ("CIT Preferential Holiday"). The CIT Preferential Holiday commences either from the first year of commercial operations or from the first year of profitable operation after offsetting tax losses from prior years.

(d) **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 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 to 5% from 10%.

The income tax charges of the Group for the three and six months ended 30 June 2010 and 2009 are analysed as follows:

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2010	2009	2010	2009
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
PRC current tax	356,083	184,948	666,058	289,978
Deferred tax	<u>92,442</u>	<u>15,025</u>	<u>139,842</u>	<u>26,562</u>
	<u>448,525</u>	<u>199,973</u>	<u>805,900</u>	<u>316,540</u>

The tax on the Group's profit before income tax differs from the theoretical amount that would arise using the tax rate of 22% for the three and six months ended 30 June 2010 (for the three and six months ended 30 June 2009: 20%), the tax rate of the major subsidiaries of the Company before preferential tax treatments. The difference is analysed as follows:

	Unaudited Three months ended 30 June		Unaudited Six months ended 30 June	
	2010 RMB'000	2009 RMB'000	2010 RMB'000	2009 RMB'000
Profit before income tax	2,379,718	1,401,721	4,539,511	2,571,898
Less: Share of profit of associates	<u>(11,334)</u>	<u>(3,452)</u>	<u>(24,247)</u>	<u>(8,824)</u>
	<u>2,368,384</u>	<u>1,398,269</u>	<u>4,515,264</u>	<u>2,563,074</u>
Tax calculated at a tax rate of 22% (for the three and six months ended 30 June 2009: 20%)	521,044	279,654	993,358	512,615
Effects of different tax rates available to different companies of the Group	(61,617)	(29,390)	(165,428)	(69,957)
Effects of tax holiday on assessable profit of subsidiaries	(110,978)	(92,624)	(204,515)	(198,832)
Income not subject to tax	(5,258)	—	(5,258)	—
Expenses not deductible for tax purposes	31,692	28,372	49,916	39,304
Withholding tax on the earnings anticipated to be remitted by PRC subsidiaries	80,000	—	115,000	—
(Utilisation of previously unrecognised deferred tax assets)/Unrecognised deferred tax assets	<u>(6,358)</u>	<u>13,961</u>	<u>22,827</u>	<u>33,410</u>
Tax charge	<u>448,525</u>	<u>199,973</u>	<u>805,900</u>	<u>316,540</u>

10 Earnings per share

(a) Basic

Basic earnings per share (“EPS”) is 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		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2010	2009	2010	2009
Profit attributable to equity holders of the Company for the period (RMB'000)	<u>1,916,502</u>	<u>1,192,410</u>	<u>3,699,696</u>	<u>2,227,850</u>
Weighted average number of ordinary shares in issue (thousand shares)	<u>1,817,677</u>	<u>1,800,959</u>	<u>1,814,795</u>	<u>1,798,190</u>
Basic EPS (RMB per share)	<u><u>1.054</u></u>	<u><u>0.662</u></u>	<u><u>2.039</u></u>	<u><u>1.239</u></u>

(b) **Diluted**

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 diluted EPS). No adjustment is made to earnings (numerator).

	Unaudited		Unaudited	
	Three months ended		Six months ended	
	30 June		30 June	
	2010	2009	2010	2009
Profit attributable to equity holders of the Company for the period (RMB'000)	<u>1,916,502</u>	<u>1,192,410</u>	<u>3,699,696</u>	<u>2,227,850</u>
Weighted average number of ordinary shares in issue (thousand shares)	1,817,677	1,800,959	1,814,795	1,798,190
Adjustments for share options (thousand shares)	34,494	39,797	37,619	38,246
Adjustments for awarded shares (thousand shares)	<u>6,522</u>	<u>825</u>	<u>6,632</u>	<u>638</u>
Weighted average number of ordinary shares for the calculation of diluted EPS (thousand shares)	<u>1,858,693</u>	<u>1,841,581</u>	<u>1,859,046</u>	<u>1,837,074</u>
Diluted EPS (RMB per share)	<u>1.031</u>	<u>0.647</u>	<u>1.990</u>	<u>1.213</u>

11 **Dividend**

A final dividend in respect of the year ended 31 December 2009 of HKD0.40 per share (2008: HKD0.25 per share and a special dividend of HKD0.10 per share) was proposed pursuant to a resolution passed by the Board on 17 March 2010 and approved by shareholders in the annual general meeting on 12 May 2010. Such dividend, totalling approximately HKD727,180,000 (equivalent to RMB639,264,000) (final dividend for 2008: HKD629,802,000 (equivalent to RMB554,604,000)), had been paid as at 30 June 2010.

The Board did not propose any interim dividend.

OPERATING INFORMATION

The following table sets forth certain operating statistics relating to our Internet platforms and value-added services as at the dates and for the periods presented:

	As at 30 June 2010	As at 31 March 2010	Percentage change
	<i>(in millions)</i>		
Active IM user accounts	612.5	568.6	7.7%
Peak simultaneous online IM user accounts (for the quarter)	109.4	105.3	3.9%
Average daily IM user hours (for the last 15/16 days of the quarter)	1,713.8	1,546.7	10.8%
Active Qzone user accounts	458.5	428.0	7.1%
Peak simultaneous online QQ Game user accounts (for the quarter)	6.2	6.8	-8.8%
Fee-based Internet value-added services registered subscriptions	63.2	59.9	5.5%
Fee-based mobile and telecommunications value-added services registered subscriptions	24.1	23.3	3.4%

In the second quarter of 2010, the number of active users and peak simultaneous online user accounts for our IM platform recorded healthy growth. With the commencement of summer holiday for students towards the end of the quarter, as well as the increasing usage of our IM service on mobile devices, the growth of average daily user hours was higher than that of active users. Qzone's active user base further expanded during the quarter as our new social networking services ("SNS") applications gained popularity and as we launched promotional activities. Peak simultaneous online user accounts for QQ Game decreased, primarily due to fewer in-game promotions compared to the previous quarter and cannibalisation from social games. For our Internet value-added services, registered subscriptions increased, mainly driven by growth in QQ Membership and Qzone. Registered subscriptions to our mobile and telecommunications value-added services also increased, fueled by organic growth of our bundled SMS packages.

FINANCIAL PERFORMANCE HIGHLIGHTS

First Half of 2010

The following table sets forth the comparative figures for the first half of 2010 and the first half of 2009:

	Unaudited	
	Six months ended	
	30 June 2010	30 June 2009
	<i>RMB'000</i>	<i>RMB'000</i>
Revenues	8,895,240	5,382,788
Cost of revenues	<u>(2,811,294)</u>	<u>(1,720,527)</u>
Gross profit	6,083,946	3,662,261
Interest income	111,196	61,569
Other losses, net	(7,860)	(37,012)
Selling and marketing expenses	(415,757)	(212,692)
General and administrative expenses	<u>(1,251,727)</u>	<u>(910,647)</u>
Operating profit	4,519,798	2,563,479
Finance costs	(4,534)	(405)
Share of profit of associates	<u>24,247</u>	<u>8,824</u>
Profit before income tax	4,539,511	2,571,898
Income tax expense	<u>(805,900)</u>	<u>(316,540)</u>
Profit/Total comprehensive income for the period	<u><u>3,733,611</u></u>	<u><u>2,255,358</u></u>
Attributable to:		
Equity holders of the Company	3,699,696	2,227,850
Non-controlling interests	<u>33,915</u>	<u>27,508</u>
	<u><u>3,733,611</u></u>	<u><u>2,255,358</u></u>

Revenues. Revenues increased by 65.3% to RMB8,895.2 million for the first half of 2010 from RMB5,382.8 million for the first half of 2009.

	Unaudited			
	Six months ended			
	30 June 2010		30 June 2009	
	Amount	% of total revenues	Amount	% of total revenues
<i>(RMB in thousands, except percentages)</i>				
Internet value-added services	6,969,353	78.3%	4,061,031	75.5%
Mobile and telecommunications value-added services	1,292,358	14.5%	909,548	16.9%
Online advertising	601,854	6.8%	389,607	7.2%
Others	<u>31,675</u>	<u>0.4%</u>	<u>22,602</u>	<u>0.4%</u>
Total revenues	<u>8,895,240</u>	<u>100.0%</u>	<u>5,382,788</u>	<u>100.0%</u>

Cost of revenues. Cost of revenues increased by 63.4% to RMB2,811.3 million for the first half of 2010 from RMB1,720.5 million for the first half of 2009.

	Unaudited			
	Six months ended			
	30 June 2010		30 June 2009	
	Amount	% of segment revenues	Amount	% of segment revenues
<i>(RMB in thousands, except percentages)</i>				
Internet value-added services	2,112,960	30.3%	1,209,779	29.8%
Mobile and telecommunications value-added services	463,440	35.9%	348,641	38.3%
Online advertising	188,371	31.3%	125,424	32.2%
Others	<u>46,523</u>	<u>146.9%</u>	<u>36,683</u>	162.3%
Total cost of revenues	<u>2,811,294</u>		<u>1,720,527</u>	

Second Quarter of 2010

Unaudited consolidated revenues for the second quarter of 2010 were RMB4,669.2 million, an increase of 62.2% over the same period in 2009 and an increase of 10.5% from the first quarter of 2010.

Revenues from our Internet value-added services for the second quarter of 2010 were RMB3,582.0 million, an increase of 66.1% over the same period in 2009 and an increase of 5.7% from the first quarter of 2010.

Revenues from our mobile and telecommunications value-added services for the second quarter of 2010 were RMB674.1 million, an increase of 43.4% over the same period in 2009 and an increase of 9.0% from the first quarter of 2010.

Revenues from our online advertising business for the second quarter of 2010 were RMB397.5 million, an increase of 63.6% over the same period in 2009 and an increase of 94.5% from the first quarter of 2010.

Cost of revenues for the second quarter of 2010 was RMB1,482.9 million, an increase of 58.7% over the same period in 2009 and an increase of 11.6% from the first quarter of 2010.

Selling and marketing expenses for the second quarter of 2010 were RMB230.3 million, an increase of 101.0% over the same period in 2009 and an increase of 24.2% from the first quarter of 2010.

General and administrative expenses for the second quarter of 2010 were RMB666.0 million, an increase of 46.2% over the same period in 2009 and an increase of 13.7% from the first quarter of 2010.

Operating profit for the second quarter of 2010 was RMB2,371.4 million, representing an increase of 69.5% over the same period in 2009 and an increase of 10.4% from the first quarter of 2010. As a percentage of revenues, operating profit represented 50.8% for the second quarter of 2010, compared to 48.6% for the same period of 2009 and 50.8% for the first quarter of 2010.

Profit for the second quarter of 2010 was RMB1,931.2 million, representing an increase of 60.7% over the same period in 2009 and an increase of 7.1% from the first quarter of 2010. As a percentage of revenues, profit for the period represented 41.4% for the second quarter of 2010, compared to 41.8% for the same period of 2009 and 42.7% for the first quarter of 2010.

Profit attributable to equity holders of the Company for the second quarter of 2010 was RMB1,916.5 million, an increase of 60.7% over the same period in 2009 and an increase of 7.5% from the first quarter of 2010.

MANAGEMENT DISCUSSION AND ANALYSIS

Second Quarter of 2010 Compared to First Quarter of 2010

The following table sets forth the comparative figures for the second quarter of 2010 and the first quarter of 2010:

	Unaudited	
	Three months ended	
	30 June 2010	31 March 2010
	<i>RMB'000</i>	<i>RMB'000</i>
Revenues	4,669,180	4,226,060
Cost of revenues	<u>(1,482,939)</u>	<u>(1,328,355)</u>
Gross profit	3,186,241	2,897,705
Interest income	54,005	57,191
Other gains/(losses), net	27,415	(35,275)
Selling and marketing expenses	(230,340)	(185,417)
General and administrative expenses	<u>(665,961)</u>	<u>(585,766)</u>
Operating profit	2,371,360	2,148,438
Finance costs	(2,976)	(1,558)
Share of profit of associates	<u>11,334</u>	<u>12,913</u>
Profit before income tax	2,379,718	2,159,793
Income tax expense	<u>(448,525)</u>	<u>(357,375)</u>
Profit/Total comprehensive income for the period	<u><u>1,931,193</u></u>	<u><u>1,802,418</u></u>
Attributable to:		
Equity holders of the Company	1,916,502	1,783,194
Non-controlling interests	<u>14,691</u>	<u>19,224</u>
	<u><u>1,931,193</u></u>	<u><u>1,802,418</u></u>

Revenues. Revenues increased by 10.5% to RMB4,669.2 million for the second quarter of 2010 from RMB4,226.1 million for the first quarter of 2010. The following table sets forth our revenues by line of business for the second quarter of 2010 and the first quarter of 2010:

	Unaudited			
	Three months ended			
	30 June 2010		31 March 2010	
	% of total		% of total	
	Amount	revenues	Amount	revenues
	<i>(RMB in thousands, except percentages)</i>			
Internet value-added services	3,581,976	76.7%	3,387,377	80.2%
Mobile and telecommunications value-added services	674,120	14.4%	618,238	14.6%
Online advertising	397,520	8.5%	204,334	4.8%
Others	15,564	0.4%	16,111	0.4%
Total revenues	<u>4,669,180</u>	<u>100.0%</u>	<u>4,226,060</u>	<u>100.0%</u>

- Revenues from our Internet value-added services increased by 5.7% to RMB3,582.0 million for the second quarter of 2010 from RMB3,387.4 million for the first quarter of 2010. Online gaming revenues increased by 5.9% to RMB2,142.7 million despite weaker seasonality. This was mainly driven by increased monetisation of Cross Fire, as well as revenue contribution from recently launched MMOGs. Revenues from our community value-added services increased by 5.5% to RMB1,439.3 million. QQ Membership benefited from growth in monthly subscriptions, largely due to enriched online and offline privileges. Revenues from Qzone increased with improved user loyalty and stickiness, mainly fueled by enhancements in bundled privileges relating to social games. Revenues from QQ Show also increased as we continued to enhance user value and experience of the product.
- Revenues from our mobile and telecommunications value-added services increased by 9.0% to RMB674.1 million for the second quarter of 2010 from RMB618.2 million for the first quarter of 2010. This was primarily driven by growth in the user base of our bundled SMS packages as we enhanced privileges and features. Revenues from mobile social games also increased.

- Revenues from our online advertising business increased by 94.5% to RMB397.5 million for the second quarter of 2010 from RMB204.3 million for the first quarter of 2010. This primarily reflected favourable seasonality in the second quarter, as well as our focus on leveraging major events, including the World Cup and the World Expo, to generate business opportunities.

Cost of revenues. Cost of revenues increased by 11.6% to RMB1,482.9 million for the second quarter of 2010 from RMB1,328.4 million for the first quarter of 2010. This mainly reflected an increase in sharing costs, bandwidth and server custody fees, staff costs and equipment depreciation. As a percentage of revenues, cost of revenues increased to 31.8% for the second quarter of 2010 from 31.4% for the first quarter of 2010. The following table sets forth our cost of revenues by line of business for the second quarter of 2010 and the first quarter of 2010:

	Unaudited			
	Three months ended			
	30 June 2010		31 March 2010	
		% of		% of
	Amount	segment	Amount	segment
	<i>(RMB in thousands, except percentages)</i>			
Internet value-added services	1,100,032	30.7%	1,012,928	29.9%
Mobile and telecommunications value-added services	242,094	35.9%	221,346	35.8%
Online advertising	117,428	29.5%	70,943	34.7%
Others	<u>23,385</u>	150.3%	<u>23,138</u>	143.6%
Total cost of revenues	<u>1,482,939</u>		<u>1,328,355</u>	

- Cost of revenues for our Internet value-added services increased by 8.6% to RMB1,100.0 million for the second quarter of 2010 from RMB1,012.9 million for the first quarter of 2010. This was primarily due to an increase in sharing costs as a result of revenue growth from our licensed games. Other costs, including bandwidth and server custody fees and equipment depreciation, also increased as our business expanded.
- Cost of revenues for our mobile and telecommunications value-added services increased by 9.4% to RMB242.1 million for the second quarter of 2010 from RMB221.3 million for the first quarter of 2010. This was mainly driven by the increase in staff costs and telecommunications operators' revenue share.

- Cost of revenues for our online advertising business increased by 65.5% to RMB117.4 million for the second quarter of 2010 from RMB70.9 million for the first quarter of 2010. This was mainly due to an increase in sales commissions paid to advertising agencies as a result of the growth in our advertising revenues.

Other gains/(losses), net. Other gains, net of RMB27.4 million were recorded for the second quarter of 2010, compared to other losses, net of RMB35.3 million for the first quarter of 2010. The change was mainly the result of the fact that no donation was made to the Tencent Charity Fund in the second quarter, whereas RMB40.0 million was contributed to the fund in the previous quarter. It also reflected an increase in government subsidies and recognition of gain on foreign exchange forward contracts, which we entered into for the purpose of managing our foreign currency exposure related to our USD-denominated bank borrowings.

Selling and marketing expenses. Selling and marketing expenses increased by 24.2% to RMB230.3 million for the second quarter of 2010 from RMB185.4 million for the first quarter of 2010. This was mainly driven by an increase in our brand investments, including advertising campaigns for the World Cup and the World Expo. As a percentage of revenues, selling and marketing expenses increased to 4.9% for the second quarter of 2010 from 4.4% for the first quarter of 2010.

General and administrative expenses. General and administrative expenses increased by 13.7% to RMB666.0 million for the second quarter of 2010 from RMB585.8 million for the first quarter of 2010. This was primarily due to the expansion of our research and development team in support of our growth strategy. Other staff costs also increased as our business scale grew. As a percentage of revenues, general and administrative expenses increased to 14.3% for the second quarter of 2010 from 13.9% for the first quarter of 2010.

Income tax expense. Income tax expense increased by 25.5% to RMB448.5 million for the second quarter of 2010 from RMB357.4 million for the first quarter of 2010. The increase primarily reflected higher profit before tax and an increase in deferred tax liabilities recognised in respect of withholding taxes applicable on unremitted retained earnings expected to be paid by our PRC subsidiaries to their overseas parent companies. Additional tax expense was also provided during the quarter upon the finalisation of our enterprise income tax assessment for 2009.

Profit for the period. Profit for the period increased by 7.1% to RMB1,931.2 million for the second quarter of 2010 from RMB1,802.4 million for the first quarter of 2010. Net margin was 41.4% for the second quarter of 2010 compared to 42.7% for the first quarter of 2010.

Profit attributable to equity holders of the Company. Profit attributable to equity holders of the Company increased by 7.5% to RMB1,916.5 million for the second quarter of 2010 from RMB1,783.2 million for the first quarter of 2010.

Second Quarter of 2010 Compared to Second Quarter of 2009

The following table sets forth the comparative figures for the second quarter of 2010 and the second quarter of 2009:

	Unaudited	
	Three months ended	
	30 June 2010	30 June 2009
	<i>RMB'000</i>	<i>RMB'000</i>
Revenues	4,669,180	2,878,423
Cost of revenues	<u>(1,482,939)</u>	<u>(934,613)</u>
Gross profit	3,186,241	1,943,810
Interest income	54,005	27,520
Other gains/(losses), net	27,415	(2,192)
Selling and marketing expenses	(230,340)	(114,587)
General and administrative expenses	<u>(665,961)</u>	<u>(455,629)</u>
Operating profit	2,371,360	1,398,922
Finance costs	(2,976)	(653)
Share of profit of associates	<u>11,334</u>	<u>3,452</u>
Profit before income tax	2,379,718	1,401,721
Income tax expense	<u>(448,525)</u>	<u>(199,973)</u>
Profit/Total comprehensive income for the period	<u>1,931,193</u>	<u>1,201,748</u>
Attributable to:		
Equity holders of the Company	1,916,502	1,192,410
Non-controlling interests	<u>14,691</u>	<u>9,338</u>
	<u>1,931,193</u>	<u>1,201,748</u>

Revenues. Revenues increased by 62.2% to RMB4,669.2 million for the second quarter of 2010 from RMB2,878.4 million for the second quarter of 2009. The following table sets forth our revenues by line of business for the second quarter of 2010 and the second quarter of 2009:

	Unaudited			
	Three months ended			
	30 June 2010		30 June 2009	
	% of total		% of total	
	Amount	revenues	Amount	revenues
	<i>(RMB in thousands, except percentages)</i>			
Internet value-added services	3,581,976	76.7%	2,156,468	74.9%
Mobile and telecommunications value-added services	674,120	14.4%	470,003	16.3%
Online advertising	397,520	8.5%	243,044	8.5%
Others	<u>15,564</u>	<u>0.4%</u>	<u>8,908</u>	<u>0.3%</u>
Total revenues	<u>4,669,180</u>	<u>100.0%</u>	<u>2,878,423</u>	<u>100.0%</u>

- Revenues from our Internet value-added services increased by 66.1% to RMB3,582.0 million for the second quarter of 2010 from RMB2,156.5 million for the second quarter of 2009. Our online gaming revenues increased by 72.7% to RMB2,142.7 million, primarily driven by increased popularity of our major advanced casual games and MMOGs. The increase was also attributable to the revenue contribution from our recently launched MMOGs. The increase was partially offset by a decline in revenues from more mature MMOGs. Revenues from our community value-added services increased by 57.2% to RMB1,439.3 million. Qzone registered significant growth in revenues as our SNS applications enhanced user activity and engagement as well as stimulated growth of monthly subscriptions. Revenues from QQ Membership grew as a result of improved user loyalty and stickiness, driven by enhancements in online and offline privileges as well as value-added functions. Revenues from QQ Show increased as a result of growth in monthly subscriptions driven by enhanced features and user value.
- Revenues from our mobile and telecommunications value-added services increased by 43.4% to RMB674.1 million for the second quarter of 2010 from RMB470.0 million for the second quarter of 2009. This was mainly attributable to growth in revenues from our bundled SMS packages as we added more privileges and features and enhanced user experience. It also reflected growth in

revenues from mobile social games. The increase was partly offset by lower revenues from WAP services due to the suspension of WAP billing by China Mobile since 30 November 2009 as well as a decline in revenues from legacy mobile voice value-added services.

- Revenues from our online advertising business increased by 63.6% to RMB397.5 million for the second quarter of 2010 from RMB243.0 million for the second quarter of 2009. The increase mainly reflected enhanced market recognition of the strengths of our Internet platforms among advertisers, as well as our focus on leveraging major events, including the World Cup and the World Expo, to generate business opportunities. Search-based advertising revenues decreased as we transitioned into our self-developed search engine in the second half of last year.

Cost of revenues. Cost of revenues increased by 58.7% to RMB1,482.9 million for the second quarter of 2010 from RMB934.6 million for the second quarter of 2009. This primarily reflected an increase in sharing costs, staff costs, telecommunications operators' revenue share as well as equipment depreciation. As a percentage of revenues, cost of revenues decreased to 31.8% for the second quarter of 2010 from 32.5% for the second quarter of 2009. The following table sets forth our cost of revenues by line of business for the second quarter of 2010 and the second quarter of 2009:

	Unaudited			
	Three months ended			
	30 June 2010		30 June 2009	
	Amount	% of segment revenues	Amount	% of segment revenues
	<i>(RMB in thousands, except percentages)</i>			
Internet value-added services	1,100,032	30.7%	665,155	30.8%
Mobile and telecommunications value-added services	242,094	35.9%	179,581	38.2%
Online advertising	117,428	29.5%	73,423	30.2%
Others	<u>23,385</u>	150.3%	<u>16,454</u>	184.7%
Total cost of revenues	<u>1,482,939</u>		<u>934,613</u>	

- Cost of revenues for our Internet value-added services increased by 65.4% to RMB1,100.0 million for the second quarter of 2010 from RMB665.2 million for the second quarter of 2009. This was mainly the result of the growth in sharing costs due to increased revenues from our licensed games. Other costs, including staff costs and equipment depreciation, also increased as our business grew.

- Cost of revenues for our mobile and telecommunications value-added services increased by 34.8% to RMB242.1 million for the second quarter of 2010 from RMB179.6 million for the second quarter of 2009. This was primarily driven by an increase in telecommunications operators' revenue share due to growth in revenues. Staff costs also increased.
- Cost of revenues for our online advertising business increased by 59.9% to RMB117.4 million for the second quarter of 2010 from RMB73.4 million for the second quarter of 2009. This was primarily due to an increase in sales commissions paid to advertising agencies and staff costs as our business scale expanded.

Other gains/(losses), net. Other gains, net of RMB27.4 million were recorded for the second quarter of 2010, compared to other losses, net of RMB2.2 million for the second quarter of 2009. The change was mainly due to the fact that no donation was made to the Tencent Charity Fund in the second quarter of 2010, whereas RMB25.0 million was contributed to the fund in the second quarter of 2009. The change also reflected recognition of gain on foreign exchange forward contracts, which we entered into for the purpose of managing our foreign currency exposure related to our USD-denominated bank borrowings, during the second quarter of 2010. The aforementioned factors were partly offset by a reduction in fair value gains on financial assets held for trading and government subsidies.

Selling and marketing expenses. Selling and marketing expenses increased by 101.0% to RMB230.3 million for the second quarter of 2010 from RMB114.6 million for the second quarter of 2009. This was primarily driven by an increase in our brand investments, including advertising campaigns for the World Cup and the World Expo, and the promotion of our online games. Staff costs also increased as our business scale expanded. As a percentage of revenues, selling and marketing expenses increased to 4.9% for the second quarter of 2010 from 4.0% for the second quarter of 2009.

General and administrative expenses. General and administrative expenses increased by 46.2% to RMB666.0 million for the second quarter of 2010 from RMB455.6 million for the second quarter of 2009. This mainly reflected an expansion of our research and development team in support of our growth strategy. Staff costs also increased due to the growth of our business. As a percentage of revenues, general and administrative expenses decreased to 14.3% for the second quarter of 2010 from 15.8% for the second quarter of 2009.

Income tax expense. We recorded income tax expense of RMB448.5 million for the second quarter of 2010 compared to RMB200.0 million for the second quarter of 2009. The change primarily reflected growth in profit before tax and an increase in deferred tax liabilities recognised in respect of withholding taxes applicable on unremitted retained earnings expected to be paid by our PRC subsidiaries to their overseas parent companies. It also reflected higher tax rates for certain subsidiaries.

Profit for the period. Profit for the period increased by 60.7% to RMB1,931.2 million for the second quarter of 2010 from RMB1,201.7 million for the second quarter of 2009. Net margin was 41.4% for the second quarter of 2010 compared to 41.8% for the second quarter of 2009.

Profit attributable to equity holders of the Company. Profit attributable to equity holders of the Company increased by 60.7% to RMB1,916.5 million for the second quarter of 2010 from RMB1,192.4 million for the second quarter of 2009.

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2010 and 31 March 2010, we had the following major financial resources in the form of cash and investments:

	Unaudited	
	30 June	31 March
	2010	2010
	RMB'000	RMB'000
Cash and cash equivalents	6,486,312	6,795,966
Term deposits with initial term of over three months	7,422,082	6,673,010
Held-to-maturity investments	<u>—</u>	<u>341,315</u>
Total	<u>13,908,394</u>	<u>13,810,291</u>

Note: The above table excludes RMB1,214.5 million of restricted deposits pledged as part of a USD178.4 million short-term bank borrowing arrangement, as such deposits are scheduled to offset the borrowed amount at the maturity of the loan.

As at 30 June 2010, RMB627.2 million of our financial assets 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.

Our short-term bank borrowings were denominated in USD and amounted to RMB2,755.1 million as at 30 June 2010, of which RMB1,193.2 million was secured by RMB1,214.5 million of restricted deposits as mentioned in the note above and RMB1,561.9 million was unsecured. The borrowings were incurred for the purpose of managing the allocation of our onshore and offshore working capital. We had strong financial resources and cash flow generated from operating activities to meet these obligations.

BUSINESS REVIEW AND OUTLOOK

In the second quarter of 2010, we achieved solid financial and operating performance, riding on the growth of our Internet platforms. Our Internet value-added services (“IVAS”) registered revenue growth, mainly driven by increased monetisation of Cross Fire, contributions from our recently launched online games and growth of our community value-added services. Our mobile and telecommunications value-added services (“MVAS”) experienced a healthy revenue increase as well, largely due to an expansion of the user base of our bundled SMS packages. Our online advertising business grew significantly during the quarter, mainly due to favourable seasonality and our successful leveraging of major events, including the World Cup and the World Expo, to generate advertising opportunities. Looking into the third quarter of 2010, we expect online games within our IVAS business to benefit from positive seasonality due to summer school holidays. However, the year-on-year growth rate of the overall IVAS business is expected to slow down compared to the previous year as it already has reached a relatively larger revenue base. For MVAS, the regulatory environment is still uncertain. For example, a new rule that requires service providers to conduct double confirmation plus reminder services for monthly subscriptions has been announced recently. In addition, competition on the mobile Internet front will continue to intensify. On the other hand, business models in the industry remain underdeveloped as mobile Internet in China is still in a relatively early stage of development.

IM Platform

The quarter saw a steady growth in the user base of our core IM platform, with active user accounts and peak concurrent user accounts (“PCU”) increasing to 612.5 million and 109.4 million respectively. User activeness also increased, mainly due to growing usage of our IM services on mobile devices. We expect that going forward mobile Internet will become an increasingly important driver for the expansion of our IM user base as a result of the fast growing mobile Internet user base in China. On the other hand, as the growth of our current major social games is slowing down, the contribution from SNS applications to our IM user growth will decrease.

QQ.com

QQ.com has continued to enhance its market recognition and media influence in the second quarter, leveraging coverage and sponsorship related to the World Cup and the World Expo, as well as our brand advertising campaigns for these two major events.

For the World Cup, QQ.com offered a wide range of compelling content, including video clips for all matches and interviews with popular players, experts and professionals. In addition, we leveraged the integration between QQ.com and other platforms of Tencent, such as IM and Qzone, to deliver an innovative and interactive World Cup experience to users. A major TV advertising campaign for the World Cup was also launched to increase awareness of our services and reinforce our brand position. As a result of such efforts, QQ.com was ranked number one among major portals in China, in terms of traffic generated and user satisfaction for the event, according to the surveys by ComScore and Tsinghua University respectively. For the World Expo, as the exclusive Internet service sponsor of the event, we are responsible for the development, operation and maintenance of the official website, as well as the overall operation of the Online World Expo which, for the first time in the history of the Expo, allows people from all over the world to experience the Expo over the Internet. We have also introduced different products and campaigns to enhance public awareness and participation, including our Expo channel which provides comprehensive coverage of the event. Going forward, we will leverage the positive impact we made in these major events to further enhance the position of QQ.com as a mainstream media platform in China.

Internet value-added services

Our community value-added services registered growth in the second quarter. For QQ Membership, monthly subscription increased with improved user loyalty and stickiness. This reflected our continued efforts in enriching online and offline privileges associated with IM, online games, lifestyle services and e-commerce to increase user value. For SNS, active user accounts of Qzone increased to 458.5 million at the end of the second quarter of 2010, a growth of 7.1% compared to the previous quarter. This was primarily driven by the launch of promotional activities related to the fifth anniversary of Qzone. We also enhanced the attractiveness of our monthly subscription service by bundling more privileges related to SNS applications. In addition, we have enriched our offerings by introducing new third-party applications on Qzone and Xiaoyou, and commencing closed beta testing of QQ Restaurant, a self-developed social game which integrates with QQ Farm and QQ Ranch. As we have already accumulated a large user base of social

games over the previous quarters, we expect the positive impact of SNS applications to the active user base of Qzone will lessen over time. For QQ Show, monthly subscription continued to grow during the quarter as we increased marketing activities to promote the awareness of QQ Show among QQ users.

Our online game business registered modest growth during the second quarter. This was mainly driven by increased monetisation of Cross Fire as we launched new game items. Our recently launched game titles, namely Dragon Power, a hardcore 2D MMOG, and World of Fantasy, a self-developed MMOG, also contributed to the growth in revenues. QQ Game experienced modest growth in revenues during the quarter, although its PCU declined to 6.2 million due to fewer in-game promotions compared to the previous quarter and cannibalisation from social games. For Dungeon and Fighter, PCU and revenues declined slightly as a result of bot-fighting and weaker seasonality. Looking ahead, with slowing industry growth, intensifying competition and increasing sophistication of gamers, the success rate and extent of success for new game titles may decrease. In view of such challenges, we are extending the development process of our new games to upgrade content and quality. As a result, we are delaying QQ Xian Xia Zhuan to the end of 2010 or early 2011, and Feng Shen Ji to 2011. On the other hand, we believe that the online game industry will see more regulations as it becomes a significant component of China's cultural and entertainment industry. While some of these regulations might have impact on our business, the additional regulations should foster a healthier industry environment over the longer term.

Mobile and telecommunications value-added services

Our MVAS business registered healthy growth during the quarter as we enriched the privileges and features of our bundled SMS packages, and as the popularity of our mobile social games increased. Our WAP portal experienced an increase in traffic as a result of growth in the overall market and our efforts to improve its content and user experience. To position ourselves for growth opportunities in the mobile Internet sector, we have been extending our PC-based services to mobile platforms and customising our applications for a larger variety of mobile devices.

Online advertising

In the second quarter of 2010, our online advertising business benefited from positive seasonality. We also focused on leveraging our Internet platforms and major events, including the World Cup and the World Expo, to generate advertising opportunities. As a result, our revenues and client base registered significant growth during the

quarter, demonstrating increased market recognition of the strengths of our Internet platforms and our media influence. We believe that with the investments in our brand and major events, we are better positioned to exploit the growth opportunities in China's advertising market over the long term.

OTHER INFORMATION

Employee and Remuneration Policies

As at 30 June 2010, the Group had 8,687 employees (30 June 2009: 6,421), most of whom are based in Shenzhen, the PRC. The number of employees employed by the Group varies from time to time depending on need 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 programmes, 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 2010 was RMB1,397.0 million (for the six months ended 30 June 2009: RMB950.2 million).

Purchase, Sale or Redemption of the Company's Listed Securities

Save as disclosed in this announcement, 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 2010.

Audit Committee

The Audit Committee, which is comprised two independent non-executive directors and one non-executive director of the Company, 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 Auditors, has reviewed the Group's unaudited Interim Financial Information for the three and six months ended 30 June 2010.

Compliance with the Code on Corporate Governance Practices

Code provision A.4.2 of the Code on Corporate Governance Practices as set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") 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 of the Company ("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, in the annual general meeting of the Company held in May 2010 (the “2010 AGM”), two directors retired and were re-elected and the re-election of Mr Lau Chi Ping Martin, who was re-elected in 2007, was not considered in the 2010 AGM and his re-election will be considered in subsequent annual general meeting. Code provision A.4.2 regarding the retirement 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 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 2009 annual report of the Company, which was the position as at 31 December 2009, none of the directors of the Company is aware of any information which would reasonably indicate that the Company has not, for any part of the six months ended 30 June 2010, complied with the code provisions of Appendix 14 to the Listing Rules.

As to the deviation from code provisions A.2.1 and A.4.2 of Appendix 14 to the Listing Rules, 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.

APPRECIATION

On behalf of the Board, I would like to thank our employees for their valuable contributions and remarkable efforts, which enabled the Company to gain a better position in a competitive market full of challenges and uncertainties, as well as the support of the stakeholders for their continuing trust and confidence in our Group.

By Order of the Board
Ma Huateng
Chairman

Hong Kong, 11 August 2010

As at the date of this announcement, the directors of the Company are:

Executive Directors:

Ma Huateng, Lau Chi Ping Martin and Zhang Zhidong;

Non-Executive Directors:

Antonie Andries Roux and Charles St Leger Searle; and

Independent Non-Executive Directors:

Li Dong Sheng, Iain Ferguson Bruce and Ian Charles Stone.

This announcement contains forward-looking statements relating to the business outlook, forecast business plans and growth strategies of the Group. These forward-looking statements are based on information currently available to the Group and are stated herein on the basis of the outlook at the time of this announcement. They are based on certain expectations, assumptions and premises, some of which are subjective or beyond our control. The forward-looking statements may prove to be incorrect and may not be realised in future. Underlying the forward-looking statements are a large number of risks and uncertainties. Further information regarding these risks and uncertainties is included in our other public disclosure documents.