

KONGZHONG CORP  
Form 424B4  
July 09, 2004

**Table of Contents**

PROSPECTUS

Filed pursuant to Rule 424(b)(4)  
Registration Statement No. 333-116172

10,000,000 American Depositary Shares

**KongZhong Corporation**

Representing 400,000,000 Ordinary Shares

This is our initial public offering of American Depositary Shares, or ADSs. Each ADS represents 40 of our ordinary shares. We are selling 8,000,000 ADSs, representing 320,000,000 ordinary shares, and our selling shareholders are selling 2,000,000 ADSs, representing 80,000,000 ordinary shares. No public market currently exists for our ADSs or ordinary shares. The initial offering price of our ADSs is \$10.00 per ADS.

The ADSs have been approved to be included for quotation on the Nasdaq National Market under the symbol KONG.

**Before buying any ADSs, you should read the discussion of material risks of investing in our ADSs in Risk factors beginning on page 13.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

	Per ADS	Total
Initial public offering price	\$ 10.00	\$ 100,000,000
Underwriting discounts and commissions	\$ 0.70	\$ 7,000,000
Proceeds, before expenses, to us	\$ 9.30	\$ 74,400,000
Proceeds, before expenses, to the selling shareholders	\$ 9.30	\$ 18,600,000

The underwriters may also purchase up to 1,500,000 ADSs from us at the public offering price, less underwriting discounts and commissions, within 30 days from the date of this prospectus. The underwriters may exercise this option only to cover over-allotments, if any. We will not receive any proceeds from the sale of ADSs by the selling shareholders.

At our request, the underwriters have reserved at the initial public offering price up to 5% of the ADSs for sale to certain of our business associates, friends and family of employees and directors of our company, and other persons associated with us who have expressed an interest in purchasing our ADSs in this offering.

The underwriters are offering the ADSs as set forth under Underwriting. Delivery of the ADSs will be made on or about July 14, 2004.

**UBS Investment Bank**

**Banc of America Securities LLC**

**CIBC World Markets**

The date of this prospectus is July 8, 2004

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**Table of Contents**

You should only rely on the information contained in this prospectus. We have not authorized anyone to provide you with information different from that contained in this prospectus. We are offering to sell, and seeking offers to buy, ADSs only in jurisdictions where offers and sales are permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of ADSs.

**TABLE OF CONTENTS**

<u>Prospectus summary</u>	1
<u>Risk factors</u>	13
<u>Special note regarding forward-looking statements</u>	30
<u>Our corporate structure</u>	31
<u>Use of proceeds</u>	35
<u>Dividend policy</u>	36
<u>Dilution</u>	37
<u>Capitalization</u>	39
<u>Exchange rate information</u>	41
<u>Selected consolidated financial and operating data</u>	42
<u>Management's discussion and analysis of financial condition and results of operations</u>	44
<u>Industry overview</u>	62
<u>Business</u>	67
<u>Management</u>	86
<u>Regulation</u>	91
<u>Related party transactions</u>	96
<u>Principal and selling shareholders</u>	101
<u>Description of share capital</u>	104
<u>Description of American Depositary Shares</u>	112
<u>Shares eligible for future sale</u>	123
<u>Taxation</u>	125
<u>Underwriting</u>	131
<u>Legal matters</u>	137
<u>Experts</u>	137
<u>Expenses related to this offering</u>	138
<u>Where you can find more information</u>	139
<u>Enforceability of civil liabilities</u>	140
<u>Index to financial statements</u>	F-1

**Table of Contents**

**Prospectus summary**

*This summary highlights information contained elsewhere in this prospectus. You should read the entire prospectus carefully. Unless the context otherwise requires, information contained in this prospectus assumes that the underwriters will not exercise their option to purchase additional ADSs in this offering. All references to KongZhong, we, us, or our include KongZhong Corporation and its subsidiary and operating companies as a combined entity. All references to and statements regarding China, the People's Republic of China, or the PRC, in this prospectus do not apply to Hong Kong, Macau and Taiwan. All references to RMB or Renminbi are to the legal currency of China and all references to US dollars and \$ are to the legal currency of the United States.*

**OUR BUSINESS**

We are the leading provider of advanced second generation, or 2.5G, wireless interactive entertainment, media and community services, in terms of revenue, to customers of China Mobile Communications Corporation, or China Mobile, which has the largest mobile subscriber base in the world. China Mobile ranked KongZhong as the number one wireless value-added service provider on its network in terms of revenue for 2.5G wireless value-added services in 2003 and the first quarter of 2004. In addition, we have recently begun to provide wireless value-added services on the networks of China United Telecommunications Corporation, or China Unicom, China Telecommunications Corporation, or China Telecom, and China Network Communications Group Corporation, or China Netcom. Each of China Mobile, China Unicom, China Telecom and China Netcom is a state-owned enterprise, the majority of the equity interest of which is owned by the People's Republic of China. We are headquartered in Beijing and provide our services throughout China.

We primarily deliver our services through the 2.5G wireless standard. The higher transmission capacity of 2.5G allows users to access higher quality graphics and richer content and interactivity, in comparison with the second generation, or 2G, wireless standard, which has slightly lower service fees and may be accessed through less expensive mobile handsets. We deliver our 2.5G services through wireless access protocol, or WAP, multimedia messaging services, or MMS, and Java™ technology platforms. We also offer a range of data and voice services based on the 2G wireless standard through short messaging services, or SMS, interactive voice response, or IVR, and color ring back tones, or CRBT, technology platforms.

We deliver a broad range of services, through multiple technology platforms, which users can access directly from their mobile phones by choosing an icon embedded in select models of handsets, or from a mobile operator's portal or web site. Our services are organized in three major categories, consisting of:

Ø **Interactive entertainment.** Our interactive entertainment services include mobile games, pictures, karaoke, electronic books and mobile phone personalization features, such as ringtones, wallpaper, clocks and calendars.

Ø **Media.** Our media services provide content such as domestic and international news, entertainment, sports, fashion, lifestyle and other special interest areas.

Ø **Community.** Our community services include interactive chat, message boards, photo albums, dating and networking.

Our focus on establishing a leadership position in the rapidly growing advanced wireless value-added services market in China and our ability to cultivate cooperation arrangements with the mobile operators, mobile handset manufacturers and distributors, content providers and other business partners to produce, promote and market our services in the Chinese market have resulted in rapid growth of our financial and operating performance. Through these cooperation arrangements, we provide or promote our services and obtain content, and pay service fees to these mobile operators,

## **Table of Contents**

mobile handset manufacturers, mobile handset distributors, content providers and other partners, where relevant. Since commencing operations in May 2002, we have:

- Ø Grown our revenues and net income to \$7.8 million and \$2.4 million, respectively, in 2003;
- Ø Grown our revenues and net income to \$7.1 million and \$3.1 million, respectively, in the first quarter of 2004;
- Ø Grown our gross revenues and net income by 86% and 101%, respectively, in the first quarter of 2004 over the previous quarter;
- Ø Maintained our focus on 2.5G services, with 2.5G services contributing approximately 73% of our gross revenues in the first quarter of 2004; and
- Ø Increased our number of registered users to 9.4 million, of which 5.8 million users were classified as active users during the first quarter of 2004.

## **INDUSTRY OVERVIEW**

The wireless value-added services market, which provides services that allow mobile phone users to receive and transmit text, images and other forms of digital data or voice content via their mobile handsets, represents a new and fast-growing sector within China's rapidly evolving telecommunications industry. Analysys Consulting Ltd., or Analysys, estimates that total wireless value-added services revenue in China rose from \$211.5 million in 2002 to \$452.5 million in 2003 and is expected to grow to \$800.4 million in 2004. Chinese consumers have been quick to adopt and use new wireless value-added services as a means of communication, as well as a source of information and entertainment, partly due to the proliferation of mobile phones as a more accessible alternative to both fixed-line phone services and personal computer-based Internet services in China.

The evolution of the market for mobile services in China has thus far closely followed the industry development experienced in Japan and Korea, where mobile operators have provided platforms for third party service providers to offer services to customers of the mobile operator.

China Mobile launched its Monternet™ platform for wireless value-added services in November 2000 and China Unicom launched its Uni-Info™ platform in May 2001, using a business model similar to the model used in Japan and Korea. Key characteristics of China's wireless value-added services market include the rapid expansion of China's mobile telecommunications industry, increasing user receptivity, the availability of more advanced handsets in the Chinese market and support from mobile operators.

The wireless value-added services market in China is evolving as mobile telecommunications technology becomes more advanced. China Mobile began operating its 2.5G network in May 2002 and China Unicom began operating its 2.5G network in November 2002. Gartner Dataquest estimates that 48% and 60% of the mobile handsets sold in China in 2004 and 2005, respectively, will be General Packet Radio Services, or GPRS, handsets with 2.5G capability. Analysys estimates that the market for WAP services will increase to \$97.9 million in 2004 from \$25.7 million in 2003, representing an increase of 280%, and MMS services will increase to \$82.8 million in 2004 from \$27.8 million in 2003, representing an increase of 198%.

## **OUR STRENGTHS AND CHALLENGES**

We are an early entrant in China's 2.5G wireless value-added services market. Since our establishment, we have moved quickly to identify market trends, develop technologically advanced services and capture market share, with particular focus on the rapidly growing market for 2.5G services. As a

**Table of Contents**

result, we believe that we are well-positioned to capture the growth opportunities in China's wireless value-added services market. We have developed the following principal strengths:

- Ø Established market position with a well-recognized brand name in wireless interactive entertainment, media and community services;
- Ø Strategic relationships with China's largest mobile operator and key content and distribution partners, including handset manufacturers;
- Ø Leadership in understanding and addressing customer needs by offering a diversified portfolio of innovative services;
- Ø Product development team devoted to enhancing current and developing new services; and
- Ø Experienced management team.

Our ability to realize our business objectives and execute our strategies is subject to risks and uncertainties, including the following:

- Ø Our dependence on China Mobile for substantially all of our revenue and our dependence on its billing system;
- Ø Our limited operating history and dependence on our key personnel;
- Ø The possibility that the PRC government could determine that the agreements that establish our operating structure do not comply with PRC government restrictions on foreign investment in the value-added telecommunications industry;
- Ø The intense competition that we face in the wireless value-added services market due to low barriers to entry;
- Ø The rapidly evolving wireless value-added industry, which makes predicting future consumer acceptance and demand difficult;
- Ø Investors may not be able to exercise their right to vote the ordinary shares underlying our ADSs;
- Ø Cayman Islands law may provide shareholders with fewer rights than they would be afforded under the United States law; and
- Ø The uncertain legal and regulatory environment in China, which could limit the legal protections available to foreign investors.

Users can purchase our value-added services on a per-use basis and, in most cases, on a subscription basis. We provide our services mainly pursuant to our cooperation arrangements with the mobile operators, the terms of which are generally for one year or less. We do not directly bill our users, and depend on the billing systems and records of the mobile operators to bill and collect all fees. We generally do not have the ability to independently verify the accuracy of the billing systems of the mobile operators. As mobile operators do not provide us detailed revenue breakdown on a service-by-service basis, we depend on our internal database system to monitor revenue derived from each of our services. We make our business decisions based on our internal data, taking into account other factors including strategic considerations.

We initially ascertain the value of our services provided based on delivery confirmations sent to us by the networks of the mobile operators within 72 hours of delivery, but record revenues based solely on the monthly statements provided to us by the mobile operators. There has historically been a discrepancy, of approximately 10% in both 2003 and the first quarter of 2004, between the value we calculate based on delivery confirmations and the value that we are entitled to receive based on the monthly statements provided by the mobile operators. From time to time, for purposes of reporting our quarterly results to the market, we may need to estimate a portion of our reported revenue for the

**Table of Contents**

services provided in the event that we have not received monthly statements from the mobile operators by the time we report our earnings for a particular period.

**OUR STRATEGIES**

Our strategic objective is to build the leading brand and be the leading provider of wireless interactive entertainment, media and community services to mobile phone users among all mobile operators in China. We intend to undertake strategic initiatives focused on expanding our market presence, diversifying our range of service offerings and sustaining and enhancing our profitability and market position. In particular, we intend to:

- Ø Further promote and develop the KongZhong brand;
- Ø Capture market opportunities to strengthen and diversify our business and revenue streams;
- Ø Continue to develop and expand the scope of strategic relationships with key industry players;
- Ø Continue to develop and diversify our portfolio of service offerings to attract new customers and to increase usage among our existing customers;
- Ø Enhance our profitability by optimizing our product mix and focusing on the development and marketing of advanced wireless value-added services; and
- Ø Selectively acquire businesses that enhance our service portfolio, proprietary content, distribution channels and technology.

**CORPORATE STRUCTURE**

We were incorporated in May 2002 under the laws of the Cayman Islands. We conduct our business in China solely through our wholly-owned subsidiary, KongZhong Beijing. In order to meet domestic ownership requirements under PRC law, which restrict us and KongZhong Beijing, as foreign or foreign-invested companies, from operating in certain value-added telecommunications and Internet services, we have established Beijing AirInbox in China, which is wholly-owned by PRC citizens. In addition, we have recently established Beijing Boya Wuji in China, which is also wholly-owned by PRC citizens. We do not have any equity interest in Beijing AirInbox or Beijing Boya Wuji, but instead enjoy the economic benefits of these companies through a series of contractual arrangements which we and KongZhong Beijing have entered into with these companies and their respective shareholders. These contractual arrangements include agreements on provision of loans, provision of services, license of intellectual property, and certain corporate governance and shareholder rights matters.



**Table of Contents**

The chart below sets forth our corporate and share ownership structure as of the date of this prospectus, after giving effect to this offering, and assuming that (i) all of our preferred shares are converted into ordinary shares and (ii) the underwriters do not exercise their over-allotment options.

**PRINCIPAL EXECUTIVE OFFICES**

Our principal executive office is currently located at 8/F, Tower A, Yuetan Building, No. 2 Yuetan North Street, Beijing, China 100045, and will be moved to 33/F, Tengda Building, No. 168, Xiwai Avenue, Haidian District, Beijing, China, 100044 in August 2004. Our telephone number is (8610) 6808-1818. Our web site address is <http://www.kongzhong.com>. Information contained on our web site does not constitute a part of this prospectus. Our agent for service of process is CT Corporation System at 111 Eighth Avenue, New York, New York 10011.

**Table of Contents**

**THE OFFERING**

*Unless otherwise indicated, information in this prospectus assumes that the underwriters will not exercise the over-allotment option to purchase additional American Depositary Shares, or ADSs. See Underwriting.*

The Offering	10,000,000 ADSs, representing 400,000,000 ordinary shares.
ADSs	Each ADS represents 40 ordinary shares that will be held by Citibank, N.A., as depositary. At the request of our investors or their representatives, the ADSs will be evidenced by American Depositary Receipts, or ADRs. As an ADR holder, you will not be treated as one of our shareholders. You will have rights as provided in the deposit agreement. Under the deposit agreement, you may instruct the depositary to vote the shares underlying the ADRs. The depositary will pay you the cash dividends or other distributions it receives on shares after deducting fees and expenses. You must pay a fee for each issuance or cancellation of an ADS, distribution of securities by the depositary or any other depositary service. You may turn in your ADRs at the depositary's office and, after payment of some fees and expenses, the depositary will deliver the deliverable shares underlying your ADSs to you. To better understand the terms of the ADSs, you should carefully read the section in this prospectus entitled Description of American depositary shares. We also encourage you to read the deposit agreement, which is an exhibit to the registration statement that includes this prospectus.
Ordinary Shares	Shares in our registered capital, par value of \$0.0000005 per share.
Over-allotment Option	To the extent that the underwriters sell more than 10,000,000 ADSs, they have the option to purchase up to an additional 1,500,000 ADSs from us at the initial public offering price less underwriting discounts and commissions.
Price per ADS in the Offering	The initial public offering price per ADS is \$10.00. The initial public offering price per ADS is payable in U.S. dollars.
Use of Proceeds	Our net proceeds from this offering will be approximately \$72 million. We anticipate using these net proceeds for acquisitions or investments in businesses that we believe are complementary to our existing business, product development, sales and marketing and general corporate purposes. See Use of proceeds. We will not receive any proceeds from the sale of ADSs by the selling shareholders.

**Table of Contents**

Directed Share Program	At our request, the underwriters have reserved at the initial public offering price up to 5% of the ADSs for sale to certain of our business associates, friends and family of our employees and directors and other persons associated with us who have expressed an interest in purchasing our ADSs in this offering.
Risk Factors	See Risk factors and other information included in this prospectus for a discussion of factors you should carefully consider before deciding to invest in our ADSs.
ADSs Offered by Us	8,000,000 ADSs
ADSs Offered by Our Selling Shareholders	2,000,000 ADSs
Ordinary Shares Outstanding After the Offering	1,370,000,000 ordinary shares.
ADS Equivalents Outstanding After the Offering	34,250,000 ADSs
Listing	We have received approval to have our ADSs included for quotation on the Nasdaq National Market.
Proposed Nasdaq Symbol for Our ADSs	KONG

**CONVENTIONS**

The information in this prospectus gives effect to the automatic conversion of all of our outstanding Series A convertible preferred shares, or Series A preferred shares, and Series B redeemable convertible preferred shares, or Series B preferred shares, into an aggregate of 581,000,000 ordinary shares, which conversion will occur concurrently with the consummation of this offering. In addition, unless specifically indicated otherwise or unless the context otherwise requires, the information in this prospectus gives effect to the 20-for-1 share split of our ordinary shares as effected on March 18, 2004.

The number of ordinary shares outstanding after this offering is based on the number of shares outstanding as of March 31, 2004 and does not include: (i) 86,120,000 ordinary shares subject to options outstanding, of which 18,045,000 were exercisable, as of March 31, 2004 and (ii) 18,880,000 additional ordinary shares that are reserved for issuance under our 2002 Equity Incentive Plan, or the 2002 Plan. See Management Stock options.

Unless otherwise noted, all translations from RMB to U.S. dollars and from U.S. dollars to RMB were made at the noon buying rate in the City of New York for cable transfers in RMB per U.S. dollar as certified for customs purposes by the Federal Reserve Bank of New York on March 31, 2004, which was RMB8.2770 = \$1.00.

We make no representation that the RMB or U.S. dollar amounts referred to herein could have been or could be converted to U.S. dollars or RMB, as the case may be, at any particular rate.

**Table of Contents**

**Summary consolidated financial and operating data**

The following summary consolidated financial data should be read in conjunction with our audited consolidated financial statements, the notes thereto and Management's discussion and analysis of financial condition and results of operations included elsewhere in this prospectus. We commenced operations in May 2002. The summary consolidated statements of operations data for the period from May 6, 2002 to December 31, 2002, for the year ended December 31, 2003 and the three months ended March 31, 2004, and the summary consolidated balance sheet data as of December 31, 2002 and 2003 and March 31, 2004 set forth below are derived from our audited consolidated financial statements included elsewhere in this prospectus. Our audited consolidated financial statements have been prepared and presented in accordance with generally accepted accounting principles in the United States, or U.S. GAAP, and audited by Deloitte Touche Tohmatsu. Due to the relatively new and rapidly evolving nature of the wireless value-added services industry in China, the short history of our company and other factors affecting our business as described under Risk factors, our results of operations in any period are not necessarily indicative of the results that may be expected for any future period.

**Table of Contents**

Consolidated statements of operations data	For the period from May 6, 2002 to December 31, 2002	For the year ended December 31, 2003	For the three months ended March 31, 2003	For the three months ended March 31, 2004
(in thousands of U.S. dollars, except share and per share data)				
Gross revenues	\$ 200.3	\$ 7,806.7	\$ 703.0	\$ 7,147.6
Cost of revenues	(84.3)	(2,284.0)	(146.5)	(2,239.0)
Gross profit	116.0	5,522.7	556.5	4,908.6
Operating expenses:				
Product development	164.2	1,369.5	176.2	716.5
Sales and marketing	128.9	841.4	140.7	294.1
General and administrative	317.3	882.7	142.4	675.7
Amortization of deferred stock compensation		22.0		80.8
Total operating expenses	610.4	3,115.6	459.3	1,767.1
Income (loss) from operations	(494.4)	2,407.1	97.2	3,141.5
Other expenses				(0.7)
Interest income, net	0.5	1.0	(0.1)	1.3
Net income (loss) before income taxes	(493.9)	2,408.1	97.1	3,142.1
Income tax expense				
Net income (loss)	\$ (493.9)	\$ 2,408.1	\$ 97.1	\$ 3,142.1
Net income (loss) per share:				
Basic	\$ 0.00	\$ 0.01	\$ 0.00	\$ 0.01
Diluted	\$ 0.00(1)	\$ 0.00	\$ 0.00	\$ 0.00
Shares used in calculating net income (loss) per share:				
Basic	415,547,794	469,000,000	469,000,000	469,000,000
Diluted	415,547,794(1)	1,094,824,434	1,090,364,373	1,098,206,555
Pro forma net income (loss) per share (unaudited)				
Basic	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Diluted	\$ 0.00(1)	\$ 0.00	\$ 0.00	\$ 0.00
Shares used in calculating pro forma net income (loss) per share				
Basic	622,124,999	1,050,000,000	1,050,000,000	1,050,000,000
Diluted	622,124,999(1)	1,094,824,434	1,090,364,373	1,098,206,555

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Pro forma net income (loss) per ADS equivalent				
Basic	\$ (0.03)	\$ 0.09	\$ 0.00	\$ 0.12
Diluted	\$ (0.03)	\$ 0.09	\$ 0.00	\$ 0.11

(1) Anti-dilutive preferred shares and options were excluded from the weighted average ordinary shares outstanding for the diluted per share calculation. For 2002, basic loss per share did not differ from diluted loss per share.

**Table of Contents**

Consolidated balance sheet data	As of			
	December 31, 2002	December 31, 2003	March 31, 2004	March 31, 2004
	(in thousands of U.S. dollars)		(unaudited)	Pro forma (unaudited) <sup>(1)</sup>
Cash and cash equivalents	\$ 2,646.2	\$ 3,742.6	\$ 5,736.2	\$ 5,736.2
Accounts receivable	\$ 132.3	\$ 1,703.9	\$ 3,268.8	\$ 3,268.8
Property and equipment, net	\$ 251.0	\$ 848.5	\$ 1,104.2	\$ 1,104.2
Total assets	\$ 3,101.3	\$ 6,567.5	\$ 10,518.1	\$ 10,518.1
Total current liabilities	\$ 75.0	\$ 1,047.3	\$ 1,654.4	\$ 1,654.4
Series B redeemable convertible preferred shares	\$ 2,970.0	\$ 2,970.0	\$ 2,970.0	\$
Total shareholders' equity	\$ 56.3	\$ 2,550.1	\$ 5,772.9	\$ 8,742.9
Total liabilities and shareholders' equity	\$ 3,101.3	\$ 6,567.5	\$ 10,518.1	\$ 10,518.1

- (1) The unaudited pro forma balance sheet information as of March 31, 2004 assumes the conversion upon completion of the initial public offering of all shares of convertible preferred shares outstanding as of March 31, 2004 into ordinary shares.

Operating data	For the period from May 6, 2002 to December 31, 2002	For the year ended December 31, 2003	For the three months ended March 31, 2004
	(in thousands)		
2.5G <sup>(1)</sup>			
Subscriptions <sup>(2)</sup>	351.6	9,021.3	5,508.0
Downloads <sup>(3)</sup>		2,722.1	2,334.2
2G <sup>(4)</sup>			
Subscriptions <sup>(2)</sup>	50.0	1,925.4	2,194.2
Downloads <sup>(3)</sup>	800.0	6,127.4	1,634.6
Total			
Subscriptions <sup>(2)</sup>	401.6	10,946.7	7,702.3
Downloads <sup>(3)</sup>	800.0	8,849.5	3,968.8

- (1) Includes WAP, MMS and Java™. We began to provide WAP, MMS and Java™ services on a paid basis in September 2002, April 2003 and November 2003, respectively.
- (2) Total number of paid monthly subscriptions in the relevant period.
- (3) Total number of paid downloads in the relevant period, excluding downloads made pursuant to subscriptions.
- (4) Includes SMS, IVR and CRBT. We began to provide SMS, IVR and CRBT services on a paid basis in July 2002, December 2003 and October 2003, respectively.

**Table of Contents**

**Summary unaudited consolidated quarterly financial and operating data**

The following summary unaudited consolidated quarterly financial data should be read in conjunction with our audited consolidated financial statements, the notes thereto and Management's discussion and analysis of financial condition and results of operations included elsewhere in this prospectus. The summary unaudited consolidated quarterly financial data for each of the periods presented below were derived from our management financial information, which was prepared on substantially the same basis as our audited consolidated financial statements and includes all adjustments that we consider necessary for a fair presentation of our financial position and operating results for the periods presented. Due to the relatively new and rapidly evolving nature of the wireless value-added services industry in China, the short history of our company and other factors affecting our business as described under Risk factors, our results of operations in any period are not necessarily indicative of the results that may be expected for any future periods.

**For the three months ended**

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**June 30,    September 30,    December 31,**