

Giant Interactive Group Inc.
Form 20-F
June 17, 2011

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 20-F**

(Mark One)

**REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE
SECURITIES EXCHANGE ACT OF 1934
OR**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2010

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
OR**

**SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

**Date of event requiring this shell company report
For the transition period from to .
Commission file number: 001-33759
Giant Interactive Group Inc.**

(Exact name of Registrant as specified in its charter)

Not applicable

(Translation of Registrant's name into English)

Cayman Islands

(Jurisdiction of incorporation or organization)

**11/F, No. 3 Building, 700 Yishan Road
Shanghai, 200233, People's Republic of China**
(Address of principal executive offices)

Eric He

Chief Financial Officer

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Telephone: (86 21) 3397 9999

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(Name, Telephone, E-mail and/or Facsimile Number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class

Name of each exchange on which registered

American Depositary Shares, each representing one
ordinary share, par value US\$0.0000002 per share

New York Stock Exchange

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Securities registered or to be registered pursuant to Section 12(g) of the Act.

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 228,019,412 ordinary shares.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

If this report is an annual or transaction report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP International Financial Reporting Standards as issued by the International Accounting Standards Board Other

If "Other" has been checked in response to the previous question indicate by check mark which financial statement item the registrant has elected to follow. Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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INTRODUCTION

Except where the context otherwise requires and for purposes of this annual report only:

we, us, our company, and our, refer to Giant Interactive Group Inc., its predecessor entities and subsidiaries, and its consolidated affiliated entities;

China or PRC refers to the People's Republic of China, excluding, for purposes of this annual report only, Taiwan and the Special Administrative Regions of Hong Kong and Macau;

monthly average concurrent users, or ACU, of any of our games is determined as follows: we first determine the number of users logged onto the game at five-minute intervals, and average that data over the course of a day to derive the daily average. The daily average data are then averaged over the monthly period to derive the monthly average concurrent users;

quarterly active paying players, or APP, is the aggregate number of accounts for our games that have been charged at least once during the quarterly period;

quarterly average concurrent users, or ACU, of any of our games is the average of monthly average concurrent users of such game during the quarterly period;

quarterly average revenues per user, or ARPU, is our online game net revenues during the quarterly period divided by the quarterly active paying players of these games during the quarterly period; our definition of ARPU may not be comparable to similarly titled measures presented by other online game companies;

quarterly peak concurrent users, or PCU, of any of our games is the peak concurrent users of such game during the quarterly period;

a shard is, with respect to an online game, one of multiple independent copies of the game world. In a sharded game, such as ZT Online or Giant Online, players may only interact with other players in one shard at one time;

All references to Renminbi or RMB are to the legal currency of China, all references to US dollars, dollars, or US\$ are to the legal currency of the United States, and all references to HK\$ are to the legal currency of the Hong Kong Special Administrative Region of China;

ordinary shares refers to our ordinary shares, par value US\$0.0000002 per share;

ADSs refers to our American depositary shares, each of which represents one ordinary share;

ADRs refers to American depositary receipts, which, if issued, evidence our ADSs;

PRC GAAP refers to accounting principles and the relevant financial regulations applicable to PRC enterprises; and

US GAAP refers to generally accepted accounting principles in the United States.

This annual report on Form 20-F includes our audited consolidated statements of operation data for the years ended December 31, 2008, 2009 and 2010 and audited consolidated balance sheet data as of December 31, 2009 and 2010.

We and certain of our shareholders completed the initial public offering of 65,777,036 ADSs, each representing one ordinary share, on November 6, 2007. Our ADSs are listed on the New York Stock Exchange under the symbol GA.

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FORWARD-LOOKING STATEMENTS

This annual report on Form 20-F contains forward-looking statements that relate to our current expectations and views of future events. The forward-looking statements are contained principally in the items entitled Information on the Company, Risk Factors, Operating and Financial Review and Prospects, Financial Information, and Quantitative and Qualitative Disclosures About Market Risk. Our forward-looking statements relate to events that involve known and unknown risks, uncertainties and other factors, including those listed under Risk Factors, which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements.

In some cases, these forward-looking statements can be identified by words or phrases such as may, will, expect, anticipate, aim, estimate, intend, plan, believe, potential, continue, is/are likely to or other similar expressions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. These forward-looking statements include, among other things, statements relating to:

our anticipated growth and marketing strategies;

our future business development, results of operations and financial condition;

our ability to develop and commercialize new online games, including our ability to manage our development expenses;

market acceptance of our online games;

our ability to introduce expansion packs and updates to our existing online games;

our ability to license our online games to third party operators;

our ability to manage our existing licensing arrangements, including our ability to anticipate and manage licensing fees;

competition from other online game developers and operators;

our expectations for a rise in online payment systems and associated online crime;

our ability to anticipate and manage Internet access fees and server maintenance costs;

our intentions regarding management of our employees and liaison personnel;

our ability to comply with regulation applying to online games;

our ability to effectively protect our existing and future intellectual property and not to infringe on the intellectual property of others;

our ability to expand our business through organic growth and strategic acquisitions;

our ability to integrate and manage our investment in Five One Network Development Co., or 51.com;

fluctuations in general economic and business conditions in China; and

impact of the current worldwide economic crisis on our business.

If any one or more of the assumptions underlying the market data turns out to be incorrect, actual results may differ from the projections based on these assumptions. You should not place undue reliance on these forward-looking statements.

The forward-looking statements made in this annual report relate only to events or information as of the date on which the statements are made in this annual report. Except as required by law, we undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise, after the date on which the statements are made or to reflect the occurrence of unanticipated events. You should read this annual report and the documents that we reference in this annual report completely and with the understanding that our actual future results may be materially different from what we expect.

Market Data and Forecasts

This annual report also contains data related to the online gaming industry in China. This market data includes projections that are based on a number of assumptions. The online gaming market may not grow at the rate projected by market data, or at all. The failure of this market to grow at the projected rate may have a material adverse effect on our business and the market price of our ADSs. In addition, the rapidly changing nature of the online gaming industry subjects any projections or estimates relating to the growth prospects or future condition of our market to significant uncertainties. Furthermore, our actual results may differ from the projections if any one or more of the assumptions underlying the market data turns out to be incorrect. You should not place undue reliance on market forecasts regarding the online gaming industry in China.

Unless otherwise indicated, information in this annual report concerning economic conditions and our industry is based on information from independent industry analysts and publications, as well as our estimates. Except where otherwise noted, our estimates are derived from publicly available information released by third party sources, as well as data from our internal research, and are based on such data and our knowledge of our industry, which we believe to be reasonable.

Table of Contents**PART I.****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION**A. Selected Financial Data**

The selected consolidated financial data for the three years ended December 31, 2008, 2009 and 2010, and the selected consolidated balance sheet data for the two years ended December 31, 2009 and 2010, were derived from our audited consolidated financial statements appearing in this annual report beginning on page F- 1 . The selected consolidated balance sheet data for the years ended December 31, 2006, 2007 and 2008 have been derived from our audited consolidated balance sheets as of December 31, 2006, 2007 and 2008, which are not included in this annual report. The selected consolidated statement of operations and comprehensive income data for the years ended December 31, 2006 and 2007 have been derived from our audited consolidated financial statements for the year ended December 31, 2006 and 2007, which are not included in this annual report. The following consolidated financial data summary for the periods and as of the dates indicated below should be read in conjunction with, and are qualified in their entirety by reference to, our consolidated financial statements and related notes and Item 5, Operating and Financial Review and Prospects below.

Our audited consolidated financial statements are prepared in accordance with US GAAP, and have been audited by Ernst & Young Hua Ming, an independent registered public accounting firm. The report of Ernst & Young Hua Ming on the consolidated financial statements as of December 31, 2009 and 2010 is included elsewhere in this annual report.

Our historical results for any prior period are not necessarily indicative of results to be expected for any future period.

Consolidated Statement of Operations and Comprehensive Income Data:

	Year Ended December 31,					US\$
	2006 RMB	2007 RMB	2008 RMB	2009 RMB	2010 RMB	
	(In thousands, except per share and per ADS data)					
Net revenue:						
Online games	408,499	1,521,396	1,589,676	1,293,018	1,289,481	195,376
Licensing revenues		6,140	4,391	10,687	42,667	6,465
Other revenue, net			612	130	668	101
Total net revenue	408,499	1,527,536	1,594,679	1,303,835	1,332,816	201,942
Cost of services	(45,195)	(174,086)	(217,899)	(204,070)	(199,122)	(30,170)
Gross profit	363,304	1,353,450	1,376,780	1,099,765	1,133,694	171,772
Operating (expenses) income:						
Research and product development	(14,799)	(26,918)	(88,539)	(113,354)	(186,037)	(28,187)
Sales and marketing	(80,460)	(189,403)	(241,575)	(119,600)	(143,006)	(21,668)
General and administrative	(26,098)	(74,130)	(141,786)	(121,446)	(119,447)	(18,098)
Government financial incentives	1,621	16,779	63,084	88,460	57,386	8,695
Impairment of intangible assets					(46,558)	(7,054)

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Total operating expenses	(119,736)	(273,672)	(408,816)	(265,940)	(437,662)	(66,312)
Income from operations	243,568	1,079,778	967,964	833,825	696,032	105,460
Interest income	1,136	53,878	184,964	102,200	136,098	20,621
Investment income (loss)		2,562	1,171	(5,971)		
Unrealized loss on investment held-for-trading			(300)			
Other (expense) income, net	(86)	126	(843)	14,025	65,466	9,919
Income before income tax expenses	244,618	1,136,344	1,152,956	944,079	897,596	136,000
Income tax expenses			(39,368)	(85,060)	(89,322)	(13,534)
Share of loss of an equity investee					(648)	(98)
Net income	244,618	1,136,344	1,113,588	859,019	807,626	122,368
Net loss attributable to non controlling interests				295	3,563	540

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	Year Ended December 31,					US\$
	2006 RMB	2007 RMB	2008 RMB	2009 RMB	2010 RMB	
	(In thousands, except per share and per ADS data)					
Net income attributable to the Company's shareholders	244,618	1,136,344	1,113,588	859,314	811,189	122,907
Other comprehensive loss, net of tax						
Foreign currency translation	146	(51,927)	(192,424)	(12,769)	(73,194)	(11,090)
Reclassification adjustment				(1,814)		
Unrealized holding gains (losses)			76,969	(30,951)	(14,540)	(2,203)
Total other comprehensive loss, net of tax	146	(51,927)	(115,455)	(45,534)	(87,734)	(13,293)
Comprehensive income	244,764	1,084,417	998,133	813,780	723,455	109,614
Net earnings per ordinary shares, basic	1.22					
Net earnings per ordinary shares, diluted	1.22					
Net earnings per ADS ⁽¹⁾ , basic		5.40	4.65	3.80	3.57	0.54
Net earnings per ADS, diluted		5.25	4.49	3.67	3.47	0.53
Shares used in computation, basic	200,000,000	210,574,196	239,458,633	226,278,227	227,308,854	227,308,854
Shares used in computation, diluted	200,148,401	216,255,503	247,895,076	233,960,556	233,928,400	233,928,400

(1) Each ADS represents one ordinary share.

Selected Consolidated Balance Sheet Data:

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	December 31, 2006 (RMB)	December 31, 2007 (RMB)	December 31, 2008 (RMB) (in thousands)	December 31, 2009 (RMB)	December 31, 2010 (RMB) (US\$)	
Assets						
Cash and cash equivalents	451,371	7,295,470	1,696,273	1,097,155	2,776,936	420,748
Total current assets	466,658	7,373,495	5,236,061	5,102,972	6,304,005	955,152
Property and equipment, net	36,491	127,631	213,905	178,670	143,286	21,710
Total non-current assets	38,146	214,228	766,363	1,349,690	804,138	121,839
Total assets	504,804	7,587,723	6,002,424	6,452,662	7,108,143	1,076,991
Total current liabilities	238,867	1,282,199	603,608	547,448	700,314	106,108
Total liabilities	254,942	1,282,199	629,294	547,869	700,500	106,136
Total shareholders equity	249,862	6,305,524	5,373,130	5,897,185	6,392,860	968,615
Non controlling interest				7,608	14,783	2,240
Total liabilities and equity	504,804	7,587,723	6,002,424	6,452,662	7,108,143	1,076,991

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	For the quarter ended				
	March 31, 2010	June 30, 2010	September 30, 2010	December 31, 2010	March 31, 2011
	(in thousands, except average revenues per user)				
Average Concurrent Users	588	670	538	584	586
Peak Concurrent Users	1,611	1,657	1,466	1,713	1,916
Active Paying Players	1,373	1,435	1,497	1,693	1,779
Average Revenues per User (RMB)	220	223	225	215	216

Exchange Rate Information

Our business is conducted in China and substantially all of our net revenues are denominated in Renminbi. This annual report contains translations of Renminbi amounts into U.S. dollars at specific rates solely for the convenience of the reader. Conversions of Renminbi into U.S. dollars in this annual report are based on the noon buying rate in The City of New York for cable transfers of Renminbi as certified for customs purposes by the Federal Reserve Bank of New York. Unless otherwise noted, all translations from Renminbi to U.S. dollars and from U.S. dollars to Renminbi in this annual report were made at a rate of RMB6.6000 to US\$1.00, the noon buying rate in effect as of December 31, 2010. We make no representation that any Renminbi or U.S. dollar amounts could have been, or could be, converted into U.S. dollars or Renminbi, as the case may be, at any particular rate, the rates stated below, or at all. The PRC government imposes control over its foreign currency reserves in part through direct regulation of the conversion of Renminbi into foreign exchange and through restrictions on foreign trade. On June 10, 2011, the noon buying rate was RMB6.4801 to US\$1.00.

The following table sets forth information concerning exchange rates between the Renminbi and the U.S. dollar for the periods indicated.

Period	Period End	Noon Buying Rate		
		Average ⁽¹⁾ (RMB per US\$1.00)	Low	High
2006	7.8041	7.9723	7.8041	8.0702
2007	7.2946	7.5806	7.2946	7.8127
2008	6.8225	6.9477	6.7800	7.2946
2009	6.8259	6.8307	6.8176	6.8470
2010	6.6000	6.7696	6.6000	6.8330
December 2011	6.6000	6.6497	6.6000	6.6745
January	6.6017	6.5964	6.5809	6.6364
February	6.5713	6.5761	6.5520	6.5965
March	6.5488	6.5645	6.5483	6.5743
April	6.4900	6.5267	6.4900	6.5477
May	6.4786	6.4957	6.4786	6.5073
June (through June 10, 2011)	6.4801	6.4790	6.4754	6.4824

(1) Averages for a period are calculated by using the average of the exchange rates on the end of each month during the period. Monthly averages are calculated by using the average of the daily rates during the relevant period.

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Risks Relating to Our Business and Industry

Our limited operating history and the unproven long-term potential of our online game business model make evaluating our business and prospects difficult.

We began offering our first product, the free-to-play massively multiplayer online role playing game, or MMORPG, ZT Online, on a commercial basis in January 2006. As of the date of this annual report, we operate eight additional MMORPGs, one casual massively multiplayer online game, or MMO, and one strategy browser game. All but one of these games is based upon the free-to-pay revenue model and we expect the substantial majority of our net revenues to continue to be generated by free-to-play

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games. Under this revenue model, players are able to play the online game free of charge for an unlimited amount of time, but are charged for purchases of in-game items, such as weapons, clothing and other accessories. While other online game companies have adopted the free-to-play revenue model, it is still relatively new compared to the more proven time-based model. The free-to-play model requires us to design games that not only attract players to spend more time playing, but also encourage them to purchase in-game items. The sale of in-game items requires us to track closely consumers' preferences, especially in-game spending trends.

Due to both our limited operating history and the relatively new free-to-play online game revenue model, it may be difficult for you to evaluate our business, financial performance and prospects. In addition, we may not have sufficient experience to address the risks and difficulties frequently encountered by young companies using relatively new business models in rapidly evolving markets, such as China's online game market. These risks and difficulties include, but are not limited to, our potential failure to develop, acquire or license additional online games that are appealing to players, our ability to retain existing players and attract new players for our online games, our ability to adapt to competitive market conditions and our ability to respond in a timely manner to technological changes or resolve unexpected network interruptions. If we are unsuccessful in addressing these risks and difficulties, our business, financial condition and results of operations may be adversely affected.

We have been, and may continue to be, substantially dependent on ZT Online Series, which has accounted for nearly all of our historical net revenues. Any reduction in ZT Online Series' player base or any decrease in its popularity could materially and adversely affect our business, financial condition and results of operations, and any change in the accounting policies relating to that game could cause our online game revenues to fluctuate.

Since inception, sales of virtual value-added items and services related to the ZT Online Series have accounted for nearly all of our net revenues. We commercially launched ZT Online in 2006 and subsequently commercially launched or introduced multiple versions of ZT Online, which includes ZT Online Classic Edition, ZT Online PTP and ZT Online Green Edition. ZT Online, together with multiple versions of ZT Online launched, introduced or to be launched in the future, are collectively referred to as the ZT Online Series. In addition, we have developed ZT Online II, the sequel to ZT Online, which is currently under closed beta testing. Although we currently operate eleven games, seven of which are not part of the ZT Online Series, we expect that we will continue to derive the majority of our net revenues in 2011 from the ZT Online Series. Our business will therefore remain highly sensitive to the profitability and popularity of the ZT Online Series, and any reduction in the ZT Online Series games player base or any decrease in its popularity in China due to competition with our other online games or those of third parties or otherwise could materially and adversely affect our business, financial condition and results of operations. For example, in the third quarter of 2009 our quarterly net online game revenues decreased by RMB73.7 million to RMB287.5 million from RMB361.2 million the prior quarter, which we believe was primarily due to a change in our monetization features for ZT Online to reduce the number of in-game promotional items. Furthermore, any lasting or prolonged server interruption due to network failures or other factors or any other adverse developments specific to the ZT Online Series could prevent and otherwise deter players from making purchases of virtual items and services. This could also materially and adversely affect our business, financial condition and results of operations.

With respect to those virtual items that we sell that are not consumed at a predetermined time or otherwise do not have a limitation on repeated use, our accounting policies require us to recognize the related revenue over the estimated lifespan of that virtual item as determined by historical player usage patterns and playing behavior. In some cases, this period can be as long as the estimated lifespan of the game. We continuously monitor the useful life of each type of virtual item we sell and of our games, and will adjust these as appropriate. Any such adjustment may cause our revenues to be recognized over a significantly different time period, and may cause our net revenues to fluctuate from prior periods. For example, in 2010, based on our internally calculated gameplay statistics, we determined that inactive players of ZT Online are players who have not played our game in 270 days consecutively, as opposed to 180 days as determined in 2008, 2009 and to 90 days as determined in 2007. As a result of this change, we have lengthened the period we amortize the life of certain virtual items, thereby reducing our online game net revenues.

We will also need to expend considerable resources to ensure ZT Online Series' continued success. To maximize the lifespan of an online game, it is necessary to continuously improve and update the game on a timely basis with new content and features that appeal to our players. We may fail to develop improvements, updates and/or

enhancements on a timely basis, if at all. Any such failure may cause the game to lose popularity, which could result in lower net revenues.

If we are unable to develop, purchase or license additional online games that are attractive to players and result in overall revenue growth, our business, financial condition and results of operations may be materially and adversely affected and our ability to recover related product research and development costs, purchase costs or licensing fees may become limited.

In order to maintain our long-term profitability and financial and operational success, we must continually develop, purchase or license new online games that are attractive to players to replace our existing online games as they reach the end of their useful economic life. We currently operate eleven games and we have licensed or developed additional games that we plan to operate in the future. Our new games may not be released on time and may not be profitable or popular among online game players in China. If our newly introduced games fail to attract new players or fail to result in increased online game revenues, our business, financial condition and results of operations may be materially and adversely affected.

The success of our internally developed games will largely depend on our ability to anticipate and effectively respond to changing player tastes and preferences and continually make technical advances to our platform. Developing games internally requires substantial initial investment prior to commercial launch of the games as well as a significant commitment of future resources. In addition, our ability to purchase or license successful online games will depend on their availability at acceptable terms, including price, our ability to compete effectively against other potential purchasers or licensees to attract the developers of these games, and our ability to obtain government approvals required for the purchase or licensing and operation of these games. The games that we develop, purchase or license may not be attractive to players, may be viewed by the regulatory authorities as not complying with

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content restrictions, may not be launched as scheduled or may not compete effectively with our competitors' games. Additionally, new technologies in our competitors' online game programming or operations could render our games obsolete or unattractive to players, thereby limiting our ability to recover related product research and development costs, purchase costs and licensing fees. If we are not able to successfully develop, purchase or license online games appealing to players, our future profitability and growth prospects will decline.

Our new online games may attract away players of our established games, which could materially and adversely affect our business, results of operations and financial condition.

We currently operate eleven games, including five games in the ZT Online Series, and we have licensed or developed additional games that we plan to operate in the future. Our new or future games may attract players away from our older games. In particular, since our new game ZT Online II is a sequel to and shares the same basic plot and features as our older game ZT Online, this new game may attract players away from ZT Online. Although we intend to target different types of players through ZT Online Series and ZT Online II and therefore minimize players of our existing games leaving such games in favor of our future games, we anticipate such movement may occur. This would decrease our established games' number of concurrent users, which could make these games less attractive to other players. Furthermore, if former players of our established games spend less money to purchase virtual items and services or playing time on our new online games than they would have spent if they had continued playing our established games, our business, results of operations and financial condition could be materially and adversely affected.

We face significant competition, which could reduce our market share and adversely affect our business, financial condition and results of operations.

The online game industry in China is highly competitive. Given the relatively low entry barriers to operating online games, we expect more companies to enter the online game industry in China and a wider range of online games to be introduced to the China market. Our MMORPGs mainly compete with certain MMORPGs developed and/or operated in China, including Fantasy Westward Journey, developed and operated by NetEase.com, Inc.; World of Warcraft, developed by Blizzard Entertainment and operated by NetEase.com, Inc.; Tian Long Ba Bu, developed and operated by Changyou.com Limited; Zhu Xian, developed and operated by Perfect World, Co., Ltd.; and MIR, developed and operated by Shanda Interactive Entertainment Limited. Our principal competitors also include online game companies such as CDC Corporation, Kingsoft Corporation, Nineyou International Limited, Tencent Holdings Ltd., Webzen Inc., The 9 Limited, Changyou.com Limited, Perfect World, Co., Ltd., Shanda Interactive Entertainment Limited, NetEase.com, GigaMedia Limited, and Net Dragon Websoft Inc. Furthermore, we expect companies from more developed gaming markets, such as the United States and South Korea, to continue to enter into the online game industry in China and more games developed by overseas entities will be licensed to be operated in Chinese markets.

Many of our existing competitors, as well as a number of potential new competitors, have longer operating histories, greater brand name recognition, larger international player bases and significantly greater game development, technical, financial and marketing resources than we have. Furthermore, any of our current or future competitors may be acquired by, receive investments from or enter into other commercial relationships with larger, more well-established and well-financed companies and therefore obtain greater financial, marketing and development and licensing resources than we have. This may allow them to devote greater resources than we can to the development and promotion of new online games and technologies similar to or better than our own. These competitors may engage in more extensive research and development, undertake more far-reaching marketing campaigns, adopt more aggressive pricing policies and make more attractive offers of employment to our existing and potential employees than we can. In addition, our existing and potential international competitors may establish cooperative relationships among themselves or with our local competitors. This may significantly enhance their competitiveness in the online game industry in China. New and increased competition may result in larger discounts demanded by our distributors, or price reductions in our virtual items and services, any of which could adversely affect our net revenues. In addition, the increased competition in the online game industry in China could make it difficult for us to retain and expand our existing player base, which could reduce the number of dedicated players and players with high disposable incomes that play our games and from whom we derive most of our net revenues. If we are unable to compete effectively in the online game market in China, our business, financial condition and results of

operations would be materially and adversely affected.

We and our games have been, and in the future may be, subject to negative publicity, which may discourage people from playing our games and adversely affect our business, financial condition, results of operations and prospects.

ZT Online has developed a large player base since its commercial launch in January 2006, and has therefore been the subject of a large volume of media reports and communications on the Internet by players as well as bloggers and other online commentators, some of which have been negative. ZT Online has also been the subject of criticism relating to technical problems affecting the game from time to time. Some media reports and Internet postings regarding us, our chairman and our games have been false or misleading. Although we take steps to refute and correct this false and misleading information when it comes to our attention, these efforts may not be successful. Negative publicity about our games may lead players to stop playing those games, and might also make them less willing to play any future games that we introduce, all of which could materially and adversely affect our business, financial condition, results of operations and prospects.

Our operating results fluctuate from period to period, making them difficult to predict.

Our operating results from period to period are highly dependent upon, and will fluctuate, based on the following factors:

the availability, quality and playability of our games;

the period of time over which we recognize revenue for some of our virtual items in our free-to-play games, which in certain cases is based on the estimated lifespan of our virtual items, which may be adjusted from time to time;

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the number of games that we and our competitors offer players, and our respective pricing;

changes in our game features and the corresponding impact on player behavior and purchasing patterns (for example, our changes in the monetization structure of ZT Online to reduce the number of in-game promotional activities led to a decrease in our APP in the third quarter of 2008 and cancellation of selected monetization features such as Treasury Box in the third quarter of 2009);

the quality, variety, popularity and mix of virtual items and services available for purchase in our free-to-play games and related in-game promotional efforts;

game development costs and licensing or royalty payments for games potentially licensed in the future;

the amount of overseas licensing net revenues generated through our licensing arrangements with operators of our games;

our introduction of new online games, which may attract players away from our established games, and the mix of sales of our games;

the mix of sales through our distributors (who purchase prepaid game cards at a discount to their face value) and direct sales of game points to players through our website;

the breadth and depth of our distribution network and the corresponding availability of our prepaid game cards;

the success of our advertising and promotional efforts; and

seasonality of our sales of prepaid game cards and revenue recognition based on our game players' behavior, during and around the Chinese New Year holidays in the first quarter, and the National Day holidays in the fourth quarter, when fewer of our targeted players play our games.

Due to these and other factors, our operating results will vary from period to period, will be difficult to predict for any given period, may be adversely affected from period to period and may not be indicative of our future performance.

Our limited resources may affect our ability to manage our growth.

Our growth to date has placed, and our anticipated further expansion will continue to place, a significant strain on our management, systems and resources. For example, during the period following the commercial launch of our first online game in January 2006 to December 2010, our total employees (not including liaison personnel) increased from approximately 200 to 1,844. We intend to increase our employee headcount even further, by increasing our number of research and development and customer service representatives. In addition to training and managing our workforce, we will need to continue to develop and improve our financial and management controls and our reporting systems and procedures.

We may not be able to successfully implement our growth strategies, which would materially and adversely affect our revenue, profitability and competitiveness.

We are pursuing a number of growth strategies, including developing new online games and related products and services to attract more players, enhancing existing online games to retain existing players, reorganizing our game development studios, pursuing opportunities for acquisitions and investments, expanding into markets outside of China, and entering into strategic cooperation arrangements.

For example, we are reorganizing our game development studios by establishing various subsidiaries that are generally 51% owned by us and 49% owned by the relevant development team members based on our Win@Giant incubation initiative, with an aim to facilitate our development of new online games. Each reorganized studio will focus upon producing and supporting internally developed games, and will be incentivized based upon the success of

these games. Pursuant to this reorganization, Giant Online, one of our existing MMORPGs, will be supported by Shanghai Juhuo Network Technology Co., Ltd., or Juhuo Network, and the development and subsequent supportive work for ZT Online II will be conducted by Shanghai Jujia Network Technology Co., Ltd., or Jujia Network.

In addition, in connection with the establishment of our reorganized studios, we provide loans to certain development team members to finance their capital contributions to the studios, and such loans are typically provided on an unsecured and interest free basis without any fixed term for repayment. As of December 31, 2010, the outstanding principal amount of these loans was RMB 10.8 million (US\$1.6 million). Any deterioration in the financial condition of these reorganized studios, or the game developers to whom we have made loans, may result in losses to us and could have a material adverse effect on our financial condition and results of operations.

We are also pursuing opportunities for acquisitions and investments. For example, we acquired a controlling equity interest in Hangzhou Snow Wolf Software Co. Ltd., or Snow Wolf, a game development studio, in May 2009 and we acquired the entire equity interest of Beijing Julun Network Technology Co. Ltd., or Julun Network, another game development studio, in November 2010. In addition, we have made minority investments in 51.com, a Chinese social networking site, Mobile Embedded Technology Inc., a mobile platform operating company, and Shanghai Ruichuang Network Technology Co., operator of the internet portal website www.2345.com.

We are also exploring strategic cooperation arrangements with other internet service providers. For example, in the fourth quarter of 2010, in order to explore the potential convergence between online games and other entertainment media, we established a cooperative relationship with Huayi Brothers Media Corporation, or Huayi Brothers, a diverse media, entertainment and leisure group. We sold to Huayi Brothers our controlling interest in Huayi Giant, which holds the intellectual property and development team for K III. Following the sale, Huayi Brothers holds a 51% interest in Huayi Giant, while we hold a 34% interest and the employees of Huayi Giant hold a 15% interest. In addition, in October 2009 we entered into a three year non-exclusive license agreement for ZT Online Green Edition with Shenzhen Tencent Computer Systems Company Limited, or Tencent. Pursuant to the license, Tencent operates ZT Online Green Edition on its QQ Game platform in exchange for a royalty payable to us.

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Our experience with our various new growth strategies is limited. Accordingly, we cannot assure you whether all or any of these strategies will be successful. If we are unable to implement our growth strategies, our revenue and profitability may not grow as we expect, and our competitiveness may be materially and adversely affected.

We may not sustain our historical growth rate or profitability.

We have experienced significant revenue growth in a relatively short period of time. After commercially launching our first game in January 2006, net revenues increased from RMB408.5 million in 2006 to RMB1,527.5 million in 2007 and to RMB1,594.7 million in 2008, representing a 273.9% increase in 2007 and an 4.4% increase in 2008. However, our net revenues decreased by 18.2% to RMB1,303.8 million in 2009 and increased slightly to RMB1,332.8 million in 2010. Although we believe the decrease of our net revenues in 2009 was largely due to new regulations on certain game features promulgated by the PRC government and a change of our in-game monetization features, we may not sustain our historical levels of revenue growth in future periods due to a number of different factors, including, among others, economic factors out of our control, competitiveness in the online game industry, in which market share can be quickly acquired or lost, the greater difficulty of growing at sustained rates from a larger net revenue base, the need to increase our research and product development expenses in order to develop new and successful games, the potential need to expend greater amounts in order to license or acquire new games, and our inability to prevent our other costs and operating expenses from increasing. Accordingly, you should not rely on the results of any prior period as an indication of our future operating performance.

We may be adversely affected by the slowdown of China's economy caused in part by the global crisis in the financial services and credit market starting from the second half of 2008.

We rely on the spending of our game players for our revenues, which may in turn depend on the players' level of disposable income, perceived future earnings capabilities and willingness to spend. China's economy experienced a slowdown after the second quarter of 2008, when the quarterly growth rate of gross domestic product reached 11.9%. A number of factors have contributed to this slowdown, including appreciation of the Renminbi, which has adversely affected China's exports, and tightening macroeconomic measures and monetary policies adopted by the PRC government aimed at preventing overheating of China's economy and controlling China's high level of inflation. The slowdown was further exacerbated by the recent global crisis in the financial services and credit markets, which in recent months has resulted in extreme volatility and dislocation of the global capital markets. In the first quarter of 2009, the growth rate of China's gross domestic product decreased to 6.1%, and the closing of the Shanghai Stock Exchange Composite Index dropped from its high of 6,124 reached on October 16, 2007 to 2,481 on May 21, 2010.

It is uncertain how long the global crisis in the financial services and credit markets will continue and the degree of adverse impact it will have on the global economy and the economies in China and other jurisdictions where we license our games. If our game players reduce their spending on playing our games due to such uncertain economic conditions, our net revenues may be adversely affected.

Our business may be materially harmed if we do not feature our games in a sufficient number of Internet cafés in China.

A substantial number of players access our game through Internet cafés. Due to limited space on their computer hard drives, Internet cafés generally only feature a limited number of games on their computers. We thus compete with a growing number of other online game operators to ensure that our games are featured on these computers. This competition may intensify in China due to a nationwide suspension of approval for the establishment of new Internet cafés since 2007. We have taken steps to ensure that our games are featured in a sufficient number of Internet cafés, such as maintaining good relationships with Internet café administrators, requiring our distributors to maintain a sales presence in a wide range of Internet cafés and through general sales and marketing efforts. If we fail to maintain good relationships with Internet café administrators, or if we and/or our distributors fail to successfully persuade Internet cafés to feature our online games on their computers, our business, financial condition and operating results may be materially and adversely affected.

The limited use of PCs in China and the relatively high cost of Internet access with respect to per capita gross domestic product may limit the development of the Internet in China and impede our growth.

Although the use of PCs in China has increased in recent years, the penetration rate for PCs in China is much lower than in the United States. In addition, despite a decrease in the cost of Internet access in China due to a decrease in the

cost of PCs and the introduction and expansion of broadband access, the cost of personal Internet access remains relatively high in comparison to the average per capita income in China. The PRC government has also promulgated a number of regulations to curb the growth of Internet cafés. See Intensified government regulation of Internet cafés could limit our ability to maintain or increase our net revenues and expand our customer base. The limited use of PCs in China, the relatively high cost of personal Internet access and increased restrictions on Internet cafés may limit the growth of our business. Furthermore, any Internet access or telecommunications fee increase could reduce the number of players that play our online games and materially and adversely affect our business, financial condition and results of operations.

We rely on our nationwide distribution network for a significant portion of our net revenues. Failure to maintain good relationships with our distributors could materially disrupt our business and harm our net revenues.

Online payment systems in China are still in a relatively early stage of development and are not as widely acceptable to customers in China as in the United States. As a result, although we make our prepaid game cards available for purchase online using an online payment system, our business is dependent on the performance of our regional distributors. In 2008, 2009 and 2010, 88.53%, 86.03% and 84.08%, respectively, of our sales proceeds were generated through sales of prepaid game cards to our distributors. Our largest distributor accounted for 6.1%, 6.3% and 5.6%, of our sales proceeds in 2008, 2009 and 2010, respectively. Maintaining relationships

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with existing distributors may be difficult and time-consuming. Although we typically enter into annual contracts with our distributors, our distribution agreements are not exclusive and do not prohibit our distributors from selling our competitors' game cards. Our failure to maintain good relationships with our distributors could restrict our sales channels or encourage our distributors to seek to distribute our competitors' products, each of which could materially disrupt our business and harm our net revenues. Furthermore, our growth strategy entails expanding our distribution network, which may be difficult to achieve in a timely manner or at all.

We may be unable to effectively manage our nationwide distribution network. Any failure by our distributors to operate in compliance with our distribution agreements and applicable law may result in liability to us, may interrupt the effective operation of our distribution network, may harm our games' reputation and may result in decreased net revenues.

We have limited ability to manage the activities of our distributors, who are independent from us. In addition, our distributors and the Internet cafés and other outlets in which they sell our prepaid game cards may violate our distribution agreements or the sales agreements between our distributors and the retail outlets. Such violations may include, among other things:

failure to meet minimum sales targets or penetration targets, or failure to maintain minimum price levels for our prepaid game cards in accordance with our distribution agreements;

failure to properly promote our online games in local Internet cafés and other important outlets, or failure to cooperate with our sales and marketing team's efforts in their designated territories; and

selling our prepaid game cards outside their designated territories, possibly in violation of the exclusive distribution rights that we have granted to other distributors.

Some of our distributors have committed such types of violations in the past, which resulted in our terminating our existing distribution agreements with the offending parties. If we decide to fine, suspend or terminate our distributors for acting in violation of our distribution agreements, or if the distributors fail to address material violations committed by any of their retail outlets, our ability to effectively sell our prepaid game cards in any given territory could be negatively impacted. These and similar actions could also negatively affect our games and our corporate image, possibly resulting in loss of players and a decline in sales. Additionally, we may be liable in China for legal or regulatory violations by any of our distributors.

We have significantly reduced our number of liaison personnel.

Beginning in the third quarter of 2008, we reduced our number of liaison personnel, from over 2,500 employees to approximately 1,150 employees by December 31, 2010, in order to reduce costs. We believe the reduction in our sales and marketing team will enhance our productivity while allowing us to maintain our previous ability to market our games and generate net revenues. However, the loss of part of our previous sales and marketing team may result in us being unable to sufficiently market our games, our former employees being employed by our competitors, or our remaining employees being unable to meet our productivity standards, which could materially and adversely affect our business, results of operations and financial condition.

We may be subject to administrative fines and other penalties in Taiwan.

In October 2006, we entered into a series of transactions whereby we attempted to obtain a 51% indirect equity interest in Lager Network, the Taiwan-based developer of K III and the graphics engine we use in Giant Online, and holder of the license to operate ZT Online in Hong Kong, Macau, Taiwan, Malaysia and Singapore. Our Taiwan legal counsel, Lee & Li, advised us that these transactions were void from the outset because of legal and administrative restrictions in Taiwan that apply to ownership of Taiwanese assets by PRC persons. These transactions were subsequently unwound. If the Taiwan regulators were to view our investment in Lager Network as not being void from the outset, we may be required to take further action to unwind our acquisition of Lager Network, and our rights to any consequent equity interests in Lager Network could be suspended, we could be ordered to cease and withdraw our consequent investment in Lager Network within a specified period, and we could be fined for our continued non-compliance. This could materially and adversely affect our business, results of operations and financial condition.

We could be liable for breaches of security of our website and third-party online payment system, which may have a material adverse effect on our reputation and business.

In 2008, 2009 and 2010, 11.47%, 13.97% and 15.92% of our sales proceeds respectively, were generated from sales of our game points through a third-party online payment system. In such transactions, secure transmission of confidential information, such as customers' debit and credit card numbers and expiration dates, personal information and billing addresses, over public networks, including our official game website, is essential for maintaining consumer confidence. We currently provide password protection for all of our player accounts. In addition to the general password protection, we also sell a dynamic password generator, which could be used for multiple accounts under a player's name, to better ensure the security of our players' accounts. While we have not experienced any breach of our security measures to date, such current security measures may be inadequate. In addition, we expect that an increasing number of our sales will be conducted over the Internet as a result of the growing use of online payment systems. We also expect that associated online crime will likely increase accordingly. We must therefore be prepared to increase our security measures and efforts so that our customers have confidence in the reliability of the online payment system that we use. We do not have control over the security measures of our third-party online payment operator, and its security measures may not be adequate at present or may not be adequate with the expected increased usage of online payment systems. We could be exposed to litigation and possible liability if we fail to secure confidential customer information, which could harm our reputation, ability to attract customers and ability to encourage players to purchase our game points.

Unexpected network interruptions, security breaches or computer virus attacks could have a material adverse effect on our business, financial condition and results of operations.

Any failure to maintain the satisfactory performance, reliability, security and availability of our network infrastructure may cause significant harm to our reputation and our ability to attract and maintain players. All of the game servers operating our games, and all

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of the servers handling log-in, billing and data back-up matters for us are hosted and maintained by third party service providers. Major risks involved in such network infrastructure include any break-downs or system failures resulting in a sustained shutdown of all or a material portion of our servers, including failures which may be attributable to sustained power shutdowns, or efforts to gain unauthorized access to our systems causing loss or corruption of data or malfunctions of software or hardware.

In the past, our server network has experienced unexpected outages for several hours and occasional slower performance in a number of locations in China as a result of failures by third party service providers. Our network systems are also vulnerable to damage from fire, flood, power loss, telecommunications failures, computer viruses, hacking and similar events. Any network interruption, virus or other inadequacy that causes interruptions in the availability of our online games or deterioration in the quality of access to our online games could reduce our players satisfaction and ultimately harm our business, financial condition and results of operations. In addition, any security breach caused by hackings, which involve efforts to gain unauthorized access to information or systems, or to cause intentional malfunctions or loss or corruption of data, software, hardware or other computer equipment, and the inadvertent transmission of computer viruses could have a material adverse effect on our business, financial condition and results of operations. We do not maintain insurance policies covering losses relating to our network systems and we do not have business interruption insurance.

Enhancements and rules changes to our games have resulted, and may continue to result, in players deciding not to play our games or making legal claims against us, which could materially and adversely affect our business, results of operations and financial condition.

We periodically introduce expansion packs and make changes to our games based on feedback gathered from users and in order to encourage player behavior consistent with the basic principles of our game-playing environment. For example, in the third quarter of 2009, we canceled certain in-game monetization features, of which the most important feature is virtual treasure box, which may contain in-game items worth more than the cost of the treasure box itself, and allowing players to hire in-game substitute players, which enables them to raise their characters experience levels without actually playing. We believe this change was the main reason for the subsequent temporary decrease in our active paying players, which fell by 7.9% from approximately 1,204,000 as of the quarter ended June 30, 2009 to 1,108,000 as of the quarter ended September 30, 2009. Our active paying players subsequently increased to approximately 1,138,000 in the quarter ended December 31, 2009 and continuously rose to approximately 1,693,000 in the quarter ended December 31, 2010. However, the ability for players to adjust to game enhancements or policy changes and return to playing our games may or may not occur in response to future enhancements or changes in policies we introduce, which could materially and adversely affect our business, results of operations and financial condition.

Additionally, our players may choose to litigate if they are dissatisfied with our game adjustments. For example, in May 2007 we were sued for damages in a local court by a player in Jilin Province in response to a rule change we implemented, whereby payments of gold coins on our virtual insurance policies, exchangeable for transferable virtual items, were modified to payments of gold coin vouchers, exchangeable for non-transferable virtual items. We had made this rule change to discourage selling of these virtual items on third-party auction websites, which could result in lower revenues generated for us by our games and which we believe is inconsistent with our game-playing principles. On November 30, 2007, the court dismissed the case for the failure to state a claim. While the amount of damages sought in this lawsuit was not significant, an unfavorable judgment against us could have subjected us to lawsuits from other players seeking damages based on similar claims, the aggregate of which could be substantial. Future litigation could result in substantial costs and diversion of our resources, and could disrupt our business, as well as have a material adverse effect on our financial condition and results of operations.

Undetected programming errors or defects in our games and the proliferation of cheating programs could materially and adversely affect our business, financial condition and results of operations.

Our online games may contain undetected programming errors or other defects. In addition, parties unrelated to us have in the past, and may again in the future, develop Internet cheating programs that enable our users to acquire superior features for their game characters for which they would otherwise be required to pay or otherwise earn through game play. Furthermore, certain cheating programs could cause the loss of a character's superior features

acquired by a player. The occurrence of undetected errors or defects in our games, and our failure to discover and disable cheating programs affecting the fairness of our game environment, could damage our and our games reputations and result in players being discouraged from playing our games and purchasing virtual items and services in our games. This could materially and adversely affect our business, financial condition and results of operations.

Our business depends substantially on the continuing efforts of our senior management, and our business may be severely disrupted if we lose their services.

Our future success heavily depends upon the continued services of our senior management. In particular, we rely on the expertise and experience of Yuzhu Shi, our founder, controlling beneficial owner and chief executive officer, in our business operations and game development, and rely on his personal relationships with our employees, the relevant regulatory authorities, our distributors, our advertising media and Lager Network, the developer of K III and the graphics engine we use in Giant Online and holder of the license to operate ZT Online in Hong Kong, Macau, Taiwan, Malaysia and Singapore. We do not maintain key-man life insurance for any of our senior management. If one or more of our senior management are unable or unwilling to continue in their present positions, we may not be able to replace them easily or at all. As a result, our business may be severely disrupted, our financial conditions and results of operations may be materially adversely affected, and we may incur additional expenses to recruit and train personnel.

Each of our executive officers has entered into an employment agreement with us, which contains confidentiality and non-competition provisions. If any disputes arise between our executive officers and us, we cannot assure you the extent to which any of these agreements could be enforced in China, where these executive officers reside and hold most of their assets, in light of the uncertainties with China's legal system.

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Our founder, controlling beneficial owner and chief executive officer, Yuzhu Shi, was previously involved in various enterprises, some of which were the subject of claims or legal actions.

Over the past 20 years, our founder, controlling beneficial owner and chief executive officer, Yuzhu Shi, previously founded, managed or was substantially involved in various enterprises, including Zhuhai Giant Hi-Tech Group Limited, or Zhuhai Giant, Giant Investment Co., Ltd., or Giant Investment, Shanghai Jiante Shengming Technology Co., Ltd., Shanghai Jiante Bio-Technology Co., Ltd., Ready Finance Limited, Stone Group Holdings Limited and Shanghai Youyuan Gardening Co., Ltd. Zhuhai Giant was founded by Mr. Shi in 1991, and Mr. Shi served as its president from 1992 to 1995. In 1998, Zhuhai Giant engaged in an unsuccessful real estate venture, which caused Zhuhai Giant to cease operations with significant outstanding debts and claims for repayment. Zhuhai Giant settled these claims through negotiations with the relevant claimants. In addition, Giant Investment and its subsidiaries were previously the subject of several claims, administrative actions and negative publicity relating to the alleged false advertising of one of its products. Previous or potential new claims relating to these enterprises, or negative publicity relating thereto, could divert Mr. Shi's attention from the management of our company, discourage investors or lenders from providing capital or loans that we may require in the future.

If we are unable to attract, train and retain key individuals and highly skilled employees, our business may be adversely affected.

If our business continues to expand, we will need to hire and retain additional qualified employees, including skilled and experienced online game developers. Since our industry is characterized by high demand and intense competition for talent, we may need to offer higher compensation and other benefits in order to retain key personnel in the future. In the fourth quarter of 2008, we introduced Win@Giant, an incubation program designed to attract talented employees, developers and business partners. While this program is intended to supplement and not replace our normal hiring efforts, we cannot assure you that this program will be successful or that we will be able to attract or retain the qualified game developers or other key personnel that we will need to achieve our business objectives. As a rapidly growing company, our ability to train and integrate new employees into our operations may not meet the increasing demands of our business, which could adversely affect our business and future growth prospects.

Future acquisitions may have an adverse effect on our ability to manage our business.

Selective acquisitions form part of our strategy to expand our business. For example, in the third quarter of 2008, we acquired a 25% interest in 51.com, a China based social networking company, for approximately US\$51.1 million. In the third quarter of 2009, we acquired a 20% interest in Mobile Embedded Technology Inc., a mobile platform operation company, for US\$5.0 million. In 2010, we acquired a 100% interest in Julun Network, a small game company engaged in MMORPG development. We do not, however, have significant experience integrating any new companies into ours or utilizing assets from acquired companies in our business, and we believe that integration of a new company's operation and personnel will require significant management attention. 51.com is currently operating as an independent entity from us. Should we decide to further integrate 51.com or any future acquired businesses into our business, the diversion of our management's attention from our business and any difficulties encountered in the integration process could have an adverse effect on our ability to manage our business.

We may pursue acquisitions of companies, technologies and personnel that are complementary to our existing business. However, our ability to grow through future acquisitions or investments or hiring will depend on the availability of suitable acquisition and investment candidates at an acceptable cost, our ability to compete effectively to attract these candidates, and the availability of financing to complete larger acquisitions. Since we expect the online game industry to consolidate in the future, we may face significant competition in executing our growth strategy. Future acquisitions or investments could result in potential dilutive issuances of equity securities or incurrence of debt, contingent liabilities or impairment of goodwill and other intangible assets, any of which could adversely affect our financial condition and results of operations. The benefits of an acquisition or investment may also take considerable time to develop and any particular acquisition or investment may not produce the intended benefits.

Future acquisitions would also expose us to potential risks, including risks associated with the assimilation of new operations, technologies and personnel, unforeseen or hidden liabilities, the diversion of resources from our existing businesses, sites and technologies, the inability to generate sufficient revenue to offset the costs and expenses of acquisitions and potential loss of, or harm to, our relationships with employees, customers, licensors and other

suppliers as a result of the integration of new businesses.

Unauthorized use of our intellectual property by third parties, and the expenses incurred in protecting our intellectual property rights, may adversely affect our business.

We regard our copyrights, trademarks, trade secrets and other intellectual property as critical to our success. Unauthorized use of the intellectual property used in our business may adversely affect our business and reputation.

We have historically relied on a combination of trademark and copyright law, trade secret protection and restrictions on disclosure to protect our intellectual property rights. Although we presently enter into confidentiality and invention assignment agreements with most of our employees, in the past we only required more senior employees or those in commercially or technically sensitive positions to do so. We cannot assure you that these confidentiality agreements will not be breached, that we will have adequate remedies for any breach, or that our proprietary technology will not otherwise become known to, or be independently developed by, third parties.

As of December 31, 2010, we own 286 registered trademarks in China and overseas in total and are in the process of applying for the registration of 201 trademarks in China and 50 trademarks overseas. We cannot assure you that any of these trademark applications will ultimately proceed to registration or will result in registration with scope adequate for our business. Some of our pending applications or registrations may be successfully challenged or invalidated by others. If our trademark applications are not successful, we may have to use different marks for affected services or technologies, or enter into arrangements with any third parties who may have prior registrations, applications or rights, which might not be available on commercially reasonable terms, if at all.

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Implementation of intellectual property laws in China has historically been lacking, primarily because of ambiguities in the laws and difficulties in enforcement. Accordingly, intellectual property right protection in China may not be as effective as in the United States or other countries. Policing unauthorized use of our proprietary technology, trademarks and other intellectual property is difficult and expensive, and litigation may be necessary in the future to enforce our intellectual property rights. Future litigation could result in substantial costs and diversion of our resources, and could disrupt our business, as well as have a material adverse effect on our financial condition and results of operations.

We may be subject to infringement and misappropriation claims in the future, which may cause us to incur significant expenses, pay substantial damages and be prevented from providing our services or technologies.

Our success depends, in part, on our ability to carry out our business without infringing the intellectual property rights of third parties. We may be subject to litigation involving claims of patent, copyright or trademark infringement, or other violations of intellectual property rights of third parties. In particular, the patent field covering online games and related technology is rapidly evolving and surrounded by a great deal of uncertainty, and we cannot assure you that our technologies, processes or methods would not be covered by third-party patents, either now existing or to be issued in the future. Future litigation may cause us to incur significant expenses, and third-party claims, if successfully asserted against us, may cause us to pay substantial damages, seek licenses from third parties, pay ongoing royalties, redesign our services or technologies, or prevent us from providing services or technologies subject to these claims. Even if we were to prevail, any litigation would likely be costly and time-consuming and divert the attention of our management and key personnel from our business operations.

We have no general business insurance coverage, which may result in our incurring substantial costs and the diversion of resources.

Insurance companies in China offer limited business insurance products and do not, to our knowledge, offer business liability insurance. While business interruption insurance is available to a limited extent in China, we have determined that the risks of disruption, cost of such insurance and the difficulties associated with acquiring such insurance on commercially reasonable terms make it impractical for us to subscribe for such insurance. As a result, we do not have any business liability, disruption or litigation insurance coverage for our operations in China. Except for legally required automobile liability insurance, we also do not carry any property or casualty insurance. Any business disruption or litigation, or any liability or damage to, or caused by, our facilities or our personnel may result in our incurring substantial costs and the diversion of resources.

We may be unable to maintain an effective system of internal control over financial reporting, and as a result we may be unable to accurately report our financial results or prevent fraud.

We are subject to provisions of the Sarbanes-Oxley Act of 2002. Section 404 of the Sarbanes-Oxley Act requires that we include a report from management on the effectiveness of our internal control over financial reporting in our annual reports on Form 20-F. In addition, our independent registered public accounting firm must attest to and report on the operating effectiveness of our internal control over financial reporting. While our management concluded that our internal control over financial reporting is effective as of December 31, 2010, and our independent registered public accounting firm reported on our internal controls over financial reporting, our management may conclude in the future that our internal controls are not effective. Our or our independent public accounting firm's failure to conclude that our internal control over financial reporting is effective could result in a loss of investor confidence in the reliability of our reporting processes, which could materially and adversely affect the trading price of our ADSs.

Our reporting obligations as a public company will continue to place a significant strain on our management, operational and financial resources and systems for the foreseeable future. Our failure to maintain effective internal control over financial reporting could result in the loss of investor confidence in the reliability of our financial reporting processes, which in turn could harm our business and negatively impact the trading price of our ADSs.

The successful operation of our business depends upon the performance and reliability of the Internet infrastructure and fixed telecommunications networks in China.

Our business depends on the performance and reliability of the Internet infrastructure in China. Almost all access to the Internet is maintained through state-owned telecommunication operators under the administrative control and regulatory supervision of the Ministry of Information Industry of China. In addition, the national networks in China

are connected to the Internet through international gateways controlled by the PRC government. These international gateways are the only channels through which a domestic user can connect to the Internet. Although the PRC government has pledged to improve the Internet infrastructure in China as part of its stimulus package introduced in the first quarter of 2009, a more sophisticated Internet infrastructure may not be developed in China. We or the players of our online games may not have access to alternative networks in the event of disruptions, failures or other problems with China's Internet infrastructure.

We face certain risks associated with our investment activities, including credit risks related to our held to maturity investment contracts.

We explore selected investment opportunities that may have strategic value to us or that are purely financial in nature, including investment contracts that provide us with a more favorable rate of return than ordinary bank deposits.

In addition, as of December 31, 2009 and 2010, we had held to maturity investment contracts, which we classify as short-term investments on our balance sheet, amounting to RMB 500.0 million and RMB 1,850.0 million (US\$280.3 million), respectively. Although our held to maturity investment contracts are secured or wholly guaranteed by reputable financial institutions, any deterioration in the financial condition of the secured collateral or these financial institutions could cause significant loss to us and have a material effect on our financial condition and results of operations.

For example, in April 2011, we committed to invest RMB 958.8 million (US\$145.3 million) in a privately held insurance company, though such investment remains subject to the approval of the China Insurance Regulatory Commission. We are an online game company, and our experience with investment activities is limited. As such, we may not be able to achieve an adequate rate of return and may suffer losses on our investments. If we experience significant losses in connection with our investment activities, our financial condition and results of operation may be materially and adversely affected.

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We face risks associated with the licensing of our games overseas, and if we are unable to effectively manage these risks, they could impair our ability to expand our business internationally.

As of the date of this annual report, we have granted to Lager Network the license to operate ZT Online in Hong Kong, Macau, Taiwan, Malaysia and Singapore. We have also granted an exclusive license to VinaGame Software Service Joint Stock Company, or VinaGame, to operate ZT Online in Vietnam. We granted an exclusive license to Astrum Nival, LLC, or Astrum Nival, to operate ZT Online in the Russia and other Russian speaking territories. We have signed a licensing agreement with Neonga AG, a German online game company to license Dragon Soul in the USA, Canada, and Europe excluding Russia and Russian speaking countries. In addition, we have also licensed The Golden Land to overseas market including Taiwan, Brazil, Turkey, Korea, Japan, Thailand, and North America and Europe, and licensed XT Online to Vietnam market. We may further license our existing and new games in other countries and regions. The offering of our games in the international markets could expose us to a number of risks, including:

difficulties in identifying and maintaining good relationships with licensees who are knowledgeable about, and can effectively distribute and operate our games in, international markets;

difficulties in maintaining the reputation of our company and our games, given that our games are operated by licensees in the international markets pursuant to their own standards;

difficulties in and costs of protecting our intellectual property rights internationally;

difficulties and costs relating to compliance with the different commercial and legal requirements of the international markets in which we offer our games, such as game import regulatory procedures, taxes and other restrictions and expenses;

difficulties and uncertainties in obtaining software export contract registration license from the relevant PRC authorities;

fluctuations in currency exchange rates; and

interruptions in cross-border Internet connections or other system failures.

Risks Related to the Regulation of Our Business

PRC regulations relating to our industry are evolving. Any adverse or unanticipated regulatory changes could significantly harm our business or limit our ability to operate.

Substantial uncertainties and restrictions exist with respect to the application and implementation of PRC laws and regulations in the online game industry. If the PRC government finds that our past or current structure for our business operations does not comply with PRC laws and regulations, we could be subject to severe penalties, including the shutting down of our operations.

Foreign ownership in Internet content providers, which includes online games, is subject to significant restrictions under current PRC laws and regulations. The PRC government regulates Internet access and the operation of online games through strict business licensing requirements and other laws and regulations, which also include limitations on foreign ownership in PRC companies that provide Internet content. Specifically, foreign investors are not allowed to own more than a 50% equity interest in any Internet content provider. In addition, foreign and foreign-invested enterprises are currently not able to apply for the required licenses for operating online games in China.

Because we are a Cayman Islands company, we and our PRC subsidiary are treated as foreign or foreign-invested enterprises under PRC laws and regulations. To comply with PRC laws and regulations, we operate our online games in China through a series of contractual arrangements entered into between our PRC subsidiary, Shanghai Zhengtu Information Technology Co., Ltd, or Zhengtu Information, and Shanghai Giant Network Technology Co., Ltd, or Giant Network, which is beneficially owned by certain of our officers and directors and other individuals, all of whom are PRC citizens. Giant Network holds a Telecommunications and Information Services Operating License, or ICP

license, issued by the Shanghai Municipal Information Commission, a local branch of the Ministry of Information Industry, which allows Giant Network to provide Internet content distribution services in Shanghai. This license is essential to the operation of our business.

Despite the lack of technical majority ownership, there exists a parent-subsidary relationship between our Cayman Islands Company and Giant Network through the irrevocable proxy agreement, whereby equity holders of Giant Network effectively assigned all of their voting rights underlying their equity interest to our Cayman Islands Company. We have entered into contractual arrangements with Giant Network pursuant to which Zhengtu Information, our wholly owned subsidiary, provides technical support and an exclusive software license to Giant Network. As a result of these contractual arrangements, under U.S. GAAP, we are also considered the primary beneficiary of Giant Network and, accordingly, we consolidate its historical results in our financial statements. For detailed descriptions of these contractual arrangements, see Information on the Company Organizational Structure and Major Shareholders and Related Party Transactions Related Party Transactions.

The relevant PRC regulatory authorities have broad discretion in determining whether a particular contractual structure is in violation of the law. For example, on July 26, 2006, the Ministry of Information Industry publicly released the Notice on Strengthening the Administration of Foreign Investment in Operating Value-added Telecom Business, dated July 13, 2006, or the MII Notice, which reiterates certain provisions under China's Administrative Rules on Telecommunications Enterprises prohibiting a domestic company that holds an ICP license from renting, transferring or selling a telecommunications license to a foreign investors

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in any form, or providing any resources, sites or facilities to foreign investors that intend to conduct value-added telecom business illegally in China. There is currently no official interpretation or implementation practice under the MII Notice. It remains uncertain how the MII Notice will be enforced and whether or to what extent the MII Notice may affect the legality of the corporate and contractual structures adopted by online game companies that operate in China, such as ours. We have made inquiries with officials at the Ministry of Information Industry but have not yet been able to obtain a definitive answer regarding implementation of the MII Notice and any implications for the legality of our corporate and contractual structures. If our corporate and contractual structures are deemed by the Ministry of Information Industry to be illegal, either in whole or in part, we may have to modify such structures accordingly to comply with regulatory requirements. However, we cannot assure you that we can achieve this without material disruption to our business.

On September 28, 2009, the General Administration of Press and Publications, or the GAPP, the National Copyright Administration, and National Office of Combating Pornography and Illegal Publications jointly published the Notice Regarding the Consistent Implementation of the "Stipulations on Three Provisions" of the State Council and the Relevant Interpretations of the State Commission Office for Public Sector Reform and the Further Strengthening of the Administration of Pre-examination and Approval of Internet Games and the Examination and Approval of Imported Internet Games (Xin Chu Lian [2009] No. 13), or the GAPP Notice. The GAPP Notice restates the general principle espoused in recently promulgated regulations that foreign investment is not permitted in Internet game operating businesses in China. Article IV of the GAPP Notice prohibits foreign investors from participating in Internet game operating businesses via wholly owned, equity joint venture or cooperative joint venture investments in China, and from controlling and participating in such businesses directly or indirectly through contractual or technical support arrangements. In the event of a violation of these provisions, GAPP shall, in conjunction with the relevant departments of the PRC, investigate and handle the same in accordance with the law. In serious cases, the relevant licenses and registrations shall be cancelled. However, as a detailed interpretation of the GAPP Notice has not been issued, it is not yet clear how this GAPP Notice will be implemented. Furthermore, as some other government authorities like the Ministry of Commerce, the MOC, and the MII did not join GAPP in issuing the Notice, the views of these bodies will be indefinite in clarifying the scope of implementation and enforcement of the GAPP Notice. Our PRC legal counsel, Grandall Legal Group (Shanghai), is of the view that, subject to the interpretation and implementation of the GAPP Notice, the ownership structure of Zhengtu Information and Giant Network and our contractual arrangements with Giant Network and its shareholders comply with and, immediately before our initial public offering, complied with current Chinese laws and regulations. In the opinion of our Chinese counsel, there are, however, substantial uncertainties regarding the interpretation and application of current or future Chinese laws and regulations and there may be changes and other developments in Chinese laws and regulations or their interpretations. Accordingly, Chinese government authorities may ultimately take a view that is inconsistent with the opinion of our PRC legal counsel. If the past or current ownership structures, contractual arrangements and businesses of our company, Zhengtu Information or Giant Network are found to be in violation of any existing or future PRC laws or regulations, including the MII Notice and the GAPP Notice, the relevant regulatory authorities would have broad discretion in dealing with such violations, including:

- revoking the business and operating licenses of Zhengtu Information or Giant Network, which are essential to the operation of our business;

- levying fines;

- confiscating our income or the income of Zhengtu Information or Giant Network;

- shutting down our servers or blocking our website;

- discontinuing or restricting our operations or the operations of Zhengtu Information or Giant Network;

imposing conditions or requirements with which we, Zhengtu Information or Giant Network may not be able to comply;

requiring us, Zhengtu Information or Giant Network to restructure the relevant ownership structure, operations or contractual arrangements;

restricting or prohibiting our use of the proceeds from our public offering to finance our business and operations in China; and

taking other regulatory or enforcement actions that could be harmful to our business.

Any of these events could materially and adversely affect our business, financial condition and results of operations.

The contractual arrangements with our affiliated Chinese entity and its shareholders, which relate to critical aspects of our operations, may not be as effective in providing operational control as direct ownership. In addition, these arrangements may be difficult and costly to enforce under PRC law.

We rely on and expect to continue rely on contractual arrangements with Giant Network and its shareholders in China to operate our business. For a description of these contractual arrangements, see Information on the Company Organizational Structure and Major Shareholders and Related Party Transactions Related Party Transactions. These contractual arrangements may not be as effective as direct ownership in providing us control over Giant Network. Direct ownership would allow us, for example, to directly exercise our rights as a shareholder to (i) effect changes in the board of Giant Network, which, in turn, could effect changes, subject to any applicable fiduciary obligations, at the management level, and (ii) derive economic benefits from the operations of Giant Network by causing it to declare and pay dividends. However, under the current contractual arrangements, as a legal matter, if Giant Network or its shareholders fails to perform their respective obligations under these contractual arrangements, we may have to incur substantial costs and expend significant resources to enforce those arrangements, and rely on legal remedies under PRC law. These remedies may include seeking specific performance or injunctive relief, and claiming damages, any of which may not be effective. For example, if any of Giant Network's shareholders refuses to transfer its equity interest in Giant Network to us or our

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designee when we exercise the purchase option pursuant to these contractual arrangements, or if any of those individuals otherwise act in bad faith towards us, we may have to take legal action to compel it to fulfill its contractual obligations. In addition, as Giant Network is jointly owned by its shareholders, it may be difficult for us to change our corporate structure or to bring claims against it or its shareholders if any of them fails to perform their obligations under the related contracts or does not cooperate with any such actions by us.

If (i) the relevant PRC authorities invalidate these contractual arrangements for violation of PRC laws, rules and regulations, (ii) Giant Network or its shareholders terminate the contractual arrangements or (iii) Giant Network or its shareholders fail to perform their obligations under these contractual arrangements, our business operations in China would be adversely and materially affected, and the value of your ADSs would substantially decrease. Further, if we fail to renew these contractual arrangements prior to their expiration, we would not be able to continue our business operations unless the then-current PRC law allowed us to directly operate the relevant businesses in China.

In addition, if Giant Network or all or part of their assets become subject to liens or rights of third-party creditors, we may be unable to continue some or all of our business activities, which could materially and adversely affect our business, financial condition and results of operations. If Giant Network undergoes a voluntary or involuntary liquidation proceeding, its shareholders or unrelated third-party creditors may claim rights to some or all of its assets, thereby hindering our ability to operate our business, which could materially and adversely affect our business, our ability to generate revenue and the market price of your ADSs.

All of these contractual arrangements are governed by PRC laws and provide for the resolution of disputes through arbitration in the PRC. Accordingly, these contracts would be interpreted in accordance with PRC laws and any disputes would be resolved in accordance with PRC legal procedures. The legal environment in the PRC is not as developed as in other jurisdictions, such as the United States. As a result, uncertainties in the PRC legal system could limit our ability to enforce these contractual arrangements. In the event we are unable to enforce these contractual arrangements, which relate to critical aspects of our operations, we may be unable to exert effective control over Giant Network and our ability to conduct our business may be negatively affected.

The contractual arrangements entered into among our PRC subsidiary, our affiliated entity and its shareholders may be subject to audit or challenge by the PRC tax authorities; a finding that our PRC subsidiary or our affiliated entity owes additional taxes could substantially reduce our net income and the value of your investment.

Under PRC laws and regulations, arrangements and transactions among related parties may be subject to audit or challenge by the PRC tax authorities. We could face material and adverse tax consequences if the PRC tax authorities determine that the contractual arrangements among Zhengtu Information, our PRC subsidiary, Giant Network, our affiliated entity, and Giant Network's shareholders do not represent arm's-length prices and adjust any of their income in the form of a transfer pricing adjustment. A transfer pricing adjustment could, among other things, result in, for PRC tax purposes, a reduction of expense deductions recorded by Zhengtu Information or Giant Network or an increase in taxable income, all of which could in turn increase our tax liabilities. In addition, the PRC tax authorities may impose late payment fees and other penalties on Zhengtu Information or Giant Network for under-paid taxes.

Our business benefits from certain preferential tax treatment and other government incentives. Expiration, discontinuation, or reduction of such treatment will increase our tax burden and reduce our net income.

Under certain PRC tax laws effective until December 31, 2007, the PRC government provided various incentives to domestic companies in the software and certain technology industries in China in order to encourage development of those industries. Both Zhengtu Information and Giant Network historically received preferential income tax treatments due to their status as software enterprises and high-tech enterprises located in the Caohejing Economic Development Zone of Xuhui District of Shanghai. Specifically, both entities enjoyed a reduced enterprise income tax rate of 15%, as compared to the statutory rate of 33%, and fixed-term tax exemptions and reductions prior to 2007, and with respect to Zhengtu Information, in 2007. See *Item 5. Operating and Financial Review and Prospects A. Operating Results Taxation China*. In addition, we have been receiving government financial incentives based on business taxes and VAT paid by us, and for qualification as high technology projects and expect to continue to receive them through December 31, 2014 because there are no conditions or performance-based obligations attached to these incentives other than our continued registration in our present district in Shanghai and they are not subject to refund. These incentives were granted by the Shanghai local government, and there can be no assurance that such

incentives we are currently enjoying will not be modified or challenged by the central government or the taxation authority. We received financial incentives totaling RMB63.1 million and RMB88.5 million and RMB57.4 million (US\$8.7 million) in 2008, 2009 and 2010, respectively. If these incentives are modified or otherwise challenged by any government authority, the loss will reduce our net income.

In 2007 China passed a new Enterprise Income Tax Law, or the New EIT Law, and its implementing rules, both of which became effective on January 1, 2008. The New EIT Law (i) reduces the top rate of enterprise income tax from 33% to 25%, (ii) permits companies to continue to enjoy their existing tax incentives, subject to certain transitional phase-out rules, and (iii) replaces tax incentives under the old laws with new tax incentives, subject to new qualification criteria (for example, the New EIT Law permits a new category of high- and new-technology enterprises to enjoy a reduced enterprise tax rate of 15%). Under the phase-out rules, enterprises established before the promulgation date of the New EIT Law and which were granted preferential EIT treatment under the then effective tax laws or regulations may continue to enjoy their preferential tax treatments until their expiration. Accordingly, Zhengtu Information, an enterprise established before the promulgation date of the New EIT Law, will continue to enjoy its preferential treatment under the phase-out rules. In addition, certain government authorities announced the new implementation of rules named Administrative Measures for Determination of High and New Technology Enterprises for application and assessment of high- and new-technology enterprise in April 2008 and every qualified company needs to re-apply for this qualification 3 months prior to the expiration of the valid period according to the new implementation rules. Zhengtu Information and Giant Network had

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obtained the qualification certificates of high- and new-technology enterprises status with a valid period of three years starting from 2008 to 2010. Therefore, Zhengtu Information and Giant Network will need to apply for an additional three-year extension upon the expiration of the current qualification certificate if they desire to continue to enjoy the 15% reduced rate for the calendar year of 2011. If they fail to maintain the High and New Technology Enterprise qualification, the applicable EIT rate may increase to up to 25%, which could have a material adverse effect on our results of operations. We cannot assure you that the tax authorities will not, in the future, discontinue any of our preferential tax treatments, potentially with retroactive effect. The discontinuation of any of our preferential tax treatments could materially increase our tax obligations. See *Item 5. Operating and Financial Review and Prospects A. Operating results Taxation China.*

We may be classified as a resident enterprise under the PRC New EIT Law; such classification could result in unfavorable tax consequences to us and our non-PRC shareholders.

The New EIT Law provides that enterprises established outside of China whose de facto management bodies are located in China are considered resident enterprises and are generally subject to the uniform 25% enterprise income tax rate on their worldwide income. In addition, a circular issued by the State Administration of Taxation regarding the standards used to classify certain Chinese enterprise controlled companies established outside of China as resident enterprises clarified that dividends and other income paid by such resident enterprises will be considered to be PRC source income, subject to PRC enterprise income tax, currently at a rate of 10%, when recognized by non-PRC shareholders. This circular also subjects such resident enterprises to various reporting requirements with the PRC tax authorities. Under the implementation regulations to the enterprise income tax, a de facto management body is defined as a body that has material and overall management and control over the manufacturing and business operations, personnel and human resources, finances and treasury, and acquisition and disposition of properties and other assets of an enterprise. In addition, the circular mentioned above details that certain Chinese-invested enterprises will be classified as resident enterprises if the following are located or resident in China: senior management personnel and departments that are responsible for daily production, operation and management; financial and personnel decision making bodies; key properties, accounting books, company seal, and minutes of board meetings and shareholders meetings; and half or more of the directors or senior management having voting rights. If the PRC tax authorities determine that our Cayman Island holding company is a resident enterprise, a number of unfavorable PRC tax consequences could follow. First, we may be subject to enterprise income tax at the rate of 25% on our worldwide income, as well as PRC enterprise income tax reporting obligations. Second, although under the New EIT Law and the Implementing Rules, dividends paid to us from our PRC subsidiaries would qualify as tax-exempted income, any such dividends paid to our company or our Hong Kong subsidiary may be subject to an enterprise income tax and the PRC foreign exchange control authorities have not yet issued guidance with respect to the processing of outbound remittances to entities that are treated as resident enterprises for PRC enterprise income tax purposes. Finally, dividends paid by us to our non-PRC shareholders and capital gains recognized by them with respect to the sale of our stock may be treated as income derived from sources within the PRC and as a result may be subject to a PRC income tax. Such determination could have a material adverse effect on our net income and results of operations, and may require us to withhold tax on our non-PRC shareholders. We are actively monitoring the resident enterprise classification rules and our Cayman Island holding company's facts and circumstances relative to the classification rules. Similar results could follow if our BVI subsidiary is considered a PRC resident enterprise.

PRC laws and regulations establish complex procedures for some acquisitions of Chinese companies by foreign investors, which could make it more difficult for us to pursue growth through acquisitions in China.

PRC laws and regulations, such as the M&A Rules promulgated by six PRC regulatory agencies in 2006, the Anti-Monopoly Law promulgated by the PRC National People's Congress in 2007 and the Circular on the Establishment of a National Security Review Mechanism for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors promulgated by the General Office of the PRC State Council in 2011, establish procedures and requirements that could make some acquisitions of Chinese companies by foreign investors and companies more time-consuming and complex, including requirements in some instances that various governmental authorities be notified in advance of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise. We may expand our business in part by acquiring complementary businesses. Complying with the

requirements of the relevant PRC laws and regulations to complete such transactions could be time-consuming, and any required approval processes may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share.

We and our investors face uncertainty with respect to indirect transfers of equity interests in PRC resident enterprises by their non-PRC holding companies.

In connection with the new EIT Law, the Ministry of Finance and State Administration of Taxation jointly issued, on April 30, 2009, the Notice on Issues Concerning Process of Enterprise Income Tax in Enterprise Restructuring Business, or Circular 59. On December 10, 2009, the State Administration of Taxation issued the Notice on Strengthening the Management on Enterprise Income Tax for Non-resident Enterprises Equity Transfer, or Circular 698. Both Circular 59 and Circular 698 are effective retroactively to January 1, 2008. Under the two circulars, non-PRC-resident enterprises may be subject to income tax on capital gains generated from their transfers of equity interests in PRC resident enterprises, or an Indirect Transfer. Using a substance over form principle, the PRC tax authorities have discretion under Circular 59 and Circular 698 to make adjustments to the taxable capital gains based on the difference between the fair value of the equity interests transferred and the cost of the investment. In addition, by promulgating and implementing the circulars, the PRC tax authorities have increased their scrutiny of the direct or indirect transfer of equity interests in a PRC resident enterprise by a non-PRC-resident enterprise. For example, Circular 698 specifies that the PRC State Administration of Taxation is entitled to redefine the nature of an equity transfer where offshore vehicles are interposed for tax-avoidance purposes and without reasonable commercial purpose.

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There is uncertainty as to the application of Circular 698. For example, while the term Indirect Transfer is not clearly defined, it is understood that the relevant PRC tax authorities have jurisdiction regarding requests for information over a wide range of foreign entities having no direct contact with China. Moreover, the implementation of Circular 698, such as the process and format of the reporting of an Indirect Transfer to the competent tax authority of the relevant PRC resident enterprise remains unclear. In addition, there are not any formal declarations with regard to how to determine whether a foreign investor has adopted an abusive arrangement in order to reduce, avoid or defer PRC tax. Circular 698 may be determined by the tax authorities to be applicable to our private equity financing transactions, disposal of our subsidiaries, acquisitions of complementary businesses, or disposal of shares or ADSs in our company, where non-PRC resident investors are involved. As a result, we and our non-PRC resident investors may, when doing transactions that involve the transfer of our shares or equity interests of our subsidiaries, become at risk of being taxed under Circular 698 and may be required to expend valuable resources to comply with Circular 698 or to establish that we or our non-PRC resident shareholders should not be taxed under Circular 698, which may have a material adverse effect on our financial condition and results of operations or such non-PRC resident investors investments in us.

Intensified government regulation of Internet cafés could limit our ability to maintain or increase our net revenues and expand our customer base.

Starting in 2001, the Chinese government began tightening its supervision of Internet cafés, closing unlicensed Internet cafés, requiring those remaining open to install software to prevent access to sites deemed subversive and requiring web portals to sign a pledge not to host subversive sites. In February 2007, 14 PRC national government authorities, including the Ministry of Information Industry, the Ministry of Culture and the General Administration of Press and Publication, jointly issued a notice suspending nationwide approval for the establishment of new Internet cafés beginning 2007 and enhancing the punishment for Internet cafés admitting minors. This suspension may continue indefinitely. Furthermore, the Chinese government's policy, which encourages the development of a limited number of national and regional Internet café chains and discourages the establishment of independent Internet cafés, may slow down the growth of Internet cafés.

As Internet cafés are the primary venue for users to play our games, any reduction in the number, or any slowdown in the growth, of Internet cafés in China will limit our ability to maintain or increase our net revenues and expand our customer base, which will in turn materially and adversely affect our business and results of operations.

The laws and regulations governing the online game industry in China are developing and subject to future changes. If we fail to obtain or maintain all applicable permits and approvals, our business and operations would be materially and adversely affected.

The online game industry in China is highly regulated by the Chinese government. Various regulatory authorities of the Chinese central government, such as the State Council, the GAPP, the Ministry of Culture and the Ministry of Public Security, are empowered to issue and implement regulations governing various aspects of the online game industry.

We are required to obtain various permits or approvals from different regulatory authorities in order to operate online games. For example, an Internet content provider, or ICP, must obtain an ICP license in order to engage in any commercial ICP operations within China. In addition, an online game operator must also obtain a license from the Ministry of Culture and a license from the GAPP in order to distribute games through the Internet. Some of the licenses are subject to annual inspection by relevant government authorities, such as the ICP license. If we fail to maintain any of these required permits or approvals, we may be subject to various penalties, including fines and the discontinuation or restriction of our operations. Any such disruption in our business operations would materially and adversely affect our business, financial condition and results of operations.

Since we have licensed some of our games to overseas companies for operation outside mainland China, such as ZT Online to Lager Network, VinaGame and Astrum Nival, Dragon Soul to Neonga AG, The Golden Land to overseas markets including Taiwan, Brazil, Turkey, Korea, Japan, Thailand, and North America and Europe, XT Online to the Vietnam market and we may further license our existing and new games in other countries and regions, we are required to submit our software export contracts to the data center of the Ministry of Commerce and obtain a software export contract registration license for such software exports. Failure to obtain this license may cause us to

incur penalties such as warning and restrictions on or discontinuation of our self-export operations. For the games that we commercially launched in or after 2011, such as Elsword and Allods Online, there is an additional set of regulatory requirements with which we must comply. This includes obtaining game content approval from the Ministry of Culture, completing registration with the Ministry of Commerce and the State Copyright Bureau, obtaining a software product registration certificate from the Ministry of Information Industry, and obtaining a publication approval from the General Administration of Press and Publication and other procedures or formalities which the relevant authorities further require. Any failure by us to obtain these permits or approvals may cause us to suspend operation of our online games, or otherwise cause us to incur penalties, including fines and restrictions on or discontinuation of our operations, which could materially and adversely affect our business, financial condition and results of operations

As the online game industry is at an early stage of development in China, new laws and regulations may be adopted from time to time to require additional licenses and permits other than those we currently have, and address new issues that may arise. As a result, substantial uncertainties exist regarding the interpretation and implementation of current and any future Chinese laws and regulations applicable to the online games industry. While we believe that we are in compliance with all applicable Chinese laws and regulations currently in effect with the exception of those the violation of which has been disclosed in this annual report or would not otherwise have an adverse effect on Zhengtu Information and Giant Network as a whole, we cannot assure you that we will not be found in violation of any current or future Chinese laws and regulations.

Regulation and censorship of information disseminated over the Internet in China may adversely affect our business, and we may be liable for information displayed on, retrieved from, or linked to our websites.

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In recent years, the Chinese government has adopted certain regulations governing Internet access and the distribution of news and other information over the Internet. Under these regulations, ICPs and Internet publishers are prohibited from posting or displaying over the Internet content that contradicts the fundamental principles of China's Constitution; compromises state security, divulges state secrets, subverts state power or damages national unity; harms the dignity or interests of the state; incites ethnic hatred or racial discrimination or damages inter-ethnic unity; sabotages China's religious policy or propagates heretical teachings or feudal superstitions; disseminates rumors, disturbs social order or disrupts social stability; propagates obscenity, pornography, gambling, violence, murder or fear or incites the commission of crimes; insults or slanders a third party or infringes upon the lawful rights and interests of a third party; or includes other content prohibited by laws or administrative regulations. Any person that fails to comply with these requirements may have its ICP license and other required licenses revoked and its websites shut down. In the past, failure to comply with these requirements has resulted in the closure of some websites. Website operators may also be held liable for censored information displayed on, retrieved from or linked to their websites. We believe that we are currently in compliance with the regulations and policies mentioned above. However, the Chinese government authorities may not take a view that is consistent with ours.

The Ministry of Information Industry has published regulations that subject website operators to potential liability for content included on their websites and the actions of users and others using their websites, including liability for violations of Chinese laws prohibiting the dissemination of content deemed to be socially destabilizing. The Ministry of Public Security has the authority to order any local Internet service provider, or ISP, to block any Internet website maintained outside China at its sole discretion. Periodically, the Ministry of Public Security has stopped the dissemination over the Internet of information which it believes to be socially destabilizing. The State Secrecy Bureau, which is directly responsible for the protection of State secrets of the Chinese government, is authorized to block any website it deems to be leaking State secrets or failing to meet the relevant regulations relating to the protection of State secrets in the dissemination of online information.

As these regulations are relatively new and subject to interpretation by the relevant authorities, it may not be possible for us to determine in all cases the type of content that could result in liability for us as a website operator. In addition, we may not be able to control or restrict the content of other ICPs linked to or accessible through our websites, or content generated or placed on our websites by our users, despite our attempt to monitor such content. To the extent that regulatory authorities find any portion of our content objectionable, they may require us to limit or eliminate the dissemination of such information or otherwise curtail the nature of such content on our websites, which may reduce our user traffic and have a material adverse effect on our financial condition and results of operations. In addition, we may be subject to significant penalties for violations of those regulations arising from information displayed on, retrieved from or linked to our websites, including a suspension or shutdown of our operations.

The PRC government controls virtually all Internet access in China, and requires all computers sold in China to be installed with government-designated software to censor websites deemed inappropriate by the government, which may potentially discourage or restrict the use of the Internet or our online games, and consequently adversely impact our business, financial conditions and results of operation.

The PRC government controls virtually all Internet access in China and may occasionally block Internet access throughout the country or in certain regions due to political concerns, in particular in response to, or out of concerns with respect to, special incidents or significant events, thereby preventing people in China, including our game players, from accessing the Internet and playing our online games.

On May 19, 2009, the MII issued a notice regarding the Pre-installment of Green Dam Web Filter Software on Computers. According to this notice, commencing on July 1, 2009, all computers sold in China are required to be installed with a government-designated software, called Green Dam Youth Escort, to block unhealthy words or pictures. However, according to media reports, such software may compromise the security of personal information. Given the controversy generated by this notice, the MII announced on June 30, 2009 that it would extend the deadline for the implementation of the notice. According to recent media reports, the minister of the MII further stated on August 13, 2009 that the Chinese government will not require all computers sold in China to be installed with the filter software but that computers used in schools, Internet cafes and other public places will be required to be installed with the filter software in order to prevent young people from being harmed by unhealthy online content. It is

currently unclear to what extent this notice would be implemented. Although this notice is not intended to block access to online games, if any content of our online games is found by the filter software to contain unhealthy words or pictures, our website may be blocked by the software, and as a result users who play our games will not be able to access our online games, which would have an adverse effect on our business, financial conditions and results of operation.

Compliance with the laws or regulations governing virtual currency may result in us having to obtain additional approvals or adversely affect our game operation revenues.

In June 2009, the MOC and the Ministry of Commerce jointly published the Notice on Strengthening the Administration Work of the Virtual Currency in Online Games, or the Virtual Currency Notice, to require businesses that (i) issue online game virtual currency (in the form of prepaid cards and/or pre-payment or prepaid card points) or (ii) offer online game virtual currency transaction services to apply for approval from the MOC through its provincial branches within three months following the date of such notice. The Virtual Currency Notice prohibits businesses that issue online game virtual currency from providing services that would enable the trading of such virtual currency. Any business that fails to submit the requisite application will be subject to sanctions, including but not limited to warnings, mandatory corrective measures and fines. The Virtual Currency Notice also prohibits online game operators from allocating virtual items or virtual currency to players based on random selection through lucky draw, wager or lottery which involves cash or virtual currency directly paid by the players. The Virtual Currency Notice also regulates, among other things, that game operators may not issue virtual currency to game players through means other than purchased by game players with legal currency. Moreover, any businesses that do not provide online game virtual currency transaction services are required to adopt

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technical measures to restrict the transfer of online game virtual currency among accounts of different game players. The MOC issued the Tentative Measures for Online Games Administrative, or the Online Game Measures, in June 2010, which provides, among other things, that virtual currency issued by online game operators may only be used in exchange for the operator's own online game products and services and may not be used to pay for the products and services of other entities. The above restrictions may limit our ability to maintain or increase our revenues and adversely affect our results of operations and business prospects.

Regulations relating to offshore investment activities by PRC residents may increase our administrative burdens and create regulatory uncertainties that could restrict our overseas and cross-border investment activity, and a failure by our shareholders who are PRC residents to make any required applications and filings pursuant to such regulations may prevent us from being able to distribute profits and could expose us and our PRC resident shareholders to liability under PRC law.

A Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Return Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies, or Notice 75, was promulgated by the PRC State Administration of Foreign Exchange, or SAFE, in October 2005 that requires registration with the local SAFE in connection with direct or indirect offshore investments by PRC residents. The regulation applies to our shareholders who are PRC residents and also applies to our offshore acquisitions.

The Notice 75 retroactively requires registration by March 31, 2006 of direct or indirect investments previously made by PRC residents in offshore companies. SAFE issued subsequent guidance to its local branches for implementing Notice 75. The guidance standardizes more specific and stringent supervision on the registration relating to Notice 75. Specifically it requires PRC residents holding any equity interest in offshore companies, directly or indirectly, controlling or nominal, to make registration with SAFE and imposes obligations on the PRC subsidiaries of offshore companies to facilitate and urge registrations by relevant PRC residents and to file with SAFE the stock options granted by offshore companies to any PRC resident. The registration and filing procedures under Notice 75 are prerequisites for other approval and registration procedures necessary for capital inflow from the offshore entity, such as inbound investments or shareholders loans, or capital outflow to the offshore entity, such as the payment of profits or dividends, liquidation distributions, equity sale proceeds, or the return of funds upon a capital reduction.

We have already notified our shareholders, and the shareholders of the offshore entities in our corporate group, who are PRC residents to urge them to make the necessary applications and filings as required under this regulation. However, as a result of uncertainty concerning the reconciliation of the new regulation and ambiguities in SAFE registration procedures for registering PRC residents' share obtained from exercise of share options, 190 PRC individuals in all who have exercised their options to purchase our ordinary shares in accordance with our Employee Share Option Scheme in 2010 are currently unable to register their share ownership with Shanghai SAFE. These individuals are actively communicating with Shanghai SAFE to seek alternative solutions. We do not expect that the inability by those individuals to register share ownership with Shanghai SAFE will have a material adverse effect on our business. We are committed to complying, and to ensuring that our shareholders who are subject to the regulation comply, with the relevant rules. However, we