



Kingsoft Corporation Limited

金山軟件有限公司

(Continued into the Cayman Islands with limited liability)

(Stock Code: 3888)

Announcement of Unaudited Results For the Three Months Ended September 30, 2008

The Board (“Board”) of directors (the “Directors”) of Kingsoft Corporation Limited (the “Company”) announces the unaudited results of the Company and its subsidiaries (the “Group”) for the three months ended September 30, 2008. This announcement is made as part of the Group’s current practice to publish its quarterly financial results and pursuant to Rule 13.09 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

FINANCIAL HIGHLIGHTS

| | For the three months ended | | | YoY* change % | QoQ* change % |
|--|---|--|---|---------------------|---------------------|
| | September 30, 2007 <i>RMB’000</i> (<i>unaudited</i>) | June 30, 2008 <i>RMB’000</i> (<i>unaudited</i>) | September 30, 2008 <i>RMB’000</i> (<i>unaudited</i>) | | |
| Revenue | 146,957 | 171,769 | 216,956 | 48 | 26 |
| Profit attributable to equity holders of the Company** | 29,974 | 50,823 | 102,868 | 243 | 102 |
| | <i>RMB cent</i> | <i>RMB cent</i> | <i>RMB cent</i> | | |
| Basic earnings per share | 3.48 | 4.76 | 9.68 | 178 | 103 |
| Diluted earnings per share | 3.33 | 4.55 | 9.18 | 176 | 102 |

* YoY change % represents a comparison between the current reporting period and the same period last year. QoQ change % represents the comparison between the current reporting period and the previous period.

** Profit attributable to equity holders of the Company excluding the effect of share-based compensation cost is RMB115.2 million, RMB62.0 million and RMB58.0 million for the three months ended at September 30, 2008, June 30, 2008 and September 30, 2007, respectively. This represents a YoY increase of 99% and QoQ increase of 86%.

OPERATIONAL HIGHLIGHTS

| | For the three months ended | | | YoY change % | QoQ change % |
|--|----------------------------|------------------|-----------------------|--------------------|--------------------|
| | September 30, 2007 | June 30, 2008 | September 30, 2008 | | |
| Online Games | | | | | |
| Daily Average Peak Concurrent Users | 529,794 | 846,180 | 990,855 | 87 | 17 |
| Monthly Average Paying Users | 1,035,371 | 1,036,692 | 1,239,609 | 20 | 20 |
| Monthly Average Revenue per Paying User in RMB | 31 | 34 | 40 | 29 | 18 |
| Online Services of Internet securities | | | | | |
| Daily Average Paying Users | 6,505,150 | 8,696,519 | 8,657,001 | 33 | 0 |
| Monthly Average Revenue per Paying User in RMB | 1.4 | 1.6 | 1.7 | 21 | 6 |

The Board announces the unaudited results of the Group for the three months ended September 30, 2008.

The unaudited condensed consolidated income statement, and unaudited condensed consolidated balance sheet of the Group are listed below:

CONDENSED CONSOLIDATED INCOME STATEMENT

| | For the three months ended | | |
|--|-----------------------------------|--------------------|-------------------------------|
| | September 30, 2007 | June 30, 2008 | September 30, 2008 |
| | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i> |
| | <i>(Unaudited)</i> | <i>(Unaudited)</i> | <i>(Unaudited)</i> |
| Revenue: | | | |
| Entertainment software | 101,183 | 107,849 | 148,916 |
| Applications software | 45,607 | 62,361 | 64,472 |
| Others | 167 | 1,559 | 3,568 |
| | <u>146,957</u> | <u>171,769</u> | <u>216,956</u> |
| Cost of revenue | <u>(24,150)</u> | <u>(24,721)</u> | <u>(29,036)</u> |
| Gross profit | 122,807 | 147,048 | 187,920 |
| Research and development costs, net of government grants | (20,335) | (30,301) | (28,463) |
| Selling and distribution costs | (31,627) | (44,718) | (40,944) |
| Administrative expenses | (13,301) | (18,573) | (21,342) |
| Share-based compensation costs | (28,115) | (11,165) | (12,350) |
| Other operating costs | (146) | (1,973) | (1,675) |
| Other income and gains | (10) | 240 | 12,500 |
| | <u>29,273</u> | <u>40,558</u> | <u>95,646</u> |
| Operating profit | 29,273 | 40,558 | 95,646 |
| Finance income | 2,642 | 5,830 | 6,464 |
| Share of gain/(loss) of an associate | (937) | 8,233 | 7,367 |
| Share of loss of a jointly-controlled entity | — | (288) | (359) |
| | <u>30,978</u> | <u>54,333</u> | <u>109,118</u> |
| Profit before tax | 30,978 | 54,333 | 109,118 |
| Income tax expense | (3,621) | (4,358) | (6,849) |
| | <u>27,357</u> | <u>49,975</u> | <u>102,269</u> |
| Profit for the period | <u>27,357</u> | <u>49,975</u> | <u>102,269</u> |

CONDENSED CONSOLIDATED INCOME STATEMENT (CONTINUED)

| | For the three months ended | | |
|--|---|---|---|
| | September 30, 2007 <i>RMB'000</i> <i>(Unaudited)</i> | June 30, 2008 <i>RMB'000</i> <i>(Unaudited)</i> | September 30, 2008 <i>RMB'000</i> <i>(Unaudited)</i> |
| Attributable to: | | | |
| Equity holders of the Company | 29,974 | 50,823 | 102,868 |
| Minority interests | (2,617) | (848) | (599) |
| | <u>27,357</u> | <u>49,975</u> | <u>102,269</u> |
| | <i>RMB</i> | <i>RMB</i> | <i>RMB</i> |
| Earnings per share attributable to ordinary equity holders of the Company | | | |
| Basic | 0.0348 | 0.0476 | 0.0968 |
| Diluted | 0.0333 | 0.0455 | 0.0918 |

CONDENSED CONSOLIDATED BALANCE SHEET

| | As at September 30, 2008 <i>RMB'000</i> <i>(Unaudited)</i> | As at December 31, 2007 <i>RMB'000</i> <i>(Audited)</i> |
|--|--|---|
| ASSETS | | |
| Non-current assets | | |
| Property, plant and equipment | 270,101 | 45,446 |
| Intangible assets | 31,337 | 14,281 |
| Lease prepayment | 7,179 | 7,304 |
| Interest in an associate | 18,697 | 1,014 |
| Interest in a jointly-controlled entity | 1,753 | — |
| Loan receivables | 1,267 | 1,784 |
| Deferred tax assets | 60,971 | 52,814 |
| Deferred cost | 719 | 1,890 |
| Long-term prepayments | 5,589 | — |
| | <u>397,613</u> | <u>124,533</u> |
| Current assets | | |
| Inventories | 4,118 | 2,019 |
| Trade receivables | 88,153 | 60,226 |
| Prepayments and other receivables | 43,849 | 47,743 |
| Income tax receivable | 128 | 522 |
| Deferred cost | 6,956 | 8,939 |
| Due from related parties | — | 9,862 |
| Credit-linked deposits | 108,140 | — |
| Cash and cash equivalents | 951,217 | 1,246,077 |
| | <u>1,202,561</u> | <u>1,375,388</u> |
| Current liabilities | | |
| Trade payables | 7,836 | 7,120 |
| Dividend Payables | 392 | — |
| Accrued expenses and other payables | 123,588 | 147,062 |
| Deferred revenue | 171,440 | 162,002 |
| Income tax payable | 14,506 | 6,047 |
| | <u>317,762</u> | <u>322,231</u> |
| Net current assets | <u>884,799</u> | <u>1,053,157</u> |
| Total assets less current liabilities | <u>1,282,412</u> | <u>1,177,690</u> |

CONDENSED CONSOLIDATED BALANCE SHEET (CONTINUED)

| | As at September 30, 2008 <i>RMB'000</i> <i>(Unaudited)</i> | As at December 31, 2007 <i>RMB'000</i> <i>(Audited)</i> |
|--|--|---|
| Total assets less current liabilities | <u>1,282,412</u> | <u>1,177,690</u> |
| Non-current liabilities | | |
| Deferred revenue | 33,177 | 29,726 |
| Deferred tax liabilities | <u>21,816</u> | <u>14,307</u> |
| | <u>54,993</u> | <u>44,033</u> |
| Net assets | <u><u>1,227,419</u></u> | <u><u>1,133,657</u></u> |
| Represented by: | | |
| Equity attributable to equity holders of the parent | | |
| Issued capital | 4,347 | 4,322 |
| Share premium | 773,355 | 735,510 |
| Shares held for Share Award Scheme | (25,012) | — |
| Ordinary shares subscribed | — | 319 |
| Statutory reserves | 57,570 | 57,570 |
| Employee share-based capital reserve | 184,757 | 144,741 |
| Foreign currency translation reserve | (69,083) | (28,918) |
| Retained earnings | 289,599 | 101,953 |
| Proposed dividend | <u>—</u> | <u>95,710</u> |
| | <u>1,215,533</u> | <u>1,111,207</u> |
| Minority interests | <u>11,886</u> | <u>22,450</u> |
| Total equity | <u><u>1,227,419</u></u> | <u><u>1,133,657</u></u> |

Notes

1. Basis of preparation and accounting policies

Basis of preparation

The unaudited condensed consolidated quarterly financial statements do not include all the information and disclosures required in the annual financial statements and should be read in conjunction with the Group's audited financial statements for the year ended December 31, 2007.

Significant accounting policies

The accounting policies adopted in the preparation of the unaudited condensed consolidated quarterly financial statements are consistent with those followed in the preparation of the Group's audited financial statements for the year ended December 31, 2007, with the addition of the accounting policies described below:

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments or financial guarantee contracts. Gains or losses on investments of these financial assets are recognised in the income statement. The net fair value gain or loss recognised in the income statement does not include any dividends or interest earned on these financial assets, which are recognised in accordance with the policies set out for "Revenue recognition".

Where a contract contains one or more embedded derivatives, like credit-linked deposits, the entire hybrid contract may be designated as financial asset at fair value through profit or loss, except where the embedded derivative does not significantly modify the cash flows or it is clear that separation of the embedded derivative is prohibited.

Acquisitions of minority interests

Acquisitions of minority interests are accounted for using the entity concept method, whereby, the difference between the consideration and the book value of the share of the net assets acquired is recognised as a deduction of equity.

Interest in a jointly-controlled entity

A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's interests in the jointly-controlled entity are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses. The Group's share of the post-acquisition results and reserves of the jointly-controlled entity is included in the consolidated income statement and consolidated reserves, respectively.

Business combinations and goodwill

Business combinations are accounted for using the purchase method.

Goodwill is initially measured at cost being the excess of the cost of the business combination over the Group's share in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Intangible assets (other than research and development costs and goodwill)

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortised over the following estimated useful economic lives:

| | |
|-------------------------|-----------|
| Software | 1–5 years |
| Customers relationships | 4–5 years |
| Non-compete agreements | 4–5 years |
| Contract backlog | 1–2 years |

Intangible assets with finite lives are assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at each balance sheet date.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangible assets are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for on a prospective basis.

2. Business combinations

On July 31, 2008, the Group acquired the business of Shenzhen Zhaoshangzhuoer Infogate Co., Ltd. (“Shenzhen ZSZE”), an unlisted company specialising in the manufacture of Unified Threat Management (“UTM”) defense system products. According to the acquisition contract, the business acquired was defined as “INFOGATE Business”.

The fair value of the identifiable assets of the INFOGATE Business as at the date of acquisition and the corresponding carrying amounts immediately before the acquisition were:

| | Fair value recognised on acquisition <i>RMB'000</i> <i>(Unaudited)</i> | Previous carrying amount <i>RMB'000</i> <i>(Unaudited)</i> |
|---|--|--|
| Property, plant and equipment | 354 | 544 |
| Inventories | 1,591 | 1,865 |
| Customers relationships | 1,040 | — |
| Non-compete agreements | 1,120 | — |
| Software | 5,670 | — |
| In-process research and development project | 2,490 | — |
| Contract backlog | 130 | — |
| Trade name | 300 | — |
| Net assets | <u>12,695</u> | <u>2,409</u> |
| Goodwill arising on acquisition | <u>1,825</u> | |
| Total consideration, satisfied by cash | <u><u>14,520</u></u> | |

RMB'000
(Unaudited)

| | |
|--|-----------------|
| Cash flow on acquisition: | |
| Cash and bank balances acquired | — |
| Cash paid | (1,591) |
| | <hr/> |
| Net cash outflow in the three months ended September 30, 2008 | (1,591) |
| Cash payable | (12,929) |
| | <hr/> |
| Net cash outflow in respect of the acquisition of a business unit | (14,520) |
| | <hr/> <hr/> |

From the date of acquisition, INFOGATE Business has led to RMB276 thousand (unaudited) loss to the Group.

3. Post balance sheet events

Under the 2008 Share Award Scheme, the Company awarded 9,450,000 shares to the selected employees in October, 2008. Most of the awarded shares were subject to vesting over three years and performance conditions.

MANAGEMENT DISCUSSION AND ANALYSIS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2008

Revenue

The Group's revenue increased by 26% quarter-over-quarter and increased by 48% year-over-year to RMB217.0 million. Revenue from the entertainment and applications software businesses represented 69% and 30%, respectively, of the Group's total revenue.

Revenue from the entertainment software business increased by 38% quarter-over-quarter and increased by 47% year-over-year to RMB148.9 million.

Daily average peak concurrent users, a measure we use to monitor the popularity of the Group's massively multi-player online role playing games ("MMORPGs"), increased by 17% quarter-over-quarter and increased by 87% year-over-year to 1.0 million. The number of monthly average paying users increased by 20% quarter-over-quarter and increased by 20% year-over-year to 1.2 million. This quarter-over-quarter increase in monthly paying users and daily average peak concurrent users resulted from the expanded player base of JX Online World, which started unlimited close beta testing in June and then open beta testing in October.

The monthly average revenue per paying user ("monthly ARPU") for the Group's MMORPGs increased by 18% quarter-over-quarter and increased by 29% year-over-year to RMB40.

Revenue from the applications software business increased by 3% quarter-over-quarter and increased by 41% year-over-year to RMB64.5 million. The quarter-over-quarter increase primarily due to the increased sales of WPS. The year-over-year increase was primarily due to an increase in the number of subscribers for online services of Kingsoft Internet Security to 8.7 million daily average paying users. This increase in users represents a 33% year-over-year increase in daily average paying users. The number of subscribers for online services of Kingsoft Internet Security was impacted by increasing competition in China and held flat quarter-over-quarter.

Monthly ARPU for online services of Kingsoft Internet Security business increased by RMB0.1 quarter-over-quarter and increased by RMB0.3 year-over-year. This increase resulted primarily from the increased proportion of SMS subscribers with higher monthly ARPU.

Gross Profit and Cost of Revenue

The Group's gross profit increased by 28% quarter-over-quarter and increased by 53% year-over-year to RMB187.9 million. The Group's gross profit margin increased by one percentage point quarter-over-quarter and increased by three percentage points year-over-year to 87%.

The Group's cost of revenue increased by 17% quarter-over-quarter and increased by 20% year-over-year to RMB29.0 million primarily due to increased revenue from MMORPGs and online services of Kingsoft Internet Security.

Research and Development Costs

The Group's research and development costs, net of government grants decreased by 6% quarter-over-quarter and increased by 40% year-over-year to RMB28.5 million. The quarter-over-quarter decrease primarily due to the recognition of government grants related to specific research projects amounted to RMB2.8 million during the reporting period. The research and development costs before government grants remained nearly unchanged quarter-over-quarter and increased by 35% year-over-year to RMB31.2 million. The year-over-year increase mainly resulted from (i) a company-wide raise in salaries and benefits and (ii) an overall increase in research and development headcount.

Selling and Distribution Costs

The Group's selling and distribution expenses decreased by 8% to RMB40.9 million quarter-over-quarter primarily due to the reduced marketing and promotion of the First Myth II and JX Online World in this quarter. It increased by 29% year-over-year primarily due to marketing activities for the open beta testing of JX Online World.

Administrative Expenses

The Group's administrative expenses increased by 15% quarter-over-quarter and increased by 60% year-over-year to RMB21.3 million primarily due to increased professional fees, a general raise in employee salary costs and benefits, increased depreciation and amortisation charges and increased administrative office expenses, which were mainly rental costs and utilities expenses.

Share-based Compensation Costs

The Group's share-based compensation costs increased by 11% quarter-over-quarter and decreased by 56% year-over-year to RMB12.4 million. The quarter-over-quarter increase was resulted from that 5,079,000 shares were awarded on June 26, 2008 under the Share Award Scheme.

Operating Profit Excluding Share-based Compensation Costs

The Group's operating profit excluding share-based compensation costs increased by 109% quarter-over-quarter and 88% year-over-year to RMB108.0 million as a result of the combination of above reasons and the increased government grants recognised as other income and gains. The margin of operating profit excluding share-based compensation costs improved by twenty percentage points quarter-over-quarter and eleven percentage points year-over-year to 50%.

Share of Gain/Loss of an Associate

The Group's share of gain of an associate decreased by 11% quarter-over-quarter to RMB7.4 million from RMB8.2 million of the previous quarter as a result of increased selling and distribution costs related to Meng Xiang Shi Jie, the first game launched by Kingsoft Guangzhou, while we recorded a loss of RMB0.9 million for the same quarter of 2007.

Income Tax Expense

The Group's income tax expenses increased by 57% quarter-over-quarter and increased by 89% year-over-year to RMB6.8 million primarily due to the increase of the group's profit.

The effective income tax rate (excluding the impact of share-based compensation charges) was 5.6% for this quarter, 6.7% for last quarter and 6.1% for the same quarter 2007, respectively.

Profit Attributable to Equity Holders of the Company

For the reasons described above, the Group's profit attributable to equity holders of the Company increased by 102% quarter-over-quarter and increased by 243% year-over-year to RMB102.9 million.

Profit Attributable to Equity Holders of the Company before Share-based Compensation Costs

Profit attributable to equity holders of the Company before share-based compensation costs, which is defined as profit attributable to equity holders excluding the effect of share-based compensation costs attributable to the equity holders, a measure supplementary to the consolidated financial statements presented in accordance with International Financial Reporting Standards ("IFRSs").

We believe the profit attributable to equity holders of the Company before share-based compensation costs will enhance investors' overall understanding of the Company's operating performance. When assessing our operating performance, you should not consider this data in isolation or as a substitute for our profit or any other operating performance measure that is calculated in accordance with IFRSs. In addition, our profit attributable to equity holders of the Company before share-based compensation costs may not be comparable to similarly titled measures utilised by other companies.

The Group's profit attributable to equity holders of the Company before share-based compensation costs increased by 86% quarter-over-quarter and increased by 99% year-over-year to RMB115.2 million. The net profit margin excluding the effect of share-based compensation costs was 53%, 36% and 39% for the three months ended September 30, 2008, June 30, 2008 and September 30, 2007, respectively.

Liquidity and Financial Resource

The Group had a strong cash position towards the end of the reporting period. As at September 30, 2008, the Group had major financial resources in the forms of cash and cash equivalent, time deposits with initial term of over three months and credit-linked deposits amounting to RMB713.8 million, RMB237.4 million, RMB108.1 million, respectively, which totally represented 66% of the Group's total assets.

As at September 30, 2008, the Group's gearing ratio, which represents total liabilities divided by total assets, was 23%, remained unchanged as at June 30, 2008. As at September 30, 2008, the Group did not have any borrowings from banks or other institutions.

Foreign Currency Risk Management

Certain expenses of the Group were denominated in currencies other than the RMB. The Group generated foreign currency revenue from license sales made in other Asia countries. As the exchange rates of RMB against US dollar kept relative strong during the reporting period, the Group sold US dollar for RMB upon receiving US dollar revenue. Besides, the Group adopted "natural immunity" method to match the income and payment in foreign currencies by arranging some expenses and expenditures denominated in foreign currencies.

As at September 30, 2008, RMB516.9 million of the Group's financial assets were held in deposits and investments denominated in non-RMB currencies. There is a risk that we may experience a loss as a result of any foreign currency exchange rate fluctuations in connection with our deposits and investments.

Deferred Revenue

Deferred revenue (including current and non-current portion) increased by 10% quarter-over-quarter and increased by 22% year-over-year to RMB204.6 million as at September 30, 2008, which primarily resulted from the increased sales of the prepaid cards related to online games.

Net Cash Generated from Operating Activities

The Group's cash and cash equivalent and credit-linked deposits increased by 3% quarter-over-quarter to RMB1,059.4 million as a combined result of net cash inflows from operating activities and payments for the acquisition of a new office in Beijing and the construction of Zhuhai Research Center, and purchased shares under the Share Award Scheme.

Cash generated from our operating activities reflects our profit for the three months periods, as the case may be, as adjusted for non-cash items, such as depreciation, amortisation of capitalised software costs, and share-based compensation costs, as well as the effect of changes in certain balance sheet items, such as deferred revenue and accrued expenses and other payables. The Group's net cash generated by operating activities was RMB124.5 million, RMB78.5 million and RMB75.6 million for the three months ended September 30, 2008, June 30, 2008 and September 30, 2007, respectively.

Capital Expenditures

Capital expenditures represent cash payments for acquisition of property, fixed assets and intangible assets such as software. Cash used for capital expenditures was RMB69.1 million, RMB169.6 million and RMB11.4 million for the three months ended September 30, 2008, June 30, 2008 and September 30, 2007, respectively. For the three months ended September 30, 2008, we incurred more capital expenditures related to the purchase of the new office property in Beijing and the construction of the Zhuhai Research Center.

Management Comments

Pak Kwan Kau, the Chairman and CEO of the Company is pleased to report a very encouraging quarter, as the Group's revenue and net profit attributable to equity holders grew by 48% and 243% respectively over the same period last year. Mr. Kau said, "I am very satisfied with the phenomenal success of JX Online World, which has carried on the legend and influence of JX franchise, our flagship contents and the origin of Kingsoft games. In September, all of JX games inclusive of JX Online I, JX Online II and JX Online World made a combined daily average peak concurrent users of over three quarters of a million in China and overseas. The continuous success of JX self-speaks Kingsoft's leadership in producing top-quality martial arts games."

By Order of the Board
Kingsoft Corporation Limited
Pak Kwan KAU
Chairman

The PRC, November 26, 2008

As at the date of this announcement, the Executive Directors are Messrs. Pak Kwan KAU and Donghui WANG; the Non-executive Directors are Messrs. Jun LEI, Choon Chong TAY, Wai Ming WONG and Wing Chung Anders CHEUNG; the Independent Non-Executive Directors are Messrs. Shun Tak WONG, Guangming George LU and Mingming HUANG.