

Giant Interactive Group Inc.
Form 20-F
April 18, 2013
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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, 2012

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to .

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

Commission file number: 001-33759

Giant Interactive Group Inc.

(Exact name of Registrant as specified in its charter)

Not applicable

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(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)

Jazy Zhang Chief Financial Officer

11/F, No. 3 Building, 700 Yishan Road

Shanghai, 200233,

People's Republic of China

Telephone: (86 21) 3397 9999

Facsimile: (86 21) 3397 9948

(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

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: 239,252,672 ordinary shares, par value US\$0.0000002 per share.

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer.

Large accelerated filer Accelerated filer Non-accelerated filer

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 Other

by the International Accounting Standards Board

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., and, unless the context requires otherwise, its predecessor entities and subsidiaries, and its consolidated affiliated entities;

Eddia International refers to Eddia International Group Limited;

Giant HK refers to Giant Interactive (HK) Limited;

Giant Network refers to Shanghai Giant Network Technology Co., Ltd.;

PRC subsidiaries refers to subsidiaries of our Company that are organized and existing under the laws of PRC, consisting of:

Shanghai Zhengtu Information Technology Co., Ltd., or Zhengtu Information,

Zhuhai Zhengtu Information Technology Co., Ltd., or Zhuhai Zhengtu,

Hangzhou Snow Wolf Software Co., Ltd., or Snow Wolf Software,

Shanghai Zhengduo Information Technology Co., Ltd., or Zhengduo Information,

Shanghai Jujia Network Technology Co., Ltd., or Jujia Network,

Shanghai Juhuo Network Technology Co., Ltd., or Juhuo Network,

Beijing Giant Zhengtu Network Technology Co., Ltd., or Beijing Giant Zhengtu,

Chengdu Jufan Network Technology Co., Ltd., or Jufan Network,

Shanghai Zhengju Information Technology Co., Ltd., or Zhengju Information,

Shanghai Juquan Network Technology Co., Ltd., or Juquan Network,

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Shanghai Juhuan Network Technology Co., Ltd., or Juhuan Network, and

Shanghai Jujia Network Technology Co., Ltd. (II), or Jujia Network II;

PRC entities refers to PRC subsidiaries, and Giant Network and its consolidated entities, as defined hereinafter;

Giant Network and its consolidated entities refers to Giant Network, its subsidiaries and consolidated variable interest entities, which are outlined as follows:

Giant Network,

Subsidiaries of Giant Network,

Shanghai Juxin Network Technology Co., Ltd., or Juxin Network,

Beijing Julun Network Information Technology Co., Ltd., or Julun Network,

Shanghai Juzi Information Technology Co., Ltd., or Juzi Information,

Shanghai Jujia Network Technology Co., Ltd. (III), or Jujia Network III,

Shanghai Juhe Network Technology Co., Ltd., or Juhe Network,

Consolidated variable interest entities of Giant Network that are associated with Glorious Mission, our first self-developed first person shooter game project,

Wuxi Glorious Mission Co., Ltd., or Wuxi Network,

Wuxi Tiema Network Technology Co., Ltd., or Tiema Network,

Beijing Giant Glorious Mission Network Technology Co., Ltd., or Beijing Giant,

Wuxi Tiequan Network Technology Co., Ltd., or Tiequan Network,

Shanghai Giant Glorious Mission Network Technology Co., Ltd., or Shanghai Giant, and

Bengbu Giant Glorious Mission Network Technology Co., Ltd., or Bengbu Giant;

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

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quarterly average concurrent users, or ACU, of any of our games is the average of monthly average concurrent users, as defined above, 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 accounts 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 Zheng Tu Online, or 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 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;

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

virtual currency refers to a form of online platform currency which is made available for purchase through game operator's platform, website or prepaid cards and which may be exchanged for virtual coins within different games but which has no real value and may not be converted or exchanged for any real world goods, real world services or hard currency. By way of example and clarification, game points are virtual currency in our game platform; and

virtual coins refer to our in-game currency which exists in each specific game, upon redemption of game points by players at a fixed exchange rate determined by the Company, and can be used to purchase in-game virtual items and services within the game.

This annual report on Form 20-F includes our audited consolidated balance sheets as of December 31, 2011 and 2012, and the related consolidated statements of operation and comprehensive income, cash flows and changes in shareholders' equity of each of the years ended December 31, 2010, 2011 and 2012.

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 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 ability to anticipate and manage internet access fees and server maintenance costs;

our intentions regarding management of our employees;

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;

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

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 these forward-looking statements turns out to be incorrect, actual results may differ from the results suggested by the forward-looking statements based on these assumptions. You should not place undue reliance on these forward-looking statements.

The forward-looking statements in this annual report relate only to events or information as of the date of 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 of this annual report. 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.

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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 statement of operations and comprehensive income data for each of the three years in the period ended December 31, 2012, and the selected consolidated balance sheet data as of December 31, 2011 and 2012, were derived from our consolidated financial statements, which have been audited by Ernst & Young Hua Ming LLP, an independent registered public accounting firm. The report of Ernst & Young Hua Ming LLP, as well as our audited consolidated financial statements for the years ended December 31, 2010, 2011 and 2012, are included elsewhere in this annual report. The selected consolidated statements of operations and comprehensive income data for the years ended December 31, 2008 and 2009, and our consolidated balance sheets data as of December 31, 2008, 2009 and 2010, have been derived from our audited consolidated financial statements that are not included in this annual report.

Our consolidated financial statements are prepared and presented in accordance with U.S. GAAP. Our historical results do not necessarily indicate our results expected for any future periods. You should read the selected consolidated financial data in conjunction with the consolidated financial statements and the related notes included under Item 18. Financial Statements and Item 5. Operating and Financial Review and Prospects

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	2008	2009	Year Ended December 31,		2012	
	RMB	RMB	2010	2011	RMB	US\$
			RMB	RMB		
	(In thousands, except per share and per ADS data)					
Net revenue:						
Online games	1,589,676	1,293,018	1,289,481	1,701,343	2,074,950	333,052
Licensing revenues	4,391	10,687	42,667	54,538	52,186	8,376
Other revenue, net	612	130	668	36,336	24,758	3,974
Total net revenue	1,594,679	1,303,835	1,332,816	1,792,217	2,151,894	345,402
Cost of services	(217,899)	(204,070)	(199,122)	(257,246)	(288,361)	(46,285)
Gross profit	1,376,780	1,099,765	1,133,694	1,534,971	1,863,533	299,117
Operating (expenses) income:						
Research and product development	(88,539)	(113,354)	(186,037)	(230,209)	(326,793)	(52,454)
Sales and marketing	(241,575)	(119,600)	(143,006)	(169,982)	(146,452)	(23,507)
General and administrative	(141,786)	(121,446)	(119,447)	(103,727)	(148,708)	(23,869)
Government financial incentives	63,084	88,460	57,386	47,746	63,644	10,216
Impairment of intangible assets			(46,558)			
Total operating expenses	(408,816)	(265,940)	(437,662)	(456,172)	(558,309)	(89,614)
Income from operations	967,964	833,825	696,032	1,078,799	1,305,224	209,503
Interest income	184,964	102,200	136,098	141,587	105,833	16,987
Investment income (loss)	1,171	(5,971)		3,048	(243,627)	(39,105)
Unrealized loss on investment held-for-trading	(300)					
Other (expense) income, net	(843)	14,025	65,466	43,558	34,844	5,593
Income before income tax expenses	1,152,956	944,079	897,596	1,266,992	1,202,274	192,978
Income tax expenses	(39,368)	(85,060)	(89,322)	(352,378)	(124,204)	(19,936)
Share of loss of an equity investee			(648)	(8,218)	(6,117)	(982)
Net income	1,113,588	859,019	807,626	906,396	1,071,953	172,060
Net (loss) income attributable to non controlling interests		295	3,563	(26,429)	(78,234)	(12,557)
Net income attributable to the Company's shareholders	1,113,588	859,314	811,189	879,967	993,719	159,503
Other comprehensive income (loss), net of tax						
Foreign currency translation	(192,424)	(12,769)	(73,194)	(84,728)	2,735	439
Reclassification adjustment		(1,814)				
Unrealized holding gains (losses)	76,969	(30,951)	(14,540)	(15,998)	29,771	4,779
Total other comprehensive income (loss), net of tax	(115,455)	(45,534)	(87,734)	(100,726)	32,506	5,218
Comprehensive income	998,133	813,780	723,455	779,241	1,026,225	164,721
Net earnings per ordinary shares, basic	4.65	3.80	3.57	3.79	4.20	0.67

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Net earnings per ordinary shares, diluted	4.49	3.67	3.47	3.79	4.13	0.66
Net earnings per ADS ⁽¹⁾ , basic	4.65	3.80	3.57	3.79	4.20	0.67
Net earnings per ADS, diluted	4.49	3.67	3.47	3.79	4.13	0.66
Shares used in computation, basic	239,458,633	226,278,227	227,308,854	232,004,879	236,796,818	236,796,818
Shares used in computation, diluted	247,895,076	233,960,556	233,928,400	232,004,879	240,821,127	240,821,127

(1) Each ADS represents one ordinary share

Table of Contents**Selected Consolidated Balance Sheet Data:**

	2008 (RMB)	2009 (RMB)	Year Ended December 31		2012 (RMB)	(US\$)
			2010 (RMB)	2011 (RMB)		
	(in thousands)					
Assets						
Cash and cash equivalents ⁽¹⁾	1,696,273	1,097,155	2,776,936	950,321	1,943,062	311,883
Short-term investments ⁽¹⁾	3,371,828	3,802,050	3,253,362	919,775	739,315	118,668
Total current assets⁽¹⁾	5,236,061	5,102,972	6,304,005	2,179,246	3,096,518	497,025
Property and equipment, net	213,905	178,670	143,286	349,668	340,242	54,613
Investment in equity investees ⁽²⁾			35,126	351,400	377,756	60,634
Available-for-sale securities ⁽³⁾⁽⁴⁾	450,007	450,967	423,303	386,851	78,741	12,639
Total non-current assets	766,363	1,349,690	804,138	1,371,985	1,225,711	196,740
Total assets	6,002,424	6,452,662	7,108,143	3,551,231	4,322,229	693,765
Deferred revenue	403,130	321,291	442,795	529,204	486,025	78,012
Total current liabilities	603,608	547,448	700,314	1,014,916	1,026,670	164,792
Total liabilities	629,294	547,869	700,500	1,029,798	1,058,982	169,978
Total Giant Interactive Group Inc.'s equity	5,373,130	5,897,185	6,392,860	2,495,648	3,217,728	516,481
Non controlling interest		7,608	14,783	25,785	45,519	7,306
Total liabilities and equity	6,002,424	6,452,662	7,108,143	3,551,231	4,322,229	693,765

- (1) In the third quarter of 2011, we declared and paid out a special dividend of US\$3.00 per share to our ADS and ordinary share shareholders, out of which the payout was financed partially through the declaration and payout of dividends to the Company by one of its PRC subsidiaries. As such, the dividends were subject to a 10% withholding tax and, therefore, we accrued a one-time withholding income tax in the amount of RMB259.4 million associated with the repatriation of cash for the special dividend paid during the third quarter 2011.
- (2) In September 2011, we invested US\$50.0 million in the Yunfeng e-Commerce Funds for the purpose of purchasing shares of the Alibaba Group, a leading Chinese e-commerce company.
- (3) During the fourth quarter of 2012, we recorded an impairment charge of RMB240.7 million (US\$38.6 million), which relates to our 2008 investment in Five One Network Development Co. Ltd., or 51.com, as the decline in the fair value of this investment was determined to be other-than-temporary. 51.com was formerly a China-based social networking company which transitioned into an online game developer and operator in recent years. This investment loss resulted from 51.com's lower than expected core business revenue and operating cash flow, and delay in its research and development activities and planned promotion campaigns of its newly launched games.
- (4) In May 2012, the Company recharacterized its RMB27.3 million (US\$4.4 million) investment in Mobile Embedded Technology Inc. from available-for-sale securities to a cost-method investment.

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 RMB6.2301 to US\$1.00, the noon buying rate in effect as of December 31, 2012. 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 April 12, 2013, the noon buying rate was RMB6.1914 to US\$1.00.

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

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Period	Period End	Noon Buying Rate		
		Average ⁽¹⁾	High	Low
		(RMB per US\$1.00)		
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
2011	6.2939	6.4475	6.2939	6.6364
2012				
October 2012	6.2372	6.2627	6.2372	6.2877
November 2012	6.2265	6.2338	6.2221	6.2454
December 2012	6.2301	6.2328	6.2251	6.2502
2013				
January 2013	6.2186	6.2215	6.2134	6.2303
February 2013	6.2213	6.2323	6.2213	6.2438
March 2013	6.2108	6.2154	6.2105	6.2246
April 2013 (through April 12, 2013)	6.1914	6.1991	6.1914	6.2078

(1) Annual averages are calculated by using the average of the exchange rates on the end of each month during the year. Monthly averages are calculated by using the average of the daily rates during the relevant month.

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**

The ZT Online franchise of massively multiplayer online role playing games, or MMORPGs, have historically accounted for substantially all of our net revenues. Any decrease in the popularity of these games would materially and adversely affect our results of operations.

The ZT Online franchise, which consists of the ZT Online 1 Series and ZT Online 2, have historically accounted for substantially all of our net revenues. In 2006 we commercially launched ZT Online, which together with ZT Online Classic Edition, and ZT Online Green Edition, constitutes the ZT Online 1 Series. In 2011 we commercially launched ZT Online 2, which is part of the ZT Online franchise but differs from the ZT Online 1 Series games in a number of ways, including its story, gameplay, graphics, maps, quests, and characters. The most significant change in ZT Online 2 is its in-game economy. ZT Online 2's next generation in-game economy, the transaction-based revenue model which allows players to purchase in-game items from other players that have earned such items by leveling up their in-game characters and accomplishing in-game objectives, is designed to target lower spending and non-spending users as compared to that of ZT Online 1 Series, in which revenue is generated from the players' consumption of game points to purchase items sold by the in-game store. Although we currently operate thirteen games, nine of which are not part of the ZT Online franchise, we expect that we will continue to derive substantially all of our net revenues from the ZT Online franchise in the near term. Our business prospects, financial condition and results of operations would therefore be materially and adversely affected by any factor that contributes to a decline in revenue from the ZT Online franchise, including:

any reduction in purchases of virtual items or services by players of the ZT Online franchise games;

any decrease in the popularity of the ZT Online 1 Series or ZT Online 2 due to competition or otherwise;

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failure to improve, update or enhance the ZT Online franchise games in a timely or effective manner; or

any lasting or prolonged server interruption due to network failures or other factors.

As with other online games, the ZT Online franchise games have finite commercial lifespans. Although our ongoing release of new version of the ZT Online franchise games helps to extend the commercial life of the games, to ensure the continued popularity of the ZT Online 1 Series and ZT Online 2, we will need to expend considerable resources to improve and update the games on a timely basis with new content and features that appeal to our players. Any decline in the popularity of the ZT Online franchise games, whether as a result of the failure to provide timely and popular updates or otherwise, would materially and adversely affect our business prospects, financial condition and results of operation.

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If we are unable to successfully develop and license new popular online games, our business and revenues may be adversely affected.

In order to maintain our long-term profitability and financial and operational success, we must continually develop or license new online games that are attractive to our players. While many new online game products are regularly introduced to the market, only a small number of hit titles account for a significant portion of total revenue in our industry. As the online game market is limited in size, if our newly developed games are not widely accepted by the players, or if successful hit products are launched by our competitors, our market share may be adversely affected and revenues generated by our products may fall below our expectations. For example, we plan to commence closed beta testing of World of Xianxia in the second quarter of 2013, which is expected to be one of our revenue drivers in 2013. If the market acceptance of the game falls below our expectation, our business and revenue may be adversely affected.

The success of our internally developed games will largely depend on our ability to anticipate and effectively respond to changing tastes and preferences of our players and to 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, identifying new third party developed online games with strong market potential, and obtaining license to those online games on commercially reasonable terms, requires a significant degree of effort. If we are not able to successfully develop or license new hit online games that attract large numbers of players and result in substantial online game revenues, our business, financial condition and results of operations may be materially and adversely affected.

We are substantially dependent upon the MMORPG segment of China's online game industry. Any decline in the size of the MMORPG market segment, due to competition from other video game products, other entertainment products or otherwise, would adversely affect our revenues.

The MMORPG segment of China's online game industry, from which we derive substantially all of our revenues, is both rapidly evolving and subject to competition from other forms of video games and other entertainment products. The future prospects for the MMORPG market segment in China will depend on a number of factors beyond our control, including:

the growth of personal computer, internet and broadband users and their penetration in China;

whether the MMORPG segment of China's online game industry continues to grow and the rate of any such growth;

the availability and popularity of other forms of video game products, such as social networking games offered on Tencent's Qzone platform, mobile games offered on Apple's iOS platform, and console games playable on game consoles made by Sony, Nintendo and Microsoft;

the availability and popularity of other forms of online and offline entertainment, such as movies, television programs and other video content;

changes in consumer demographics and consumer tastes and preferences; and

general economic conditions, particularly economic conditions adversely affecting discretionary consumer spending.

Although MMORPGs are currently popular in China, there is no assurance that they will continue to be popular in China or elsewhere. A decline in the popularity of online games in general, or the MMORPG market segment in particular, will materially and adversely affect our business prospects, financial condition and results of operations.

The reorganization of our game development studios could materially and adversely affect our results of operations as a portion of the profits from games developed or operated by these studios will be shared with the non-controlling shareholders of these studios.

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In 2008, we introduced Win@Giant, an incubation program designed to, among other things, identify, recruit and incentivize talented individuals in the areas of game design and development. In 2009, in connection with our Win@Giant initiative, we began to reorganize our game development studios by establishing various subsidiaries that are 51% owned by us and 49% owned by the relevant development team members, which we believe provides greater incentive to the game development teams to make their games commercially successful. This studio reorganization is ongoing, and our current intention is that eventually all of our self-developed games, except for the three games in the ZT Online 1 Series, will be supported by studios that include key members of our development team as non-controlling shareholders. For additional information regarding this reorganization, see Item 4. Information on the Company Business Overview Game Development and Sourcing Game Development.

As a result of our game development studio reorganization, a portion of the net income generated by games developed or supported by these game development studios will be attributable to the non-controlling shareholders of the studios. The Company consolidates its financial results with those of the reorganized studios, and then presents the net income or loss attributable to the non-controlling shareholders as a separate non-controlling interest line item under the heading net income or loss attributable to non-controlling interests . The Company s consolidated income attributable to its shareholders is arrived at after deducting this non-controlling interest. Total non-controlling interest related to our reorganized studios increased 196.2% from RMB26.4 million in 2011 to RMB78.2 million (US\$12.6 million) in 2012, primarily due to an increase in revenue generated by games developed and supported by reorganized studios. If our games developed and/or supported by these studios become more popular and profitable in the future, this non-controlling interest amount will increase, which may result in a lower net income attributable to Company s shareholders and may materially and adversely affect our results of operations.

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We face significant competition, which could reduce our market share and adversely affect our business and net revenues.

The online game market in China is highly competitive. In recent years, numerous competitors have entered the online game market in China, and we expect more companies to enter the market and a wider range of online games to be introduced to the market. Our principal competitors include China-based online game companies such as Tencent Holdings, Ltd., Changyou.com Limited, Perfect World Co., Ltd., Shanda Games Limited and NetEase.com. In addition, we expect international game developers to continue to license more of their games for operation in China.

Many of our competitors have longer operating histories, greater brand name recognition, larger player bases and significantly greater game development, technical, financial and marketing resources than we have. Furthermore, any of our competitors may be acquired by, receive investments from or enter into other cooperative relationships with larger, more 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 international competitors may establish cooperative relationships with our local competitors, which may significantly enhance their competitiveness in the online game market 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 market 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.

Our games are currently accessed primarily through personal computers. As devices other than personal computers are increasingly used to access the internet, successful development of games for such devices will be imperative if we are to maintain or increase our revenues, and our inability to do so may result in lower growth of or a decline in revenues.

Devices other than personal computers, such as mobile phones and tablets, are used increasingly in China and in overseas markets to access the internet. We believe that, for our business to be successful, we will need to develop versions of our existing games, our pipeline games and any future games that work well with such devices. The games that we develop for such devices may not function as smoothly as our existing games, and may not be attractive to game players in other ways. In addition, manufacturers of such devices may establish restrictive conditions for developers of applications to be used on such devices, and as a result our games may not work well, or at all, on such devices. As new devices are released or updated, we may encounter problems in developing versions of our games for use on such devices and we may need to devote significant resources to the creation, support, and maintenance of games for such devices. If we are unable to successfully expand the types of devices on which our existing and future games are available, or if the versions of our games that we create for such devices do not function well or are not attractive to game players, our revenues may fail to grow and may decline.

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

We have experienced significant fluctuations in our operating results from period to period due to a variety of factors, many of which are beyond our control. Significant fluctuations in our operating results could be caused by any of the following factors, among others:

our ability to retain existing users of our games and attract new users;

the introduction of new games or expansion packs by us or our competitors;

changes in our game features and the corresponding impact on player behavior and purchasing patterns;

the adoption of new, or changes in existing government regulations;

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 for our self-developed games, and license costs and royalty payments for licensed games;

the amount of overseas licensing net revenues generated through our licensing arrangements with operators 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 success of our advertising and promotional efforts;

seasonality effect during holidays in the first quarter and fourth quarter, when fewer of our targeted players play our games; and

economic conditions in general and specifically with respect to the online game industry in China.

For example, our net revenues declined 18% in 2009, which we believe was primarily due to new regulations promulgated by the PRC government in connection with certain game features, and corresponding changes to our in-game monetization features. However, our net revenues increased 2.2%, 34.5% and 20.0%, in 2010, 2011 and 2012, respectively.

As a result, our operating results may vary from period to period, be difficult to predict for any given period, be adversely affected from period to period, and not be indicative of our future performance. In the event that our operating results do not meet our expectations or those of the public market analysts and investors, the price of our ADSs may decline.

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

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We are pursuing a number of growth strategies, including broadening our user base by diversifying our game portfolio, expanding our distribution channels by leveraging our strong relationships with internet platform partners, acquiring additional licenses to operate third party developed overseas games in China, pursuing additional licensing opportunities for operating our games overseas, and expanding into non-MMORPG market segments by developing web games, and games for operation on mobile and tablet devices.

For example, in order to expand our user base, in September 2012 we released the micro-client version of ZT Online 2 on Qihoo 360's platform. In 2012, we also licensed several of our new games to overseas partners for operations outside of China, including Genesis of the Empire, which was licensed for operation in South Korea and Vietnam, and Marine Tycoon, The Sky and World of Xianxia, which were licensed for operation in Taiwan, Hong Kong and Macau, and World of Xianxia, which was also licensed for operation in Malaysia, Singapore, Indonesia and Thailand. In addition, we have established an internal development team focusing on producing webgames, which are online games that do not require installation of client-side server software, thereby reducing the time required for players to begin playing the games. We are also exploring development of games to be operated on mobile and tablet devices.

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 remained relatively stable in 2010. In 2011, our net revenues increased to RMB1,792 million, representing a 34.5% increase, and in 2012, our net revenues increased to RMB2,152 million (US\$345.5 million), representing a 20.1% increase. 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.

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Our business may be materially harmed if our games are not featured in a sufficient number of internet cafés in China.

A substantial number of players access our game through internet cafés. Due to limited storage space on their computer hard drives for client side game software, internet cafés generally only feature a select 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.

We have taken steps to ensure that our games are featured in a sufficient number of internet cafés, such as by 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. However, the recent decrease in our reliance on distributors, due to a decrease in the proportion of our sales proceeds that are generated through the distribution of physical prepaid game cards, could reduce our sales presence in internet cafés and reduce the number of internet cafés in which our games are featured.

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 personal computers 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 personal computers in China has increased in recent years, the penetration rate for personal computers 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 personal computers 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. The limited use of personal computers 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, or failure of our distributors to comply with the terms of our distribution agreements, 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 used by customers in China as in the United States. Although online purchase of game points through our official game website has become more popular in recent years, our business is still dependent on the performance of our regional distributors, who are composed of independent third parties. In 2012, 55.4% of our sales proceeds were generated through sales of prepaid game cards to our distributors, compared to 75.2% in 2011. Our largest distributor accounted for 3.3% of our sales proceeds in 2012. Maintaining relationships 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. 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 and adversely disrupt our business and harm our net revenues.

In addition, our distributors and internet cafés and other outlets in which they sell our prepaid game cards may violate our distribution agreements. Examples of violations include:

failure to meet minimum sales targets or penetration targets, or failure to maintain minimum price levels for our prepaid game cards;

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.

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Some of our distributors have committed these types of violations in the past, which resulted in us terminating their existing distribution agreements. 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. We may also be liable in China for legal or regulatory violations by any of our distributors.

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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 2012, 44.6% of our sales proceeds were generated by players purchasing our game points directly through our official game website, and the remaining 55.4% from purchasing physical or virtual game cards through our distributors. The direct game point purchasing through our official game website is processed by a variety of third-party online payment service providers, including Alipay.com Co., Ltd, Shanghai China UnionPay E-Payment Service Co., Ltd, 99Bill Corporation, China Payment and Remittance Service Co., Ltd. and several major commercial banks. In such transactions, secure transmission of our players' confidential billing information 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 can 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, current security measures may be inadequate. 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 systems we use.

In addition, we do not have control over the security measures of our third-party online payment service providers, and those security measures may not be adequate at present or may not be adequate with the expected increased usage of online payment systems. For example, hackers have in the past used viruses to corrupt the computers of online shoppers using Taobao, a leading e-commerce website in China that allows shoppers to purchase goods from different vendors online. In addition, through a process known as phishing, hackers have created fake webpages on Taobao that appear to be selling legitimate goods online. In both situations, when an unsuspecting online shopper attempts to submit a purchase order and payment to a third party vendor on Taobao, that purchase order and payment is redirected to our website and changed into a legitimate purchase order and payment for our game points on behalf of the hacker and not the unsuspecting online shopper. Accordingly, our systems are then misled into accepting such payment and unintentionally issuing the corresponding game points to the hacker, who then uses these game points to purchase virtual items in our games with the intention of later exchanging the virtual items for cash on offline third party trading platforms. In a few instances, online shoppers on Taobao that were misled by hackers have resorted to litigation against us in order to recover their losses. Although we have not paid any compensation in connection with this litigation, and have implemented stricter security measures and cooperated with local authorities to apprehend the hackers, we could be exposed to further litigation and possible liability if we fail to detect similar fraudulent transactions, 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 and reduce player satisfaction.

Any failure to maintain satisfactory performance, reliability, security and availability of our network infrastructure, including issues arising from the internet infrastructure in China, security breaches caused by hacking and transmission of computer viruses, and natural disasters such as floods and earthquakes, may cause significant harm to our reputation and our ability to retain existing and attract new game players. In addition, all of the game servers operating our games, and all 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. Any network interruption or inadequacy that causes interruptions in the availability of our games or deterioration in the quality of access to our games could reduce our game players' satisfaction and ultimately harm our business, financial condition and results of operations. In addition, any security breach caused by hacking, 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 systems and we do not have business interruption insurance.

Changes in our lifespan estimates for the virtual items sold within our games may have a negative impact on our net revenue and results of operations.

We generally recognize revenues from virtual items sold to players of our free-to-play online games over the estimated lifespan of the relevant virtual items as determined by historical player usage patterns and playing behavior. We are committed to continually monitoring each of our games' actual operational statistics and usage patterns, comparing these actual statistics with our original estimates and refining our estimates and assumptions when they are materially differ from the actual statistics. Any adjustment in the estimated lifespan of these virtual items may cause our revenues to be recognized over a significantly different time period, which may have a negative impact on our net revenue and results of

operations.

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Undetected programming errors or defects in our games and the proliferation of cheating programs could adversely affect our business reputation and result in a decline in our active paying accounts.

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 users to acquire superior features for their game characters for which they would otherwise be required to pay or otherwise earn through game play. In addition, 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 reputation and result in a decline in our active paying accounts. This could materially and adversely affect our business, financial condition and results of operations.

We depend on our key personnel, and our business and growth prospects may be severely disrupted if we lose their services or are unable to attract new key employees.

Our future success is heavily dependent upon the continued service of our key executive officers and other key employees. In particular, we rely on the expertise, experience and leadership of Mr. Yuzhu Shi, our founder, chairman and chief executive officer, and Ms. Wei Liu, our president, in connection with our business operations and game development. We also rely on their personal relationships with our employees, the relevant regulatory authorities, and our distributors. In addition, we are dependent on a number of key technology officers and staff for the development and operation of our online games. Furthermore, we need to continue to attract and retain skilled and experienced online game development personnel to maintain our competitiveness.

If one or more of our key personnel are unable or unwilling to continue in their present positions, we may not be able to replace them easily or at all and may incur additional expenses to recruit and train new personnel. These difficulties may disrupt our business, and our financial condition and results of operations could be materially and adversely affected. We do not maintain key-person life insurance for any of our key personnel. In addition, if any of our executive officers or key employees joins a competitor or forms a competing company, we may lose know-how, trade secrets, suppliers and key professionals and staff. All of our employees, including each of our executive officers and key employees, have entered into an employment agreement with us, which contains customary non-compete provisions. Although non-compete provisions are generally enforceable under PRC laws, PRC legal practice regarding the enforceability of such provisions may not be as well-developed, and therefore we cannot assure you that a PRC court would enforce such provisions. Furthermore, since the demand and competition for talent is intense in our industry, particularly for online game development personnel and related technical personnel, we may need to offer higher compensation and other benefits in order to attract and retain key personnel in the future, which could increase our compensation expenses.

In the fourth quarter of 2008, we introduced Win@Giant, an incubation program designed to attract and retain talented employees, developers and business partners. Under Win@Giant, we have reorganized several of our game development studios by establishing various subsidiaries that are generally 51% owned by us and 49% owned by the relevant key development team members, with an aim to facilitate our development of new online games. Each reorganized studio only focuses on producing and supporting internally developed games, which we believe gives them greater incentive to make their games commercially successful. While this program is intended to supplement and not to 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 qualified game developers or other key personnel that we will need to achieve our business objectives.

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

We intend to continue expanding our business through selective acquisitions in the future. We do not, however, have significant experience in completing acquisitions or integrating new companies into our existing operations. In the event that we pursue acquisition opportunities in the future, we will face a number of risks that could materially and adversely affect our business and results of operations, including overpaying for the acquisitions, an inability to realize the synergies contemplated at the time of executing the transactions, difficulties in integrating the acquired companies, the diversion of management resources from other strategic and operational issues, the inability to retain the key employees of the acquired companies, and unknown or unforeseen assumed liabilities. For example, in 2008 we acquired a 25% equity interest in 51.com, formerly a China-based social networking company which transitioned into an online game developer and operator in recent years, for a consideration of US\$50.8 million. During the fourth quarter of 2012, we recorded an impairment charge of RMB240.7 million (US\$38.6 million) with respect to this investment due to lower than expected core business revenue and operating cash flow, and delays in research and development activities and planned promotion campaigns for newly launched games.

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

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

We have historically relied on a combination of trademark and copyright law, trade secret protection, internal security measures and restrictions on disclosure to protect our intellectual property rights. Although we enter into confidentiality and invention assignment agreements with most of our employees, 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.

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As of December 31, 2012, we own a total of 545 registered trademarks in China and overseas and are in the process of applying for the registration of 231 trademarks in China and 39 trademarks overseas. We cannot assure you that any of these trademark applications will ultimately be successful or will provide adequate protection for our business. Some of our pending applications or registrations may also be successfully challenged or invalidated by others. If our trademark applications or registrations are not successful, we may have to use different marks or otherwise enter into arrangements with third parties.

In addition, China's online game market often faces challenges from pirate servers, which are game servers operating unauthorized copies of online games that enable players to play those games without purchasing prepaid game cards or game points from the authorized operators. We mitigate the risk of pirate servers by maintaining stringent security controls over our server side software at our offices and insisting upon high security standards at the various internet data centers where our servers are housed. In addition, once pirate servers are identified, we work with local government authorities to shut the servers down. If pirate game servers continue to operate any of our games, our business, financial condition and results of operations may be materially and adversely affected.

Implementation of intellectual property laws in China has historically been lacking, primarily because of difficulties in enforcement. Accordingly, intellectual property right protection in China may not be as effective as in the United States or other developed 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 therefore we cannot assure you that our technologies, processes or methods do not infringe upon 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 purchase 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 and property insurance for our offices and fixed assets, we do not carry any other 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.

If we fail to maintain an effective system of internal control over financial reporting, our investors may lose confidence in our financial statements.

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. Our management has concluded that our internal control over financial reporting is effective as of December 31, 2012, and our independent registered public accounting firm concurred with our management's conclusion. However, if we fail to maintain effective internal control over financial reporting in the future, our management and our independent public accounting firm may not be able to conclude that our internal control over financial reporting is effective. This in turn 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. Furthermore, we have incurred and anticipated that we will continue to incur considerable costs, management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act.

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As an online game company, our experience with investment activities is limited.

We explore selected investment opportunities that may have strategic value to us or that are purely financial in nature, with the primary objective of providing us with a more favorable rate of return than that customary of ordinary bank deposits.

For example, as of December 31, 2010, 2011 and 2012, we held short-term and long-term held-to-maturity investments in the amount of RMB1,850.0 million, RMB700.0 million and RMB790.0 million (US\$126.8 million), respectively. In May 2011, we invested RMB100.0 million in a trust arrangement with China Resources SZITIC Trust Co., Ltd., which in turn invested in certain real estate development projects in the PRC cities of Ningbo and Chengdu for a period of five years. In 2012, we invested RMB600.0 million (US\$96.3 million) in two trust arrangements with Huaneng Guicheng Trust Co., Ltd., both of these trust investments are associated with certain real estate development projects and have a term of one year. Although our short-term and long-term held-to-maturity investment contracts are secured or wholly guaranteed by a reputable financial institution, a credit-worthy company, or by the properties of the underlying investment projects, any default by the trust companies or the borrowers under these trust arrangements, or any deterioration in the financial condition of the secured collateral or these financial institution or project companies could cause significant loss to us and have a material adverse effect on our financial condition and results of operations.

In addition, we have made certain equity investments. In April 2011, we committed to invest RMB30.0 million in Beijing Innovation Work Investment Center (LP), or Innovation Work, an early-stage China-based internet and technology company investment fund, which is led by Mr. Kai-Fu Lee, a well-known business leader in the internet space in China, of which RMB18.0 million had been invested by December 31, 2012. In September 2011, we invested RMB317,050,000 in the Yunfeng e-Commerce Funds, or the Yunfeng Fund, for the purpose of purchasing ordinary shares of the Alibaba Group Holding Limited, or the Alibaba Group, China's leading e-commerce company. Finally, in March 2013, we purchased a convertible bond of China Minsheng Banking Corp., Ltd. for RMB35.2 million, which may be converted into the bank's A-shares that are traded on the Shanghai Stock Exchange. For additional information regarding our equity investments, see Item 5. Operating and Financial Review and Prospects—Liquidity and Capital Resources—Investing Activities.

These equity investments are made in contemplation that the underlying businesses obtain and/or sustain continued business growth, eventually go public or be acquired, which there are no guarantees of occurring, if at all. In addition, some of these equity investments may only provide limited exits to us and therefore our investments may be illiquid until their respective maturity, or potentially until a liquidity event occurs with respect to the underlying companies that we hold interest in.

Although these equity investments may offer us potentially higher returns, these returns are not guaranteed and 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 operations may be materially and adversely affected.

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.

We have licensed eight of our self-developed games for operation in various foreign countries, regions and territories of Asia, Europe and North America by a variety of different operating partners. In 2012, our revenues from licensing our games to overseas third party operators was approximate RMB18.0 million (US\$2.9 million), accounting for approximately 0.8% of our total net revenues. Licensing our games for operation in overseas markets exposes us to a number of risks, including difficulties in:

identifying and maintaining good relations with game operators who are knowledgeable, and can effectively distribute and operate our games, in overseas markets;

negotiating licensing agreements with game operators on terms that are commercially acceptable to us and enforcing the provisions of those agreements;

developing games, updates and expansion packs catering to overseas markets and renewing our license agreements with game operators upon expiration;

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maintaining the reputation of our company and our games, given that our games are operated by game operators in the international markets with different standards;

protecting our intellectual property rights overseas and managing the related costs;

receiving and auditing the royalties we are entitled to receive;

complying with the different commercial and legal requirements of the international markets in which our games are offered, such as game import regulatory procedures, taxes and other restrictions and expenses; and

managing our foreign currency risks.

For example, in November 2012, a newly updated version of ZT Online 2 that we licensed for operation in Vietnam included a map that indicated certain islands in the South China Sea that are claimed by both Vietnam and China belong to China. After receiving considerable pressure from the Vietnamese government and media, our local operator in Vietnam stopped operating both ZT Online and ZT Online 2. Following the operation shutdown, we terminated both game license agreements.

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If we are unable to manage these risks effectively, our ability to license our games overseas may be impaired, which may materially and adversely affect our business, financial conditions and results of operations would be materially and adversely affected.

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 may lose control of Giant Network, resulting in its deconsolidation, and could be subject to severe penalties, including ceasing our operations.

Various regulations in China currently restrict or prevent foreign and foreign-invested entities from engaging in value-added telecommunication services, which are defined by PRC authorities to include operating online games and providing online advertisements. Since we are a Cayman Islands exempted company and therefore are a foreign or foreign-invested enterprise under PRC law, neither we nor our PRC subsidiaries are eligible to hold the licenses required to operate online games in China. To comply with PRC laws and regulations, we operate our online games in China through Giant Network, which is beneficially owned by certain of our officers and directors and other individuals. Through a series of contractual arrangements, Zhengtu Information is able to effect control and management of Giant Network. Giant Network, which conducts business as an internet content provider, or ICP, holds a value-added telecommunications business operating license, or ICP license, issued by the Shanghai Communications Administration, a local office of the Ministry of Industry and Information Technology of the PRC, or the MIIT, which allows Giant Network to provide internet content distribution services in Shanghai. In addition, Giant Network also holds an internet culture operation license issued by the Ministry of Culture, or MOC, and an internet publishing license issued by the General Administration of Press and Publication, or GAPP, in order to operate and distribute games through the internet. These licenses are essential to the operation of our business.

Despite the lack of technical majority ownership, there exists a parent-subsidiary relationship between our Cayman Islands Company and Giant Network through the irrevocable proxy granted by Giant Network to Zhengtu Information, a wholly owned subsidiary of our Cayman Islands Company, whereby equity holders of Giant Network effectively assigned all of their voting rights underlying their equity interest to Zhengtu Information. We have entered into contractual arrangements with Giant Network pursuant to which Zhengtu Information, our wholly owned subsidiary, provides technical support and exclusive software licenses 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 Item 4. Information on the Company Organizational Structure and Item 7. 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 MIIT publicly released the Notice on Strengthening the Administration of Foreign Investment in Operating Value-added Telecommunications Business, dated July 13, 2006, or the MIIT 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 foreign investors in any form, or providing any resources, sites or facilities to foreign investors that intend to conduct value-added telecommunication business illegally in China. There is currently no official interpretation or implementation practice under the MIIT Notice. Due to a lack of interpretative materials from the authorities, it is uncertain whether the MIIT would consider our corporate structure and the contractual arrangements as a kind of foreign investment in telecommunication services. Therefore, it is unclear what impact the MIIT Notice might have on us or the other PRC internet companies that have adopted the same or similar corporate structures and contractual arrangements as ours.

In addition, on September 28, 2009, GAPP, together with the National Copyright Administration, and the National Office of Combating Pornography and Illegal Publications jointly issued a Notice on Further Strengthening on the Administration of Pre-examination and Approval of Online Games and the Examination and Approval of Imported Online Game (Xin Chu Lian [2009] No. 13), or the GAPP Notice. The GAPP Notice restates that foreign investors are not permitted to invest in online game-operating businesses in China via wholly owned, equity joint venture or cooperative joint venture investments and expressly prohibits foreign investors from gaining control over or participating in domestic online game operators through indirect ways such as establishing other joint venture companies, or contractual or technical arrangements. However, the GAPP Notice does not provide any interpretation of the term foreign investors or makes a distinction between foreign online game companies and companies with a corporate structure that is similar to our own, including the many internet and other companies from China with shares listed on overseas stock exchanges. Thus, it is unclear whether GAPP will deem our corporate structure and operations to be in violation of these provisions.

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Furthermore, as certain other government authorities such as the Ministry of Commerce, or MOFCOM, the MOC, and the MIIT did not join GAPP in issuing the GAPP Notice, the views of these authorities are uncertain in clarifying the scope of implementation and enforcement of the GAPP Notice.

Although we are not aware of any case in which online game companies in China using contractual arrangements similar to the above arrangements have been penalized or ordered to terminate operations by PRC authorities because of these contractual arrangements, we cannot be sure that the PRC government would view our contractual arrangements to be in compliance with PRC licensing, registration or other regulatory requirements, including without limitation, the requirements described in the MIIT Notice and the GAPP Notice, existing policies, or with requirements or policies that may be adopted in the future. If any of our businesses are determined not to be in compliance with the MIIT Notice or the GAPP Notice, the PRC government could take a number of regulatory or enforcement actions that could be harmful to our business, including but not limited to: levying fines, confiscating our income, revoking our business and operating licenses, discontinuing or restricting our operations, blocking our website, requiring us to restructure our business, restricting our right to collect revenue or imposing additional conditions or requirements with which we cannot comply. We may also encounter difficulties in obtaining performance or enforcement of related contracts, thereby losing our control of Giant Network, resulting in its deconsolidation. Any of these actions could cause our business, financial condition and results of operations to suffer and subsequently the market price of our ADSs to decline. In addition, if our ownership structure was required to change, our ability to consolidate the financial results of Giant Network and its consolidated entities could be adversely affected.

The contractual arrangements with Giant Network 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.

We rely on contractual arrangements with Giant Network and its shareholders to operate our business. For a description of these contractual arrangements, see Item 4. Information on the Company Organizational Structure and Item 7. Major Shareholders and Related Party Transactions Related Party Transactions. These contractual arrangements may not be as effective as direct ownership in providing us with operational 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 directors of Giant Network, which in turn could effect changes, subject to any applicable fiduciary obligations, in the management team, and (ii) derive economic benefits from the operations of Giant Network by causing it to declare and pay dividends. Because we rely on these contractual arrangements to effect control over Giant Network, we are exposed to the risk that the shareholders of Giant Network may fail to perform his or her respective obligations under these contractual arrangements. In addition, the shareholders of Giant Network may potentially have a conflict of interest with us, and they may breach their contracts with us or cause such contracts to be amended in a manner contrary to the interest of our company, if they believe such action furthers their own interest, or if they otherwise act in bad faith. If any of the foregoing were to occur, we may have to incur substantial costs and expend significant resources to enforce these contractual arrangements.

In addition, all of these contractual arrangements are governed by PRC law and provide for the resolution of disputes through arbitration in the PRC. Accordingly, these contracts would be interpreted in accordance with PRC law and any disputes would be resolved in accordance with PRC legal procedures. We would have to rely for enforcement on legal remedies under PRC law, including specific performance, injunctive relief or damages, which may not be effective or possible. The legal environment in the PRC is not as developed as in 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, and our financial condition and results of operations may be negatively affected.

The contractual arrangements entered into among our PRC subsidiaries, Giant Network and its shareholders may be subject to audit or challenge by the PRC tax authorities; a finding that our PRC subsidiaries or Giant Network 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 our PRC subsidiaries Zhengtu Information and Zhengju Information, Giant Network, Giant Network's shareholders and our reorganized game development studios do not represent arm's-length prices and adjust any of their income in the form of a transfer pricing adjustment. In 2011, the high and new technology enterprise status of Zhengtu Information was renewed while that of Giant Network was not renewed, resulting in an income tax rate of 15% percent for Zhengtu Information and 25% for Giant Network. This difference in income tax rate may increase the risk that PRC tax authorities challenge the prices that Giant Network pays for services provided by Zhengtu Information pursuant to their contractual arrangements. A transfer pricing adjustment could result in a reduction of expense deductions recorded by Giant Network, 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, our other PRC subsidiaries or Giant Network for underpayment of taxes. For additional information regarding the preferential tax treatments of our

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various PRC entities, see Item 5. Operating and Financial Review and Prospects Operating Results Income Tax Expense China.

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We may lose the ability to use and enjoy assets held by Giant Network under contractual arrangements that are important to the operation of our business if Giant Network declares bankruptcy or becomes subject to a dissolution or liquidation proceeding.

Under our contractual arrangements, Giant Network holds assets that are critical to our business operations, such as our core intellectual property, licenses and permits, and/or joint operation agreements relating to our games and game operations. Although the Purchase Option and Cooperation Agreement among Zhengtu Information, Giant Network and shareholders of Giant Network contain terms that specifically obligate the shareholders of Giant Network to ensure the valid existence of Giant Network, in the event the shareholders breach this obligation and voluntarily liquidate Giant Network, or if Giant Network declares bankruptcy and all or part of its assets became subject to liens or rights of third-party creditors, we might be unable to continue some or all of our business operations. Furthermore, if Giant Network was to undergo a voluntary or involuntary liquidation proceeding, its shareholders or unrelated third-party creditors might claim rights to some or all of Giant Network's assets and their rights could be senior to our rights under the contractual arrangements, thereby hindering our ability to operate our business.

The discontinuation, reduction or delay of any of the preferential tax treatments or the government financial incentives currently available to us in the PRC could materially and adversely affect our business and results of operations.

Under the PRC Enterprise Income Tax Law effective on January 1, 2008, or the EIT Law, foreign invested companies such as Zhengtu Information, and domestic companies such as Giant Network, are subject to a unified income tax rate of 25%. Various favorable income tax rates are, however, available for qualified enterprises in encouraged sectors of the economy. Companies that qualify as a high and new technology enterprise, or HNTE, a status which is reassessed every three years, are subject to an income tax rate of 15%. In addition, companies that qualify as a software development enterprise are exempt from income tax for two years and subject to an income tax rate of 12.5% for the following three years.

In 2008, the Shanghai government granted Zhengtu Information HNTE status, which was successfully renewed in 2011. In 2011, the Shanghai government recognized three of our PRC subsidiaries as software development enterprises, consisting of Jujia Network and Juhuo Network, two of our 51% owned game development studios and Zhengju Information, which is our wholly owned subsidiary. In addition, Wuxi Network, which is 45% owned by Giant Network, and Beijing Giant Zhengtu, which is 51% owned by Zhengtu Information and 34% owned by Giant Network, were also recognized as software development enterprises in 2011 by Jiangsu Province and Beijing government, respectively.

We cannot assure you, however, that our PRC entities will be able to continue to qualify for preferential tax treatment. If any of our PRC entities that qualified for preferential tax treatments fails to continue to qualify in a subsequent year, our income tax expenses would increase, which may have a material adverse effect on our net income and results of operations. For additional information regarding the preferential tax treatments of our various PRC entities, see Item 5. Operating and Financial Review and Prospects Operating Results Income Tax Expense China.

In addition, in 2010, 2011 and 2012, our PRC entities received financial incentives from the government in an aggregate amount of RMB57.4 million, RMB47.7 million and RMB63.6 million (US\$10.2 million), respectively, which were calculated with reference to taxable revenues and taxable income. To be eligible to apply for the government financial incentives, we are required to meet a number of financial and non-financial criteria and, even if we meet these criteria, the grant of any incentive is still subject to the discretion of the municipal government. Moreover, the central government or municipal government could at any time eliminate or reduce these government financial incentives. Since the government has discretion in the timing of payment and the amount of the financial incentive, we cannot assure you that we will be able to continue to enjoy these government financial incentives or receive such incentives promptly. The discontinuation, reduction or delay of these government financial incentives could have a material adverse effect on our business and results of operations.

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

The 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 PRC controlled enterprises established outside of China as resident enterprises, or Circular 82, clarified that dividends and other income paid by such resident enterprises will be considered to be PRC sourced 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 EIT Law, 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, Circular 82 details that certain PRC controlled enterprises will be classified as resident enterprises if the following are located or resident in China: (i) senior management personnel and departments that are responsible for daily production, operation and

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management; (ii) financial and personnel decision making bodies; (iii) key properties, accounting books, company seal, and minutes of board meetings and shareholders meetings; and (iv) half or more of the directors or senior management having voting rights.

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Although the determining criteria set forth in Circular 82 may reflect the State Administration of Taxation's general position on how the de facto management body test should be applied in determining the tax resident status of offshore enterprises, Circular 82 only applies to offshore enterprises controlled by PRC enterprises or PRC enterprise groups, not those controlled by individuals or foreign enterprises like us. Therefore, we do not currently consider our company or any of our overseas subsidiaries to be a PRC resident enterprise. However, if the PRC tax authorities determine that our Cayman Islands 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 EIT Law and the Implementing Rules dividends paid to our non-PRC holding companies from our PRC subsidiaries would qualify as tax-exempted income, any such dividends paid to our non-PRC holding companies 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. We are actively monitoring the resident enterprise classification rules and our Cayman Islands 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.

The PRC EIT Law will affect tax exemptions on the dividends we receive and we may not be able to obtain certain treaty benefits on such dividends.

We are a holding company incorporated under the laws of the Cayman Islands. We conduct substantially all of our business through our PRC subsidiaries, Giant Network and its consolidated entities, and we derive substantially all of our income from these companies. Prior to January 1, 2008, dividends derived by foreign enterprises from business operations in China were not subject to the PRC withholding tax. However, such tax exemption ceased after January 1, 2008 and a withholding tax of 10% is imposed on all dividends declared and paid after January 1, 2008. In the third quarter of 2011, we declared and paid out a special dividend of US\$3.00 per share to our ADS and ordinary share shareholders, out of which the payout was financed partially through the declaration and payout of dividends to the Company by one of its PRC subsidiaries. As such, the dividends were subject to a 10% withholding tax and therefore, we accrued a one-time withholding income tax in the amount of RMB259.4 million associated with the repatriation of cash for the special dividend paid during the third quarter 2011.

According to the Notice of the State Administration of Taxation on Summary Table of Treaty Rates for Dividends, or Circular 112, which was issued on January 29, 2008 and the Arrangement between the PRC and the Hong Kong Special Administrative Region on the Avoidance of Double Taxation and Prevention of Tax Evasion, or the Double Taxation Arrangement (Hong Kong), which became effective on December 8, 2006, dividends from our PRC subsidiaries paid to us through our Hong Kong subsidiary may be subject to a withholding tax at a reduced rate of 5% if such Hong Kong entity owns at least 25% of the equity interest of the PRC company. The ultimate withholding tax rate will be determined by treaty between the PRC and the tax residence of the holder of the PRC subsidiaries. The State Administration of Taxation promulgated a tax notice on October 27, 2009, or Circular 601, which provides that tax treaty benefits will be denied to conduit or shell companies without business substance and a beneficial ownership analysis will be used based on a substance-over-the-form principle to determine whether or not to grant treaty benefits. It is unclear at this early stage whether Circular 601 applies to dividends from our PRC subsidiaries paid to us through our Hong Kong subsidiary. However, the issuance of Circular 601 shows that there can be no assurance that the Double Taxation Arrangement between China and Hong Kong could be successfully applied as noted above. If our Hong Kong subsidiary cannot be regarded as the beneficial owner of such dividends, it will not be entitled to the treaty benefits under the Double Taxation Arrangement (Hong Kong) and thus the dividends will be subject to normal withholding tax of 10% as provided by the PRC EIT Law.

The recently adopted PRC tax reform pilot program, which was initiated in Shanghai and may be extended to other cities in the future, requires us to pay value added tax instead of business tax in Shanghai and it could result in unfavorable tax consequences to us.

The PRC government recently adopted a PRC tax reform pilot program, which was initiated in Shanghai and may be extended to other cities in the future. On November 16, 2011, the Ministry of Finance and the State Administration of Taxation jointly issued the Circular on the Pilot Program for the Collection of Value Added Tax Instead of Business Tax, or Circular 110, and the Circular on the Pilot Program for the Collection of Value Added Tax Instead of Business Tax in Transportation and Certain Modern Service Sectors in Shanghai, or Circular 111, to provide specific implementation rules for the pilot program, which became effective January 1, 2012. Pursuant to Circular 110 and Circular 111, starting from January 1, 2012, companies that are classified by Shanghai's local tax authorities as operating business in transportation or certain modern service sectors in Shanghai are required to pay a Value Added Tax, or VAT, instead of the business tax. Specifically, a 17% rate applies to the movable property leasing services, an 11% rate applies to the transportation services and a 6% rate applies to certain other modern services, such as research and development, technological services, culture, logistics and consultation. This tax reform pilot program is new and its interpretation and enforcement involve significant uncertainties. In the event that our other PRC subsidiaries located in Shanghai engage in business falling within the category of certain modern service sectors, or if we are unable to obtain sufficient amount of qualified VAT invoices from our suppliers to offset the net revenue subject to such VAT, our PRC subsidiaries, which pay business tax at a 5% tax rate for such part of their business before the tax reform pilot program takes effect, may face unfavorable tax consequences, which may adversely affect our business, financial condition and results of operations.

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PRC laws and regulations establish complex procedures for some acquisitions of PRC 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 and amended in 2009, 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, or the National Security Review Mechanism Circular, establish procedures and requirements that could make some acquisitions of PRC 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.

In addition, the Rules of Ministry of Commerce on Implementation of Security Review Mechanism of Mergers and Acquisitions of Domestic Enterprises by Foreign Investors promulgated by the MOFCOM in August 2011, or the MOFCOM Security Review Rules, effective September 1, 2011, which implements the National Security Review Mechanism Circular, provides that, a security review by MOFCOM is required for mergers and acquisitions of PRC domestic enterprises by foreign investors (i) having national defense and security concerns, and (ii) where the foreign investors may acquire the de facto control of the PRC domestic enterprises having national security concerns such as key farm products, key energy and resources, and key infrastructure, transportation, technology and major equipment manufacturing industries. Neither the National Security Review Mechanism Circular nor the MOFCOM Security Review Rules, however, defines the term of "key or major," nor has it exhausted all the industries that may be deemed as sensitive industries subject to the security review. When deciding whether a specific merger or acquisition of a domestic enterprise by foreign investors is subject to MOFCOM's security review, the principle of substance over form should be applied and foreign investors are prohibited from bypassing the security review requirement by way of structuring transactions through proxies, trusts, indirect investments, leases, loans, control through contractual arrangements or offshore transactions. 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 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.

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.

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Starting in 2001, the PRC 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 MIIT, 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 and enhancing the punishment for internet cafés admitting minors. This suspension may continue indefinitely. Furthermore, the PRC 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. Governmental authorities may from time to time impose stricter requirements, such as limits on the ages of customers and hours of operation, as a result of the occurrence or perception of, or media attention on, gang fights, fires and other incidents occurring at or related to internet cafés.

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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 to maintain all applicable permits and approvals, our business and operations would be materially and adversely affected.

In China, the internet industry, including the operation of online games, is highly regulated by the PRC government. Various regulatory authorities of the central PRC government, such as the State Council, the MIIT, the State Administration for Industry and Commerce, or the SAIC, the MOC, GAPP, the State Administration of Radio, Film and Television, and the Ministry of Public Security, are empowered to promulgate and implement regulations governing various aspects of the internet and the online game industry.

We are required to obtain applicable permits or approvals from different regulatory authorities in order to provide online game services. For example, an internet content provider, or ICP, must obtain a value-added telecommunications business operation license, or ICP license, from the MIIT or its local offices in order to engage in any commercial ICP operations

\$

233

\$

54

\$

1,343

\$

158

Income from and gain (loss) on sale of discontinued operations, net

(6

)

50

1,815

144

Net Income

\$

227

\$

104

\$

3,158

\$

302

Denominators:

Basic weighted-average shares

412

494

438

492

Potentially dilutive common stock equivalents stock options and other employee stock plans

10

5

11

5

Diluted weighted-average shares

422

499

449

497

The dilutive effect of outstanding options and restricted stock is reflected in diluted net income per share by application of the treasury stock method, which includes consideration of unamortized share-based compensation required by SFAS No. 123 (R).

The following table presents options to purchase shares of common stock, which were not included in the computation of diluted net income per share because they were anti-dilutive.

	Three Months Ended		Nine Months Ended	
	July 31, 2006	2005	July 31, 2006	2005
Options to purchase shares of common stock (in millions)	22	53	8	54
Weighted-average exercise price	\$ 38	\$ 32	\$ 45	\$ 32
Average common stock price	\$ 33	\$ 24	\$ 35	\$ 23

The computation of diluted net income per share for the three and nine months ended July 31, 2005 does not include 36 million shares issuable upon conversion of our then-outstanding \$1.15 billion senior convertible debentures as the effect was not dilutive for that period, using the if-converted method pursuant to SFAS No. 128, Earnings per Share. The senior convertible debentures were redeemed in September 2005.

6. SHARE-BASED COMPENSATION

Effective November 1, 2005, Agilent adopted the provisions of SFAS No. 123 (R) which requires the measurement and recognition of compensation expense for all share-based payment awards made to our employees and directors including employee stock option awards, employee stock purchases made under our Employee Stock Purchase Plan (ESPP) and non-vested performance share awards granted to selected members of our senior management under the LTPP based on estimated fair values. Agilent previously applied the provisions of APB No. 25 and related Interpretations and provided the required pro forma disclosures under SFAS No. 123, Accounting for Stock-Based Compensation, (SFAS No. 123).

Following the Verigy IPO, Verigy granted new share-based payment awards to their employees and directors including employee stock option awards and employee stock purchases made under Verigy's ESPP. Included in Agilent's share-based compensation expense and recorded under the provisions of SFAS No. 123 (R) is compensation expense for the new Verigy awards. Verigy's compensation expense is based on the estimated grant date fair value method required under SFAS No. 123 (R) using a straight-line amortization method.

The following tables disclose Agilent awards excluding new Verigy awards and new Verigy awards separately with the exception of the share-based compensation expense disclosures.

As a result of the Verigy IPO and upon final distribution of Verigy shares by Agilent, non-vested Agilent stock options held by Verigy employees will forfeit. To the extent options are vested as of the date of distribution, Verigy employees will have a period of up to three months in which to exercise the Agilent options before such options are cancelled. Retirement eligible Verigy employees will have a period of up to three years in which to exercise the Agilent options before such options are cancelled. To the extent that the Agilent options were not vested as of the distribution date, Verigy will issue new Verigy options.

Pro forma Information for Periods Prior to the Adoption of SFAS No. 123 (R)

Prior to the adoption of SFAS No. 123 (R), Agilent provided the disclosures required under SFAS No. 123, as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosures. No employee share-based compensation expense was reflected in our results of operations for the three and nine months ended July 31, 2005 for employee stock option awards

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as all options were granted with an exercise price equal to the market value of the underlying common stock on the date of grant. Our ESPP was deemed non-compensatory under the provisions of APB No. 25. Compensation expense for the non-vested performance shares granted under the LTTP was recognized based on the market price of our stock each period. Forfeitures of awards were recognized as they occurred. Previously reported amounts have not been restated.

The pro forma information for the three and nine months ended July 31, 2005 was as follows:

	Three Months Ended July 31, 2005 (in millions, except per share data)	Nine Months Ended July 31, 2005
Net income as reported	\$ 104	\$ 302
APB No. 25 compensation recognized in net income, as reported	2	4
SFAS No. 123 based compensation	(53)	(164)
Tax benefit	4	11
Net income pro forma	\$ 57	\$ 153
Net income per share:		
As reported:		
Basic	\$ 0.21	\$ 0.61
Diluted	\$ 0.20	\$ 0.61
Pro forma:		
Basic and diluted	\$ 0.12	\$ 0.31

Impact of SFAS No. 123 (R)

Agilent adopted SFAS No. 123 (R) using the modified prospective transition method beginning November 1, 2005. Accordingly, during the nine months ended July 31, 2006, we recorded share-based compensation expense for awards granted prior to but not yet vested as of November 1, 2005 as if the fair value method required for pro forma disclosure under SFAS No. 123 were in effect for expense recognition purposes adjusted for estimated forfeitures. For these awards, we have continued to recognize compensation expense using the accelerated amortization method under FIN 28. For share-based awards granted after November 1, 2005 we have recognized compensation expense based on the estimated grant date fair value method required under SFAS No. 123 (R). For these awards we have recognized compensation expense using a straight-line amortization method. As SFAS No. 123 (R) requires that share-based compensation expense be based on awards that are ultimately expected to vest, estimated share-based compensation for the three and nine months ended July 31, 2006 has been reduced for estimated forfeitures. The impact on our results for share-based compensation, including the compensation expense related to new Verigy awards, for the three and nine months ended July 31, 2006 was as follows:

	Three Months Ended July 31, 2006 (in millions, except per share data)	Nine Months Ended July 31, 2006
Cost of products and services	\$ 7	\$ 23
Research and development	3	14
Selling, general and administrative	11	45
Share-based compensation expense in continuing operations	\$ 21	\$ 82
Share-based compensation expense in discontinued operations		3
Total share-based compensation expense	\$ 21	\$ 85
Impact on continuing operations per share:		
Basic	\$ 0.05	\$ 0.19
Diluted	\$ 0.05	\$ 0.18
Impact on discontinued operations per share:		
Basic		\$ 0.01
Diluted		\$ 0.01

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Impact on net income per share:

Basic	\$	0.05	\$	0.20
Diluted	\$	0.05	\$	0.19

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Share-based compensation capitalized within inventory at July 31, 2006 and April 30, 2006 was zero and \$1.7 million, respectively.

The weighted average grant date fair value of options, as determined under SFAS No. 123 (R), granted during the three and nine months ended July 31, 2006 was \$10.85 and \$10.47 per share, respectively. For the three and nine months ended July 31, 2006 the windfall tax benefit realized from exercised stock options and similar awards was immaterial. As of July 31, 2006, the total unrecorded deferred share-based compensation balance for non-vested shares, net of expected forfeitures, was approximately \$111 million which is expected to be amortized over a weighted-average period of 2.4 years.

The weighted average grant date fair value of the new Verigy options, as determined under SFAS No. 123 (R), granted during the three and nine month periods ended July 31, 2006 was \$7.28 and \$7.28 per share, respectively. For the three and nine months ended July 31, 2006, the tax benefit realized from exercised stock options and similar awards was immaterial. As of July 31, 2006, the total unrecorded deferred share-based compensation balance for non-vested shares, net of expected forfeitures was approximately \$11 million.

Valuation Assumptions

For the three and nine months ended July 31, 2006 and 2005, the fair value of share-based awards for employee stock option awards, restricted stock and employee stock purchases made under our ESPP was estimated using the Black-Scholes option pricing model. In fiscal year 2006, shares granted under the LTPP were valued using a Monte Carlo simulation. For the three and nine months ended July 31, 2005, shares granted under the LTPP were valued using the variable accounting method under APB No. 25. During the three months ended July 31, 2006 and 2005 there were no LTPP shares granted. The weighted average assumptions used for options granted and ESPP purchases during the three and nine months ended July 31, 2006 and 2005 were as follows:

	Three Months Ended July 31, 2006		2005		Nine Months Ended July 31, 2006		2005	
Stock Option Plans:								
Risk-free interest rate	5.0	%	3.9	%	4.3	%	3.5	%
Dividend yield	0	%	0	%	0	%	0	%
Volatility	31	%	31	%	29	%	39	%
Expected life	4.25 yrs		4 yrs		4.25 yrs		4 yrs	
ESPP:								
Risk-free interest rate	5.0	%	3.3	%	4.5	%	2.4	%
Dividend yield	0	%	0	%	0	%	0	%
Volatility	26	%	26	%	29	%	37	%
Expected life	0.5 yrs		0.5-1.5 yrs		0.5-1 yrs		0.5-2 yrs	
LTPP:								
Volatility of Agilent shares			N/A		28	%	N/A	
Volatility of comparator-company shares			N/A		23%-82	%	N/A	
Price-wise correlation with comparators			N/A		50	%	N/A	

Both the Black-Scholes and Monte Carlo simulation fair value models require the use of highly subjective and complex assumptions, including the option's expected life and the price volatility of the underlying stock. Beginning November 1, 2005, the expected stock price volatility assumption was determined using the implied volatility for our stock. Prior to the adoption of SFAS No. 123 (R), we used a combination of historical and implied volatility in deriving our expected volatility assumption. We have determined that implied volatility is more reflective of market conditions and a better indicator of expected volatility than a combined method of determining volatility.

Share-Based Payment Award Activity

The following table summarizes equity share-based payment award activity for the nine months ended July 31, 2006:

	Available for Grant (in thousands)	Awards Outstanding	Weighted Average Exercise Price
Balance at October 31, 2005	41,322	72,540	\$ 28
Granted	(8,247)	8,247	\$ 34
Exercised		(17,424)	\$ 25
Cancelled/forfeited	2,493	(2,493)	\$ 38
Plan shares expired		(1,005)	\$ 43
Balance at July 31, 2006	35,568	59,865	\$ 29

The options outstanding and exercisable for equity share-based payment awards as of July 31, 2006 were in the following exercise price ranges:

Range of Exercise Prices	Options Outstanding				Options Exercisable			
	Number Outstanding (in thousands)	Weighted Average Contractual Life (in years)	Weighted Average Exercise Price	Aggregate Intrinsic Value (in thousands)	Number Exercisable (in thousands)	Weighted Average Contractual Life (in years)	Weighted Average Exercise Price	Aggregate Intrinsic Value (in thousands)
\$ 0 - 15	898	5.9	\$ 12	\$ 14,737	738	5.7	\$ 13	\$ 11,735
\$15.01 - 25	15,232	7.4	\$ 20	\$ 132,546	7,350	6.9	\$ 19	\$ 71,471
\$25.01 - 30	20,043	6.0	\$ 27	\$ 24,241	19,266	5.9	\$ 27	\$ 23,459
\$30.01 - 40	19,225	7.3	\$ 34		7,840	5.0	\$ 35	
\$40.01 - 50	2,582	2.7	\$ 44		2,582	2.7	\$ 44	
\$50.01 and over	1,885	4.0	\$ 65		1,885	4.0	\$ 65	
	59,865	6.6	\$ 29	\$ 171,524	39,661	5.6	\$ 30	\$ 106,665

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on the company's closing stock price of \$28.44 at July 31, 2006, which would have been received by award holders had all award holders exercised their awards that were in-the-money as of that date. The total number of in-the-money awards exercisable as of July 31, 2006 was approximately 24 million. The aggregate intrinsic value of awards exercised during the three and nine months ended July 31, 2006 was \$5 million and \$75 million, respectively.

As of July 31, 2006, securities authorized and available for issuance in connection with our ESPP were 25,032,661. Shares authorized for issuance in connection with the ESPP are subject to an automatic annual increase of the lesser of one percent of the outstanding common stock of Agilent or an amount determined by the Compensation Committee of our Board of Directors. In no event shall the number of shares authorized for issuance in connection with the ESPP exceed 75 million shares.

Valuation Assumptions for New Verigy Awards

The fair value of the new Verigy awards granted was estimated at grant date using a Black-Scholes options-pricing model with the following weighted-average assumptions:

	Three Months Ended July 31, 2006	Nine Months Ended July 31, 2006
Risk-free interest rate for options	5.0	% 5.0 %
Risk-free interest rate for the ESPP	5.0	% 5.0 %
Dividend yield	0	% 0 %
Volatility for options	56	% 56 %
Volatility for the ESPP	39	% 39 %

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Expected option life	4.10 yrs	4.10 yrs
Expected life for the ESPP	0.5 yrs	0.5 yrs

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Because Verigy does not have historical data, they used data from peer companies to determine their assumptions for the expected option life and the volatility of their stock price. For the risk-free interest rate, they used the rate of return on US Treasury Strips.

Share-Based Payment Award Activity for New Verigy Options

The following table summarizes equity share-based payment award activity for new Verigy options for the nine months ended July 31, 2006:

	Awards Outstanding (in thousands)	Weighted Average Exercise Price
Outstanding as of October 31, 2005		
Granted	1,202	\$ 15
Exercised		
Cancellations	(2)	\$ 15
Outstanding as of July 31, 2006	1,200	\$ 15

The following table summarizes information about all options to purchase shares of Verigy ordinary shares outstanding at July 31, 2006:

Range of Exercise Prices	Options Outstanding		Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Aggregate Intrinsic Value (in thousands)
	Number Outstanding (in thousands)				
\$ 0 15	1,197		6.9	\$ 15	\$ 23
\$15.01 20	3		7.0	\$ 16	
	1,200		6.9	\$ 15	\$ 23

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on Verigy's closing stock price of \$14.95 at July 31, 2006, which would have been received by award holders had all award holders exercised their awards that were in-the-money as of that date. As of July 31, 2006, none of the new Verigy options were exercisable. Pursuant to the vesting schedule for the director and employee options granted to date by Verigy, the first vesting date for any grant is January 8, 2007.

7. INVENTORY

	July 31, 2006 (in millions)	October 31, 2005
Finished goods	\$ 320	\$ 306
Work in progress	66	63
Raw materials	319	353
Total inventory, net of reserves	\$ 705	\$ 722

8. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table presents goodwill balances and the movements for each of our reportable segments during the nine months ended July 31, 2006:

	Electronic Measurement (in millions)	Bio-analytical Measurement	Semiconductor Test Solutions	Total
Goodwill at October 31, 2005	\$ 245	\$ 52	\$ 27	\$ 324
Goodwill arising from new acquisitions	4	60		64
Foreign currency translation impact	4	2	1	7

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Goodwill at July 31, 2006	\$	253	\$	114	\$	28	\$	395
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The component parts of other intangibles as of July 31, 2006 and October 31, 2005 are shown in the table below:

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	Purchased Other Intangible Assets		
	Gross		
	Carrying	Accumulated	Net Book
	Amount	Amortization	Value
	(in millions)		
As of October 31, 2005:			
Purchased technology	\$ 153	\$ (126)	\$ 27
Customer relationships	38	(27)	11
Total	\$ 191	\$ (153)	\$ 38
As of July 31, 2006:			
Purchased technology	\$ 207	\$ (138)	\$ 69
Customer relationships	48	(31)	17
Total	\$ 255	\$ (169)	\$ 86

We recorded approximately \$64 million of other intangibles during the nine months ended July 31, 2006.

In February 2006, we acquired the remaining 49 percent minority interest in Yokogawa Analytical Systems, a joint venture between Agilent and Yokogawa Electrical Corporation. This acquisition resulted in the recording of \$43 million in intangible assets and \$60 million of goodwill. In addition, during the nine months ended July 31, 2006 we recorded one acquisition, one earn out payment on an acquisition completed in 2005, and one joint venture buyout payment. Pro forma disclosures are not presented for these acquisitions as they were not material.

Amortization of intangible assets was \$7 million and \$18 million for the three and nine months ended July 31, 2006, respectively and \$4 million and \$10 million for the same periods in the prior year. Accumulated amortization includes approximately \$2 million favorable impact related to currency. Future amortization expense related to existing purchased intangible assets is estimated to be \$7 million for the remainder of 2006, \$25 million for 2007, \$18 million for 2008 and \$36 million thereafter.

9. RESTRICTED CASH AND CASH EQUIVALENTS

As of July 31, 2006, \$1,605 million was reported as restricted cash and cash equivalents on our condensed consolidated balance sheet. Of this amount, \$1,581 million was short-term restricted commercial paper maintained in connection with our obligations to a counterparty pursuant to the Master Repurchase Agreement and related Confirmation entered into on January 27, 2006 and reported as long-term debt on our condensed consolidated balance sheet. See Note 13, Long-Term Debt and Credit Facilities.

10. WARRANTIES

Standard Warranty

Our standard warranty terms typically extend for one year from the date of delivery, but our current accrual balance includes obligations for three year agreements from prior periods. We accrue for standard warranty costs in accordance with SFAS No. 5, Accounting for Contingencies (SFAS No. 5), based on historical trends in warranty charges as a percentage of gross product shipments. The accruals are reviewed regularly and adjusted periodically to reflect changes in warranty cost estimates. Estimated warranty charges are recorded within cost of products in the period products are sold.

	FY 2006	FY 2005
	(in millions)	
Beginning balance at November 1,	\$ 46	\$ 59
Accruals for warranties issued during the period	44	41
Accruals related to pre-existing warranties (including changes in estimates)	(1)	6
Settlements made during the period	(51)	(59)
Ending balance at July 31,	\$ 38	\$ 47

Extended Warranty

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Revenue from our extended warranty contracts with terms beyond one year is deferred and recognized on a straight-line basis over the contract period. Related costs are expensed as incurred. Short-term amounts are included in deferred revenue on the condensed consolidated balance sheet and were \$47 million and \$33 million at July 31, 2006 and October 31, 2005, respectively. The long-term amounts are recorded in other liabilities on the condensed consolidated balance sheet and were \$64 million and \$56 million at July 31, 2006 and October 31, 2005, respectively.

	FY 2006	FY 2005
	(in millions)	
Beginning balance at November 1,	\$ 89	\$ 57
Recognition of revenue	(26)	(12)
Deferral of revenue for new contracts	48	36
Ending balance at July 31,	\$ 111	\$ 81

11. RESTRUCTURING AND ASSET IMPAIRMENT

We initiated several restructuring plans in prior periods: the 2001 Plan, the 2002 Plan and the 2003 Plan (Prior Plans). The workforce reduction portion of the Prior Plans was completed during fiscal year 2005. The consolidation of excess facilities portion of Prior Plans is expected to be completed within the next five years. In addition, there may be future changes in estimates for the consolidation of excess facilities related to changes in market conditions from those originally expected at the time the charges were recorded.

In the fourth quarter of 2005, we announced the sale of our semiconductor products business, which was completed on December 1, 2005. We also announced our intention to spin-off our semiconductor test solutions business. As a consequence, we launched a new restructuring program (the FY05 Plan) in the fourth quarter of 2005 to align our workforce with our smaller revenue base. During the third quarter of 2006, we continued to execute the FY05 plan, which consists of voluntary and involuntary terminations.

A summary of restructuring activity for the nine months ended July 31, 2006 is shown in the table below:

	Workforce Reduction (in millions)	Consolidation of Excess Facilities	Impairments	Total
Ending balance at October 31, 2005	\$ 44	\$ 49		\$ 93
Total charge	95	24	26	145
Asset impairments			(26)	(26)
Cash payments	(117)	(19)		(136)
Ending balance at July 31, 2006	\$ 22	\$ 54		\$ 76

The restructuring accrual for all plans, which totaled \$76 million as of July 31, 2006 and \$93 million as of October 31, 2005, is recorded in other accrued liabilities and other long-term liabilities on the condensed consolidated balance sheet and represents estimated future cash outlays. Execution of the workforce reduction component of the FY05 Plan is expected to be completed during fiscal year 2007, however lease payments for excess facilities are expected to extend over the next five years.

During the nine months ended July 31, 2006, we consolidated several facilities due to changes in our organizational structure and recorded impairment charges of \$26 million.

A summary of the statement of operations impact of the charges resulting from all restructuring plans is shown below:

	Three Months Ended July 31, 2006 (in millions)		Nine Months Ended July 31, 2006	
	2006	2005	2006	2005
Cost of products and services	\$ 8	\$ 13	\$ 27	\$ 17
Research and development	4	7	23	9
Selling, general and administrative	28	13	95	18
Restructuring and asset impairment charges in continuing operations	\$ 40	\$ 33	\$ 145	\$ 44
Restructuring charges in discontinued operations		8		10
Total restructuring and asset impairment charges	\$ 40	\$ 41	\$ 145	\$ 54

Gain on sale of Palo Alto headquarters and San Jose site

In May 2006, we completed the sale of our headquarters site in Palo Alto, California. As part of the sale transaction, we will lease back this site and occupy it until the company completes the move to our Santa Clara campus in the fourth quarter of 2006. Total consideration from the sale was \$98.5 million and we recorded a gain of \$65 million.

During the second quarter of fiscal year 2006, we sold our San Jose site as part of our facilities consolidation process for a total consideration of \$88 million and recorded a gain of \$56 million.

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12. RETIREMENT AND POST RETIREMENT PENSION PLANS

Components of net periodic costs. For the three and nine months ended July 31, 2006 and 2005, our net pension and post retirement benefit costs were comprised of:

	Pensions		Non-U.S. Plans		U.S. Post Retirement Benefit Plans	
	U.S. Plans Three Months Ended July 31, 2006 (in millions)	2005	2006	2005	2006	2005
Service cost – benefits earned during the period	\$ 11	\$ 16	\$ 11	\$ 10	\$ 1	\$ 2
Interest cost on benefit obligation	10	10	15	14	7	7
Expected return on plan assets	(13)	(12)	(21)	(18)	(6)	(6)
Amortization and deferrals:						
Actuarial (gain) loss	(1)		9	8	1	2
Prior service cost					(2)	(3)
Net plan costs	\$ 7	\$ 14	\$ 14	\$ 14	\$ 1	\$ 2
Curtailments	(12)		1		(12)	
Settlements	(4)		(4)			
Total net plan (income) costs	\$ (9)	\$ 14	\$ 11	\$ 14	\$ (11)	\$ 2
Distribution of net plan costs						
Continuing operations	\$ (9)	\$ 12	\$ 11	\$ 14	\$ (11)	\$ 2
Discontinued operations		2				
Net plan (income) costs	\$ (9)	\$ 14	\$ 11	\$ 14	\$ (11)	\$ 2

	Pensions		Non-U.S. Plans		U.S. Post Retirement Benefit Plans	
	U.S. Plans Nine Months Ended July 31, 2006 (in millions)	2005	2006	2005	2006	2005
Service cost – benefits earned during the period	\$ 35	\$ 48	\$ 33	\$ 30	\$ 3	\$ 4
Interest cost on benefit obligation	30	30	43	44	21	21
Expected return on plan assets	(39)	(36)	(59)	(55)	(18)	(18)
Amortization and deferrals:						
Actuarial (gain) loss	(2)		25	24	5	6
Prior service cost					(8)	(9)
Net plan costs	\$ 24	\$ 42	\$ 42	\$ 43	\$ 3	\$ 4
Curtailments	(34)		1		(33)	
Settlements	(4)		(12)			
Total net plan (income) costs	\$ (14)	\$ 42	\$ 31	\$ 43	\$ (30)	\$ 4
Distribution of net plan costs						
Continuing operations	\$ 7	\$ 36	\$ 39	\$ 43	\$ (9)	\$ 4
Discontinued operations	(21)	6	(8)		(21)	
Net plan (income) costs	\$ (14)	\$ 42	\$ 31	\$ 43	\$ (30)	\$ 4

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As of December 1, 2005, due to the divestiture of the semiconductor products business, we recorded curtailments and settlements as required by SFAS No. 88, Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits, (SFAS No. 88). The impact to the U.S. Plans and the U.S. Post Retirement Benefit Plan was curtailment gains of \$22 million and \$21 million, respectively. The impact on the Non-U.S. Plans was a settlement gain of \$8 million.

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Due to the separation of our semiconductor test solutions business into a separate legal company, Verigy, as of June 1, 2006, and due to significant workforce reductions, we recorded curtailments and settlements as required by SFAS No. 88 in the third quarter. The impact to the U.S. Plans and the U.S. Post Retirement Benefit Plan was a curtailment gain of \$12 million and \$12 million, respectively as well as a \$4 million settlement gain relating to the U.S. Plans. The impact to the Non-U.S. Plans was a curtailment loss of \$1 million and a settlement gain of \$4 million.

As of October 31, 2005, the accumulated benefit obligation exceeded the fair value of the plan assets for our Non-U.S. Plans thus requiring us to record an additional minimum pension liability of \$55 million. On June 1, 2006, in accordance with the separation agreement between Agilent and Verigy, the liability for Verigy employee pension benefits was transferred to separate Verigy pension plans. Agilent funded the pension liability to the extent of the accumulated benefit obligation out of operating cash. The funded status of the Non-U.S. plans required us to reverse \$53 million of the additional minimum liability along with the related deferred tax impacts, of approximately \$20 million. As of July 31, 2006 we have \$2 million of additional minimum pension liability for our Non-U.S. pension plans.

We contributed approximately \$44 million to fund our various defined benefit plans during the three months ended July 31, 2006, including a \$31 million contribution to the Verigy pension plans as noted above and \$18 million for the same period in 2005. We contributed approximately \$114 million to fund our various defined benefit plans during the nine months ended July 31, 2006 and \$73 million for the same period in 2005. We expect to contribute approximately \$8 million during the remainder of fiscal 2006, and in addition, in accordance with the master separation and distribution agreement, we will contribute approximately \$8 million to fund the Verigy pension plans after the distribution.

13. LONG-TERM DEBT AND CREDIT FACILITIES

In January 2006, Agilent Technologies World Trade, Inc., a consolidated wholly owned subsidiary of Agilent (World Trade), entered into a Master Repurchase Agreement and related Confirmation (together, the Repurchase Agreement) with a counterparty pursuant to which World Trade sold 15,000 Class A preferred shares of one of its wholly owned subsidiaries to a counterparty, having an aggregate liquidation preference of \$1.5 billion. Pursuant to the Repurchase Agreement, World Trade is obligated to repurchase from the counterparty those preferred shares for 100 percent of their aggregate liquidation preference in January 2011. The \$1.5 billion obligation of our subsidiary to repurchase the preferred shares has been treated as long-term debt on our condensed consolidated balance sheet. The related debt issuance costs of \$25 million have been deferred and recognized in other assets on our condensed consolidated balance sheet and will be amortized over the life of the Repurchase Agreement.

Under the Repurchase Agreement, World Trade is obligated to make quarterly payments to the counterparty at a rate per annum, reset quarterly, equal to three-month LIBOR plus 28 basis points. Agilent has unconditionally and irrevocably guaranteed to the counterparty the timely payment of all obligations of World Trade. The Repurchase Agreement contains customary events of default but no financial covenants. Under the Repurchase Agreement, our subsidiary has the right to accelerate the repurchase of all or any portion of the preferred shares prior to January 2011.

In connection with the Repurchase Agreement, World Trade s wholly owned subsidiary is required to hold short-term investments. As of July 31, 2006, these investments were approximately \$1,581 million. These have been separately disclosed as restricted cash and cash equivalents on our condensed consolidated balance sheet. See Note 9, Restricted Cash and Cash Equivalents.

In December 2005, we drew down \$700 million on a \$1 billion senior secured term borrowing facility to help finance our share repurchase program. The term facility allowed us a one-time borrowing at an interest rate equal to one-month LIBOR plus 30 basis points per annum, or for shorter LIBOR periods if we and the lenders so agree. In January 2006, we applied \$700 million of the proceeds from the Repurchase Agreement to repay the full amount borrowed under the Credit Agreement. Total interest expense on the senior secured term borrowing facility was \$3.6 million. The senior secured term borrowing facility expired in the first quarter of fiscal 2006.

14. STOCK REPURCHASE PROGRAM

During the fourth quarter of 2005, our Board of Directors authorized a stock repurchase program of up to \$4,466 million of our common stock. Under the program, during the fourth quarter of 2005, we repurchased 8.9 million shares for \$290 million. In November 2005, we announced our plan to commence a modified Dutch Auction tender offer for an additional 73 million shares under the program with the right to repurchase up to an additional 2 percent of our outstanding shares as of October 31, 2005. In December 2005, the tender offer expired, and we agreed to accept for payment 83 million shares at a purchase price of \$36 per share for an aggregate amount of approximately \$3 billion.

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During the third quarter of 2006, we completed our stock repurchase program. Since the initial announcement in the fourth quarter of 2005, we have repurchased approximately 125 million shares of our common stock for approximately \$4,466 million. In addition, we capitalized \$3 million of service and legal fees. Such shares are held as treasury stock and the related costs are accounted for using the cost method.

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15. COMPREHENSIVE INCOME

The following table presents the components of comprehensive income:

	Three Months Ended	
	July 31, 2006	2005
Net income	\$ 227	\$ 104
Other comprehensive income:		
Change in unrealized gain (loss) on investments	(2)	5
Change in unrealized gain (loss) on derivative instruments	(2)	10
Foreign currency translation	9	(86)
Change in minimum pension liability	53	
Deferred taxes	(18)	(5)
Comprehensive income	\$ 267	\$ 28

	Nine Months Ended	
	July 31, 2006	2005
Net income	\$ 3,158	\$ 302
Other comprehensive income:		
Change in unrealized gain (loss) on investments	(7)	14
Change in unrealized gain (loss) on derivative instruments	(8)	15
Foreign currency translation	46	(60)
Change in minimum pension liability	53	1
Deferred taxes	(17)	(8)
Comprehensive income	\$ 3,225	\$ 264

16. OTHER INCOME (EXPENSE), NET

The following table presents the components of other income (expense), net for the three and nine months ended July 31, 2006 and 2005, respectively:

	Three Months Ended		Nine Months Ended	
	July 31, 2006	2005	July 31, 2006	2005
Interest income	\$ 49	\$ 22	\$ 132	\$ 51
Interest expense	(21)	(9)	(44)	(24)
Rental income	4	7	14	22
Investment gains	1		12	8
Fee for cooperation in tax study	13		13	
Other, net	(2)	5	12	3
Other income (expense), net	\$ 44	\$ 25	\$ 139	\$ 60

Interest income is derived principally from short-term commercial paper for our restricted cash and cash equivalents and the investment of our surplus cash balances in bank time deposits and other money market instruments. The fee for cooperation in tax study is related to an agreement with Hewlett-Packard to provide assistance with a Foreign Sales Corporation Maximization Study for years prior to the 2000 spin-off of Agilent from Hewlett-Packard. For its services, Agilent earned a fee which was contingent on tax benefits having been realized.

17. PROVISION FOR TAXES

For the three and nine months ended July 31, 2006, we recorded an income tax provision of \$18 million and \$61 million on continuing operations compared to \$19 million and \$53 million in the same periods last year. The income tax provision for the three and nine months ended

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July 31, 2006, include a benefit of \$29 million related to the resolution of domestic tax-related issues for years covered by a Tax Sharing Agreement between Agilent and Hewlett Packard. The Tax Sharing Agreement is related to the 2000 spin-off of Agilent from Hewlett-Packard. For the three and nine months ended July 31, 2006, we recorded an income tax provision of zero and \$10 million, compared to \$6 million and \$18 million, respectively, on discontinued operations last year. The provision was recorded for taxes on income generated in jurisdictions other than the U.S. and entities in other foreign jurisdictions in which the company has a full valuation allowance. We intend to maintain a full valuation allowance in these jurisdictions until sufficient positive evidence exists to support the reversal of the valuation allowance.

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18. EQUITY IN NET INCOME OF UNCONSOLIDATED AFFILIATE AND GAIN ON SALE- LUMILEDS

Lumileds Lighting International, B.V. (Lumileds), was a global joint venture between Agilent and Koninklijke Philips Electronics N.V. (Philips) under a Second Amended and Restated Joint Venture Agreement (the Joint Venture Agreement), dated as of November 29, 2004, between Agilent and Philips. Lumileds manufactures high-power light emitting diodes and solid-state lighting solutions. Our ownership interest in Lumileds was approximately 47 percent as of October 31, 2005, after selling 1 percent of our interest to Philips in the second quarter of 2005. Our equity in the net income of our unconsolidated affiliate including gain on sale of our interest in Lumileds for the three and nine months ended July 31, 2006 was zero and \$901 million, respectively, and \$13 million and \$36 million respectively in the prior year.

On November 28, 2005, we completed the sale of our stake in Lumileds. Pursuant to the Share Purchase Agreement, upon closure of the sale transaction, the Joint Venture Agreement and the ancillary agreements were terminated. The purchase price paid by Philips under the Share Purchase Agreement was \$948.5 million. In addition, Lumileds repaid the \$51 million of outstanding principal debt and accrued interest due to us as of the date of sale under the Credit Agreement, dated as of November 30, 2001.

The following table shows the components of the gain from sale of Lumileds, net of income tax (in millions):

Proceeds	\$ 949
Net book value of investments	(48)
Gain on sale before taxes	901
Income taxes	
Gain from sale of Lumileds, net of taxes	\$ 901

The tax impact of the sale of our Lumileds joint venture primarily reflects the utilization of valuation allowance within the U.S.

19. SEPARATION OF OUR SEMICONDUCTOR TEST SOLUTIONS BUSINESS, VERIGY LTD.

On August 15, 2005, Agilent announced its intention to separate its semiconductor test solutions business, Verigy, into a stand-alone publicly traded company. During the third quarter of fiscal 2006, Verigy completed the initial public offering (IPO) of 8.7 million of its ordinary shares at a price of \$15 per share for total net proceeds of \$121 million. As part of the offering, Agilent made a payment to Verigy of \$19 million, the amount by which the net IPO proceeds were insufficient to complete the agreed-upon Verigy initial capitalization of \$140 million. Following the offering, Agilent owns approximately 50 million shares or 85 percent of Verigy s ordinary shares. After the offering and through the expected distribution of Agilent s shares in Verigy, Verigy will be a majority-owned subsidiary of Agilent and its results of operations and financial position will be consolidated in our consolidated financial statements.

As a result of the IPO, Agilent recorded additional paid-in capital of \$74 million related to the excess of the IPO price over the book value of the shares sold. Underwriter fees related to the IPO were approximately \$9 million which were netted against the proceeds. Agilent recorded direct IPO costs of \$2 million related to third-party legal fees, filing fees and other services. In addition, the formation of and transfer of assets to separate Verigy legal entities was subject to income taxes. As a result, Agilent recorded prepaid taxes of \$14 million.

Verigy and Agilent, and, in some cases, their respective subsidiaries, have entered into agreements providing for the June 1, 2006 separation of the semiconductor test solutions business from Agilent, including a master separation and distribution agreement. These agreements cover a variety of matters, including the transfer, ownership and licensing of intellectual property and other assets and liabilities relating to Verigy s businesses, the use of shared facilities, employee and tax-related matters and the transitional services Agilent will provide to Verigy. In addition, an ancillary agreement provided for a \$25 million revolving credit facility from Agilent to Verigy on the separation date with interest at one-month LIBOR plus 50 basis points. Amounts borrowed under the credit facility matured on the 30th day after the closing of Verigy s IPO. As of July 31, 2006, all amounts were paid back and the credit facility has expired. The agreements relating to the separation from Agilent have been negotiated in the context of a parent-subsiidiary relationship.

As of July 31, 2006, Agilent s minority interest liability was \$56 million. The distribution of Agilent s remaining shares in Verigy is expected to occur by the end of fiscal 2006. However, there are various conditions to the completion of the distribution and Agilent will determine the timing, structure and all terms of the distribution taking into account factors such as market conditions. Agilent will not be obligated to complete the distribution, and the distribution may not occur by the fiscal year end or at all. Per the transitional services agreement, Agilent expects that the majority of the services provided to Verigy will terminate on or before the distribution date, provided that such services may extend beyond the distribution date if mutually agreed upon by Agilent and Verigy.

Indemnifications to Verigy

In connection with the spin-off of Verigy, we agreed to indemnify Verigy and its affiliates against damages which it might incur in the future. These indemnifications primarily cover damages relating to liabilities of the businesses that Agilent retained and did not transfer to Verigy, liabilities that might arise under limited portions of Verigy's IPO materials that relate to Agilent, and costs and expenses incurred by Agilent or Verigy to effect the IPO, arising out of the proposed distribution of Verigy ordinary shares owned by Agilent to Agilent's stockholders, or incurred to effect the separation of the semiconductor test solutions business from Agilent to the extent incurred prior to the separation on June 1, 2006.

20. SEGMENT INFORMATION

Agilent is a measurement company, providing core bio-analytical and electronic measurement solutions to the communications, electronics, life sciences and chemical analysis industries. During the second half of 2005, we reorganized our business operations into three businesses—electronic measurement, bio-analytical measurement, and semiconductor test solutions—each of which comprises a reportable segment. As part of the reorganization, we transferred two divisions from our semiconductor test solutions segment formerly known as automated test to the electronic measurement segment. The segments were determined based primarily on how the chief operating decision maker views and evaluates our operations. Other factors, including customer base, homogeneity of products, technology and delivery channels, were also considered in determining our reportable segments on a management basis.

During the second half of 2005, Agilent also announced its intention to separate its semiconductor test solutions business, Verigy, into a stand-alone publicly traded company. In the third quarter of 2006, Verigy completed its IPO. Verigy's standalone results differ from Agilent's presentation of semiconductor test solutions as one of its segments. See Note 19, "Separation of Our Semiconductor Test Solutions Business, Verigy Ltd." for further information.

A significant portion of the segments' expenses arise from shared services and infrastructure that we have historically provided to the segments in order to realize economies of scale and to efficiently use resources. These expenses, collectively called corporate charges, include costs of centralized research and development, legal, accounting, employee benefits, real estate, insurance services, information technology services, treasury and other corporate infrastructure expenses. Charges are allocated to the segments, and the allocations have been determined on a basis that we considered to be a reasonable reflection of the utilization of services provided to or benefits received by the segments. After its separation on June 1, 2006, Agilent started billing Verigy for their use of shared services under the transition services agreement. Corporate charges previously allocated to our semiconductor products business, but not classified within discontinued operations, were not reallocated to our other segments. These charges are presented below as a component of the reconciliation between the segments' income from operations and Agilent's income from continuing operations and are classified as unallocated semiconductor products business corporate charges.

The following tables reflect the results of our reportable segments under our management reporting system. These results are not necessarily in conformity with generally accepted accounting principles in the U.S. The performance of each segment is measured based on several metrics, including income from operations. These results are used, in part, by the chief operating decision maker in evaluating the performance of, and in allocating resources to, each of the segments.

The profitability of each of the segments is measured after excluding amortization and impairment of other intangibles, restructuring and asset impairment charges, investment gains and losses, interest income, interest expense and other items as noted in the reconciliation below.

	Electronic Measurement (in millions)	Bio-analytical Measurement	Semiconductor Test Solutions	Total
Three months ended July 31, 2006:				
Total net revenue	\$ 848	\$ 391	\$ 214	\$ 1,453
Segment income from operations	\$ 125	\$ 60	\$ 45	\$ 230
Three months ended July 31, 2005:				
Total net revenue	\$ 783	\$ 341	\$ 117	\$ 1,241
Segment income (loss) from operations	\$ 77	\$ 42	\$ (18)	\$ 101

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Our total segment revenues were \$1 million lower as compared to total Agilent net revenue for the three months ended July 31, 2005 due to rounding.

	Electronic Measurement (in millions)	Bio-analytical Measurement	Semiconductor Test Solutions	Total
Nine months ended July 31, 2006:				
Total net revenue	\$ 2,509	\$ 1,136	\$ 575	\$ 4,220
Segment income from operations	\$ 334	\$ 157	\$ 90	\$ 581
Nine months ended July 31, 2005:				
Total net revenue	\$ 2,399	\$ 1,039	\$ 294	\$ 3,732
Segment income (loss) from operations	\$ 229	\$ 132	\$ (89)	\$ 272

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The following table reconciles reportable segments' income from operations to Agilent's total enterprise income from continuing operations before income taxes and equity income:

	Three Months Ended		Nine Months Ended	
	July 31, 2006	2005	July 31, 2006	2005
	(in millions)			
Total reportable segments' income from operations	\$ 230	\$ 101	\$ 581	\$ 272
Restructuring and asset impairment (1)	(40)	(33)	(145)	(41)
Business separation and infrastructure reduction costs	(46)		(111)	
Other income (expense), net	44	25	139	60
Gain on sale of Palo Alto headquarters and San Jose site	65		121	
Unallocated semiconductor products business corporate charges		(32)	(13)	(100)
Share-based compensation	(21)		(82)	
Pension curtailment gain and settlements	28		28	
Amortization of intangibles and other	(9)	(1)	(15)	(16)
Income from continuing operations before income taxes and equity income, as reported	\$ 251	\$ 60	\$ 503	\$ 175

(1) For the nine months ended July 31, 2005, restructuring and asset impairment does not include \$3 million of charges that were included in the segments' income from operations.

The following table reflects segment assets under our management reporting system. Segment assets include allocations of corporate assets, including deferred tax assets, goodwill, other intangibles and other assets.

	Electronic Measurement (in millions)	Bio-analytical Measurement	Semiconductor Test Solutions	Total
Assets:				
As of July 31, 2006	\$ 2,176	\$ 918	\$ 329	\$ 3,423
As of October 31, 2005	\$ 2,009	\$ 690	\$ 312	\$ 3,011

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (UNAUDITED)

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto included elsewhere in this Form 10-Q and in our Annual Report on Form 10-K. This report contains forward-looking statements including, without limitation, statements regarding trends, seasonality and growth in the markets we sell into, our strategic direction, our future effective tax rate and tax valuation allowance, remediation activities, new product and service introductions, product pricing, changes to our manufacturing processes, the impact of local government regulations on our ability to pay vendors or conduct operations, our liquidity position, our ability to generate cash from continuing operations, growth in our businesses, our investments, and the potential impact of our adopting new accounting pronouncements, our financial results, revenue generated from international sales, our contributions to our pension plans, our cost-control activities, the status of our restructuring programs including our lease and severance payment obligations, completion of the spinoff of the company's semiconductor test solutions business, Verigy Ltd. (Verigy), our transition to lower-cost regions, the existence or length of an economic recovery that involve risks and uncertainties. Our actual results could differ materially from the results contemplated by these forward-looking statements due to various factors, including those discussed below in Factors That May Affect Future Results and elsewhere in this Form 10-Q.

Basis of Presentation

The financial information presented in this Form 10-Q is not audited and is not necessarily indicative of our future consolidated financial position, results of operations or cash flows. Our fiscal year end is October 31, and our fiscal quarters end on January 31, April 30 and July 31. Unless otherwise stated, all dates refer to our fiscal year and fiscal periods.

In the first quarter of 2006, we completed the divestiture of our semiconductor products business. The results of our semiconductor products business are presented as a discontinued operation for all periods in the condensed consolidated financial statements included herein. See Note 4, Discontinued Operations. In the third quarter of 2006, we completed the initial public offering of our semiconductor test solutions business, Verigy Ltd., (Verigy). Verigy is a majority-owned subsidiary of Agilent and its results of operations and financial position will be consolidated in our financial statements until the expected distribution of our remaining shares in Verigy. For further information, see Note 19, Separation of Our Semiconductor Test Solutions Business, Verigy Ltd.

Restricted cash and cash equivalents in the condensed consolidated balance sheet as of October 31, 2005 have been reclassified to conform to the current period's presentation. Equity in net income of unconsolidated affiliate and gain on sale Lumileds in the condensed consolidated statement of operations and condensed consolidated statement of cash flows for the periods ended July 31, 2005 have been reclassified to conform to the current period's presentation.

Executive Summary

Agilent Technologies, Inc. (we, Agilent or the company), is the world's premier measurement company providing core bio-analytical and electronic measurement solutions to the communications, electronics, life sciences and chemical analysis industries. Agilent has two primary businesses focused on the electronic measurement market and the bio-analytical measurement market.

In the third quarter of 2005, we announced our intention to divest our semiconductor products business and our semiconductor test solutions business. In the first quarter of 2006, we completed the sale of our semiconductor products business. In the third quarter of 2006, we completed the initial public offering of 15 percent of our semiconductor test solutions business and plan to distribute the remaining ownership to Agilent shareholders by the end of the fiscal year.

For the three and nine months ended July 31, 2006, total orders were \$1.4 billion and \$4.4 billion, respectively, up 10 percent and 15 percent in comparison to the same periods last year. Net revenue of \$1.5 billion and \$4.2 billion for the three and nine months ended July 31, 2006 was up 17 percent and 13 percent, respectively, from the same periods last year.

In the electronic measurement business, we saw growth in both wireless test and general purpose test. Wireless test revenue grew due to increased demand for low-cost phones in China and India, as well as investments in 3G manufacturing and manufacturing components that go into consumer devices. General purpose test revenue grew as a result of demand for our electronic manufacturing test products.

In the bio-analytical measurement business, results were driven by our new product portfolio and a diverse global customer base. The new 1200 High Performance Liquid Chromatography (HPLC) series, as well as our new Liquid Chromatography/Mass Spectrometry (LC/MS) systems,

drove revenue growth worldwide.

Net income for the three and nine months ended July 31, 2006 was \$227 million and \$3,158 million, respectively, and \$104 million and \$302 million for the corresponding periods last year. Net income for the nine months ended July 31, 2006 includes the sale of our investment in Lumileds Lighting International B.V. (Lumileds) to Koninklijke Philips Electronics N.V. (Philips) for a gain of \$901 million and the divestiture of our semiconductor products business for a gain, net of tax, of \$1,809 million. As of the end of

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the third quarter, we have reduced our global infrastructure costs commensurate with our size and profile as a pure-play measurement company.

In January 2006, Agilent Technologies World Trade, Inc., a consolidated wholly owned subsidiary of Agilent (World Trade), entered into a Master Repurchase Agreement and related Confirmation with a counterparty pursuant to which World Trade sold 15,000 Class A preferred shares of one of its wholly owned subsidiaries to a counterparty having an aggregate liquidation preference of \$1.5 billion, and received \$1.5 billion in cash, net of debt issuance costs. In the third quarter of 2006, we completed our \$4.466 billion share repurchase program.

Looking forward, our focus will be on achieving revenue growth that is critical to leveraging our operating model. Our primary strategy is to pursue profitable revenue growth by expanding our leadership in core markets and seeking opportunities to move into adjacent markets.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Condensed Consolidated Financial Statements, which have been prepared in accordance with generally accepted accounting principles (GAAP) in the U.S. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances. The results of these estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from our estimates.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used or changes in the accounting estimate that are reasonably likely to occur could materially change the financial statements. No events occurred or circumstances changed during the period ended July 31, 2006 that required us to test goodwill for impairment. Management believes the accounting for share-based compensation, under Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS No. 123(R)), is a critical accounting policy which we adopted at the beginning of fiscal year 2006. There have been no other significant changes during the nine months ended July 31, 2006 to the items that we disclosed as our critical accounting policies and estimates in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended October 31, 2005.

Adoption of New Pronouncements

During the first fiscal quarter of 2006, we adopted SFAS No. 123 (R). See Note 6 of the condensed consolidated financial statements for a description of the pronouncement and the effects on our results of operations and financial position.

Restructuring and Asset Impairment

We initiated several restructuring plans in prior periods: the 2001 Plan, the 2002 Plan and the 2003 Plan (Prior Plans). We have executed all key activities on the Prior Plans. However, charges in connection with the consolidation of excess facilities continue to be recorded related to changes in market conditions. Lease payments and market adjustments will continue to be recorded for five years. In addition, there may be future changes in estimates for the consolidation of excess facilities related to changes in market conditions from those originally expected at the time the charges were recorded.

In the fourth quarter of 2005, we announced the sale of our semiconductor products business, which we subsequently completed on December 1, 2005, and our intention to spin off our semiconductor test solutions business. As a consequence, we launched a new restructuring program (the FY05 Plan) in the fourth quarter of 2005 to align our workforce with our smaller revenue base. The FY05 Plan consists of voluntary and involuntary terminations. We expect to finalize the FY05 Plan by the end of fiscal 2006 and complete execution of the FY05 Plan by fiscal 2007.

See Note 11, Restructuring and Asset Impairment, of the condensed consolidated financial statements for a description of the restructuring and asset impairment activity.

Foreign Currency

Our revenues, costs and expenses, and monetary assets and liabilities are exposed to changes in foreign currency exchange rates as a result of our global operating and financing activities. We hedge net cash flow and balance sheet exposures that are not denominated in the functional currencies of our subsidiaries on a short term and anticipated basis. We do experience some fluctuations within individual lines of the condensed consolidated statement of operations and balance sheet as our hedging program is not designed to offset the currency movements in each

category of revenues, expenses, monetary assets and liabilities. However,

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movements in exchange rates net of our hedging activities had no material effect on our net income in the periods presented.

Results from Continuing Operations

Orders and Net Revenue

	Three months ended July 31, 2006 (in millions)		Nine months ended July 31, 2006		Year over Year Change Three Months		Year over Year Change Nine Months	
	2005		2005		%		%	
Orders	\$ 1,424	\$ 1,300	\$ 4,365	\$ 3,791	10	%	15	%
Net revenue:								
Products	\$ 1,208	\$ 1,015	\$ 3,502	\$ 3,040	19	%	15	%
Services and other	245	227	718	692	8	%	4	%
Total net revenue	\$ 1,453	\$ 1,242	\$ 4,220	\$ 3,732	17	%	13	%

	Three months ended July 31, 2006		Nine months ended July 31, 2006		Year over Year Change Three Months		Year over Year Change Nine Months	
	%		%		%		%	
% of total net revenue:								
Products	83	%	82	%	83	%	81	%
Services and other	17	%	18	%	17	%	19	%
Total	100	%	100	%	100	%	100	%

Orders increased 10 percent and 15 percent for the three and nine months ended July 31, 2006, respectively, compared to the same periods in 2005, with all our businesses achieving growth. Our electronic measurement business achieved growth of 4 percent and 6 percent for the three and nine months ended July 31, 2006, respectively, while our bio-analytical measurement business achieved growth of 11 percent and 7 percent for the three and nine months ended July 31, 2006, respectively. Our semiconductor test solutions business, Verigy, achieved growth of 37 percent and 113 percent for the three and nine months ended July 31, 2006.

Net revenue increased 17 percent and 13 percent for the three and nine months ended July 31, 2006 compared to the same periods last year, with revenue growing faster than orders for the three months ended July 31, 2006 and revenue growth trends across the businesses similar to those seen for orders for the nine months ended July 31, 2006.

Services and other revenue include revenue generated from servicing our installed base of products, warranty extensions and consulting. Services and other revenue for the three and nine months ended July 31, 2006 increased by 8 percent and 4 percent, respectively, as compared to the same period last year. Service revenue trends tend to lag product revenue due to significant service revenue recognition being spread over extended time periods.

Operating Results

	Three months ended July 31, 2006 (in millions, except for percentages)		Nine months ended July 31, 2006		Year over Year Change Three Months		Year over Year Change Nine Months	
	2005		2005		%		%	
Gross margin on products	58	%	51	%	55	%	51	%
Gross margin on services and other	38	%	37	%	37	%	38	%
Total gross margin	54	%	48	%	52	%	49	%
Operating margin	14	%	3	%	9	%	3	%
Research and development	\$ 186	\$	183	\$	572	\$	547	
Selling, general and administrative	\$ 463	\$	378	\$	1,387	\$	1,165	
Gain on sale of Palo Alto headquarters	\$ (65)	\$		\$	(121)	\$	100	

and San Jose site

The following tables present the gross inventory changes and sales of previously reserved inventory, respectively.

Gross inventory charges

	Three Months Ended		Nine Months Ended	
	July 31, 2006	2005	July 31, 2006	2005
	(in millions)		(in millions)	
Bio-Analytical Measurement	1	1	3	2
Electronic Measurement	6	4	24	28
Semiconductor Test Solutions	2	6	16	11
Unallocated charges (1)		2	1	7
Total	9	13	44	48

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(1) Unallocated charges primarily relate to inventory write-downs for exited product lines, which management has not reflected in segment results.

Sale of previously reserved for inventory

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2006 (in millions)	2005	2006 (in millions)	2005
Bio-Analytical Measurement				(1)
Electronic Measurement	(5)	(1)	(10)	(4)
Semiconductor Test Solutions	(2)	(3)	(9)	(6)
Total	(7)	(4)	(19)	(11)

Backlog. We believe that backlog orders are not a meaningful indicator of future business prospects. Backlog, as we define it, generally only represents cumulative outstanding orders that are scheduled for delivery within a six-month period. Therefore backlog is not a material indicator of our medium or long-term business prospects. We believe that our incoming orders in any given period are more indicative of short-term revenue trends for our businesses.

Total gross margin increased 6 percentage points and 3 percentage points for the three and nine months ended July 31, 2006, respectively, compared to the same periods last year. For both the three and nine month periods ended July 31, 2006, \$11 million of the gross profit improvement, or a 2 percentage point gross margin increase for the three month period and 1 percentage point increase for the nine month period, was due to reduced general infrastructure allocations to cost of goods sold. The Agilent headcount profile is less manufacturing intensive due to the divestiture of semiconductor products. During the third quarter of fiscal year 2006, general infrastructure allocations were updated to match our new headcount profile, resulting in relatively lower allocations to cost of goods sold and higher allocations to research and development and selling, general and administrative expenses.

Research and development expenses increased 2 percent and 5 percent for the three and nine months ended July 31, 2006, respectively, compared to the same periods last year. Approximately \$2 million of the increase was due to the above-mentioned general infrastructure allocation shift. However, research and development expenses decreased 2 percent and 1 percent as a percentage of total net revenues for both the three and nine months ended July 31, 2006, compared to the same periods last year. We remain committed to bringing new products to market, and have focused our development efforts on key strategic opportunities in order to align our business with available markets and position ourselves to capture market share.

Selling, general and administrative expenses increased 22 percent and 19 percent for the three and nine months ended July 31, 2006, respectively, compared to the same periods last year, primarily due to increased employee related costs, such as variable pay and stock-based compensation expense, increased marketing costs associated with new product launches, and approximately \$9 million due to the above-mentioned general infrastructure allocation shift.

Gain on sale of Palo Alto headquarters and San Jose site was \$65 million and \$121 million in the three months and nine months ended July 31, 2006, respectively. See Note 11, Restructuring and Asset Impairment, of our condensed consolidated financial statements for further information.

At July 31, 2006, our headcount was approximately 20,100 as compared to approximately 21,100 at July 31, 2005.

Other Income (Expense), Net

Other income (expense), net was \$44 million and \$139 million for the three and nine months ended July 31, 2006, respectively. For the same periods last year, other income (expense), net was \$25 million and \$60 million, respectively. The increase in other income (expense), net is mainly due to interest income earned on our cash balances. See Note 16, Other income (expense), net, of our condensed consolidated financial statements for further information.

Equity in Net Income of Unconsolidated Affiliate Lumileds

Lumileds was a global joint venture between Agilent and Philips. Lumileds manufactures high-power light emitting diodes and solid-state lighting solutions. Agilent sold its interest in Lumileds on November 28, 2005. Our equity in net income of our unconsolidated affiliate for the

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three months ended July 31, 2006 and 2005 was zero and \$13 million, respectively. Our equity in net

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income from and gain on sale of our unconsolidated affiliate for the nine months ended July 31, 2006 was \$901 million, and our equity in net income was \$36 million as of the same period last year.

General Infrastructure and Shared Services

Infrastructure costs were \$71 million and \$183 million lower for the three and nine months ended July 31, 2006, compared to the same periods last year. Infrastructure expense reductions were related to services moved to lower cost regions, IT and facilities savings related to the semiconductor products group divestiture, and previously announced restructuring programs. We allocate expenses to our businesses according to usage of related services.

Tax Valuation Allowance and Provision for Taxes

For the three and nine months ended July 31, 2006, we recorded an income tax provision of \$18 million and \$61 million on continuing operations compared to \$19 million and \$53 million in the same periods last year. The income tax provision for the three and nine months ended July 31, 2006, include a benefit of \$29 million related to the resolution of domestic tax-related issues for years covered by a Tax Sharing Agreement between Agilent and Hewlett Packard. The Tax Sharing Agreement is related to the 2000 spin-off of Agilent from Hewlett-Packard. For the three and nine months ended July 31, 2006, we recorded an income tax provision of zero and \$10 million, compared to \$6 million and \$18 million, respectively, on discontinued operations last year. The provision was recorded for taxes on income generated in jurisdictions other than the U.S. and entities in other foreign jurisdictions in which the company has a full valuation allowance. We intend to maintain a full valuation allowance in these jurisdictions until sufficient positive evidence exists to support the reversal of the valuation allowance.

For 2006, the current estimate of the annual effective tax rate is 6.2 percent on continuing operations. The income tax rate for continuing operations was 4.3 percent for the nine months ended July 31, 2006. The tax impact of both the sale of our semiconductor products business (which is reported in discontinued operations) and our Lumileds joint venture (which is reported in continuing operations) reflected the utilization of valuation allowance within the U.S. and a low effective tax rate in other jurisdictions. Both transactions were treated as discrete events during the quarter ended January 31, 2006. Excluding the impact of the sale of the Lumileds joint venture, we anticipate the full-year 2006 effective tax rate on continuing operations to be approximately 14.4 percent. The overall tax rate reflects taxes in jurisdictions other than the U.S. and entities in other jurisdictions in which income tax or benefit continues to be offset by adjustments to the valuation allowance. This tax rate may change over time as the amount or mix of income and taxes changes. Our effective tax rate is calculated using our projected annual pre-tax income or loss from continuing operations and is affected by research and development tax credits, the expected level of other tax benefits, the effects of business acquisitions and dispositions, the impact of changes to the valuation allowance, changes in other comprehensive income, as well as changes in the mix of income and losses in those jurisdictions in which the Company operates which have varying statutory rates.

Segment Overview

Agilent is the world's premier measurement company providing core bio-analytical and electronic measurement solutions to the communications, electronics, life sciences and chemical analysis industries. Agilent has two primary businesses focused on the electronic measurement market and the bio-analytical measurement market.

In the third quarter of 2005, we announced our intention to divest our semiconductor products business and our semiconductor test solutions business. See Note 19, Separation of Our Semiconductor Test Solutions Business, Verigy Ltd. In the first quarter of 2006, we completed the sale of our semiconductor products business. In the third quarter of 2006, we completed the initial public offering of 15 percent of our semiconductor test solutions business and plan to distribute the remaining ownership to Agilent shareholders by the end of the fiscal year. In addition to the segment discussion below also see Note 20, Segment Information, of our condensed consolidated financial statements. Because of the planned spinoff of Verigy, Agilent is not reporting separate segment results for this business in this portion of our quarterly report on Form 10-Q.

Electronic Measurement

Our electronic measurement business provides standard and customized solutions that are used in the design, development, manufacture, installation, deployment and operation of electronic equipment and systems and communications networks and services.

Orders and Net Revenue

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	Three Months Ended		Nine Months Ended		Year over Year Change			
	July 31, 2006 (in millions)	2005	July 31, 2006	2005	Three Months	%	Nine Months	%
Orders	\$ 838	\$ 807	\$ 2,512	\$ 2,379	4	%	6	%
Net revenue	\$ 848	\$ 783	\$ 2,509	\$ 2,399	8	%	5	%

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Overall orders for the three and nine months ended July 31, 2006 increased 4 percent and 6 percent respectively compared with the same periods of the prior year.

Communications test orders accounted for approximately 60 percent of the electronic measurement business. Communications test orders increased 2 percent year-over-year for the three months ended July 31, 2006, and 3 percent year-over-year for the nine months ended July 31, 2006. Order increases were primarily due to spending on new and emerging wireless technologies, investment in converged device development, and continued strength of low-cost handset manufacturing in Asia.

General purpose test orders accounted for approximately 40 percent of the electronic measurement business. General purpose test orders increased 7 percent year-over-year for the three months ended July 31, 2006, and 10 percent year-over-year for the nine months ended July 31, 2006. Order increases were driven by above-market growth across the oscilloscope product lines, and strength of sales into the semiconductor industry.

Our communications test and general purpose test information above reflect a characterization by product category. We are moving toward a new methodology for defining communications test and general purpose test as the markets into which our products are sold.

Revenues for the three and nine months ended July 31, 2006 increased 8 percent and 5 percent respectively, compared to the same periods last year. Communications test increased 11 percent and 8 percent for the three and nine months ended July 31, 2006 compared to the same periods last year driven by stronger demand in handset manufacturing and wireless component test. General purpose test increased 4 percent and decreased 2 percent respectively, compared to prior year for the three and nine months ended July 31, 2006, with increased demand from semiconductor manufacturing driving stronger revenue from parametric test and nano-positioning equipment.

Looking forward, we expect gradual growth for our electronic measurement business. We expect growth to be driven by our customers expansion of wireless 3G coverage and services (high data rate, multi-media services supported by multi-functional handsets); as well as by wireline opportunities in broadband access, voice-over-internet-protocol, and fiber-to-the-home. This growth potential could be mitigated by potential budgetary pressures and delays on major U.S. Defense programs, and by potential delays in deployment of new communications technologies due to regulatory or economic pressures.

Operating Results

	Three Months Ended		Nine Months Ended		Year over Year Change			
	July 31, 2006	2005	July 31, 2006	2005	Three Months	Nine Months		
	(in millions, except for percentages)							
Gross margin	58	% 53	% 56	% 53	% 5	ppts 3		ppts
Operating margin	15	% 10	% 13	% 10	% 5	ppts 3		ppts
Research and development	\$ 118	\$ 110	\$ 347	\$ 338	7	% 3		%
Selling, general and administrative	\$ 249	\$ 228	\$ 727	\$ 694	9	% 5		%

Gross margin increased 5 percentage points and 3 percentage points respectively for the three and nine months ended July 31, 2006, compared to the same periods last year. The increase was mainly driven by higher volumes, lower manufacturing overhead, product design improvements, lower inventory charges and lower warranty costs.

Research and development expenses for the three and nine months ended July 31, 2006 increased 7 percent and 3 percent respectively, as compared to the same periods last year, driven by continued investment in new technologies and market expansion opportunities. Selling, general and administrative expenses increased 9 percent and 5 percent respectively for the three and nine months ended July 31, 2006, over the same periods in the prior year, driven by increased variable employee related costs associated with better financial performance and increased marketing communication expense in support of new product launches. Income from operations for the three and nine months ended July 31, 2006, increased \$48 million and \$105 million respectively, compared to the same periods last year.

Bio-analytical Measurement

Our bio-analytical measurement business provides application-focused solutions that include instruments; software, consumables and services that enable customers to identify quantify and analyze the physical and biological properties of substances and products. Our seven key product categories include: microarrays, microfluidics, gas chromatography, liquid chromatography, mass spectrometry, software and informatics, and related consumables, reagents and services.

Orders and Net Revenue

	Three Months Ended		Nine Months Ended		Year over Year Change			
	July 31, 2006 (in millions)	2005	July 31, 2006	2005	Three Months	%	Nine Months	%
Orders	\$ 387	\$ 348	\$ 1,166	\$ 1,089	11	%	7	%
Net revenue	\$ 391	\$ 341	\$ 1,136	\$ 1,039	15	%	9	%

Orders for the three and nine months ending July 31, 2006 grew 11 percent and 7 percent from the same periods last year.

Chemical analysis orders increased 10 percent year-over-year for the three months ended July 31, 2006, and 6 percent year-over-year for the nine months ended July 31, 2006. This reflects the strong demand we saw for our new liquid chromatography and liquid chromatography/mass spectrometry products, particularly the Rapid Resolution System. In addition, higher oil prices continued to drive increased demand for instrumentation in the petrochemical and hydrocarbon industries, as well as system upgrades for the refinery infrastructure.

Life sciences orders increased 13 percent year-over-year for the three months ended July 31, 2006, and 8 percent year-over-year for the nine months ended July 31, 2006. Americas had solid single-digit growth for the three months ended July 31, 2006; but growth was relatively flat for the nine months ended July 31, 2006. This was due to soft spending by pharmaceutical companies in the Americas region. However, the soft pharmaceutical company spending was offset by increased demand from contract research organizations and generic drug manufacturers in Europe and Asia. Europe and Asia saw double-digit growth for both the three months and nine months ended July 31, 2006.

Revenue for three and nine months ending July 31, 2006 grew 15 percent and 9 percent from the same periods last year. Chemical analysis showed solid growth for the three and nine months ending July 31, 2006 compared to the same periods last year as we continue to see strong demand for our instruments in the areas of liquid and gas chromatography and gas chromatography/mass spectrometry platforms. Life sciences grew at approximately the same rate as our chemical analysis businesses during the three and nine months ended July 31, 2006 with microarrays, liquid and gas chromatography/mass spectrometry products contributing to our growth.

Looking forward, we anticipate growth in both orders and revenue, with strength across both our life sciences and chemical analysis businesses. We expect growth to be driven by recently released products such as rapid resolution liquid chromatography and enhanced single quadrupole liquid chromatography/mass spectrometry, triple quadrupole mass spectrometry, and quadrupole time-of-flight mass spectrometry systems.

Operating Results

	Three Months Ended		Nine Months Ended		Year over Year Change			
	July 31, 2006 (in millions, except for percentages)	2005	July 31, 2006	2005	Three Months	%	Nine Months	%
Gross margin	54	% 49	% 51	% 49	% 5	ppts	2	ppts
Operating margin	15	% 12	% 14	% 13	% 3	ppts	1	ppt
Research and development	\$ 37	\$ 35	\$ 109	\$ 103	6	%	6	%
Selling, general and administrative	\$ 113	\$ 91	\$ 319	\$ 279	24	%	14	%

For the three and nine months ended July 31, 2006, gross margin improved 5 percentage points and 2 percentage points respectively, compared to the same periods last year. The improvement in gross margin was driven by increased revenue, lower manufacturing overhead, and a decrease in general infrastructure costs.

Research and development expenses increased 6 percent for the three and nine months ended July 31, 2006, compared to the same periods last year. This increase is due to increased headcount from acquisitions, investment in molecular diagnostics and program spending to support upcoming product releases, and higher general infrastructure costs.

Selling, general and administrative expenses increased 24 percent and 14 percent compared to last year. This increase is due to higher employee-related costs, incremental headcount from acquisitions, product launch expenses to support new product releases, and higher general infrastructure costs.

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For the three and nine months ending July 31, 2006, operating margin increased 3 percentage points and 1 percentage point, respectively, compared to the same periods a year ago.

Discontinued Operations

On December 1, 2005, we completed the divestiture of our semiconductor products business. As of July 31, 2006, we have recorded a gain on the sale of \$1,809 million, net of taxes of \$8 million. During the nine months ended July 31, 2006, we adjusted the gain on sale of discontinued operations by \$22 million which includes \$20 million for working capital adjustments and \$2 million for the disposal of fixed assets. The book value of net assets disposed of was \$707 million. In accordance with SFAS No. 142, approximately \$98 million of goodwill associated with the semiconductor products business was eliminated and recorded as an adjustment to the gain on sale of discontinued operations. We incurred net disposition costs of \$35 million consisting of investment banking fees, legal fees, separation costs and employee related costs, net of a pension curtailment gain of \$51 million. The proceeds, net of transaction costs and taxes, from the divestiture are approximately \$2.5 billion.

The following table summarizes results from discontinued operations for the three and nine months ended July 31, 2006 and July 31, 2005 included in the condensed consolidated statement of operations:

	Three Months Ended		Nine Months Ended	
	July 31, 2006 (in millions)	2005	July 31, 2006 (in millions)	2005
Net revenue	\$	\$ 446	\$ 141	\$ 1,302
Costs, expenses and other income (expense), net		(390)	(133)	(1,140)
Income from discontinued operations	\$	\$ 56	\$ 8	\$ 162
Gain (loss) on sale of discontinued operations	(6)		1,817	
Income from and gain (loss) on sale of discontinued operations before taxes	(6)	56	1,825	\$ 162
Provision for income taxes		6	10	18
Income from and gain (loss) on sale of discontinued operations, net	\$ (6)	\$ 50	\$ 1,815	\$ 144

FINANCIAL CONDITION

Liquidity and Capital Resources

Our financial position as of July 31, 2006 consisted of cash and cash equivalents of \$2,249 million as compared to \$2,226 million as of October 31, 2005.

Net Cash Provided by Operating Activities

Net cash provided by operating activities of continuing operations was \$226 million for the nine months ended July 31, 2006 compared to \$291 million provided in the same period in 2005. Looking forward to the remainder of the year, we expect to generate sufficient cash from continuing operations to fund our operations and investments in property, plant and equipment.

We paid approximately \$143 million in taxes during the nine months ended July 31, 2006 as compared to \$28 million in the same period in 2005. The higher tax payments in 2006 were mostly associated with the U.S. tax liability created in 2005 for repatriation of earnings from our foreign subsidiaries of \$970 million under the American Jobs Creation Act of 2004, and with the 2005 federal alternate minimum tax.

We made higher disbursements for restructuring activities of \$136 million during the first nine months of 2006, primarily in the form of severance payments, compared to \$61 million during the same period of 2005. The restructuring payments were more than offset by proceeds from the real estate sales related to the consolidation of excess facilities as reported in the investing section below. We have also paid approximately \$180 million during the nine months ended July 31, 2006 under our variable pay programs, as compared to approximately \$100 million paid out during the same period of 2005.

During the nine months ended July 31, 2006, cash used in operating activities from accounts receivable was \$90 million as compared to cash generated of \$24 million in the same period in 2005. Agilent revenues increased by approximately 13 percent during the first nine months of 2006 as compared to the same period of 2005, resulting in comparatively higher accounts receivables. However, days sales outstanding decreased to 53 days as of July 31, 2006 from 55 days a year ago reflecting the continued improvement in receivables management. Accounts payable generated cash of \$89 million for the nine months ended July 31, 2006 versus cash used of \$26 million in the same period in 2005. Cash

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used for inventory was \$27 million for the nine months ended July 31, 2006 compared to cash generation of \$11 million in the same period in 2005. Inventory days on-hand improved to 96 days as of July 31, 2006 compared to 105 days as of the end of the same period last year.

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We contributed \$42 million to our U.S. defined benefit plan during the first nine months of 2006 and 2005, representing the full year's contribution. Our international defined benefit plans are generally funded ratably throughout the year. We contributed approximately \$72 million to our international plans for the nine months ended July 31, 2006 compared to approximately \$31 million for the same period in 2005. The higher contributions during the nine months ended July 31, 2006 were due to an additional \$31 million contribution to the Verigy pension plans as provided under the employee matters agreement. Total contributions in the nine months ended July 31, 2006 were approximately \$114 million, or 56 percent more than in the same period in 2005. Our annual contributions are highly dependent on the relative performance of our assets versus our projected liabilities, among other factors. We expect to contribute approximately \$8 million in the fourth quarter of 2006.

Net cash provided by operating activities from discontinued operations was \$7 million for the nine months ended July 31, 2006 as compared to \$189 million provided by operating activities from discontinued operations for the nine months ended July 31, 2005. We completed the sale of our discontinued operations on December 1, 2005.

Net Cash Provided by (Used in) Investing Activities

Net cash provided by investing activities of continuing operations for the nine months ended July 31, 2006 was \$1,868 million compared to \$117 million used in the same period in 2005.

In December 2005, we completed the divestiture of our semiconductor products division for \$2.5 billion net of transaction costs and taxes. In November 2005, we also completed the sale of our ownership in Lumileds to Philips for approximately \$949 million, plus repayment of approximately \$51 million of outstanding principal debt and accrued interest from Lumileds.

Restricted cash, cash equivalents and investments, net, increased by \$1,583 million in the nine months ended July 31, 2006 as compared to a \$20 million increase in the same period of 2005. In connection with the financing described under *Net Cash Provided by (Used in) Financing Activities* below, Agilent Technologies (Cayco) Limited, a wholly owned subsidiary of Agilent Technologies World Trade, Inc. (*World Trade*), which is in turn a wholly owned subsidiary of Agilent, is required to hold short-term investments. These short-term investments have been disclosed as restricted cash and cash equivalents on our condensed consolidated balance sheet.

Investments in property, plant and equipment were \$165 million, an increase of \$53 million from 2005 levels. We believe that total capital expenditures for the current year will be approximately \$200 million compared to last year's \$139 million. The projected increase in the capital expenditure is due to our site restructuring following the semiconductor products division divestiture and spin-off of our semiconductor test solutions business. Proceeds from sale of property, plant and equipment were \$205 million in the nine months ended July 31, 2006 as compared to \$45 million in 2005. During the first nine months of 2006, we sold our Palo Alto headquarters and San Jose site facility for a total consideration of approximately \$186 million. We also purchased minority interest in consolidated joint ventures for \$104 million during the first nine months of 2006 which included primarily the remaining minority interest of 49 percent in Yokogawa Analytical Systems for \$98 million. In addition, in the nine months ended July 31, 2006, we invested \$30 million in the acquisitions of businesses and intangible assets, net of cash acquired, compared to \$47 million for the period ended July 31, 2005. Proceeds from the sale of short-term investments were \$25 million for the period ended July 31, 2006.

Net cash used in investing activities of discontinued operations was \$6 million for the nine months ended July 31, 2006 as compared to cash used of \$5 million for the nine months ended July 31, 2005.

Net Cash Provided by (Used in) Financing Activities

Net cash used in financing activities for the nine months ended July 31, 2006 was \$2,086 million compared to \$112 million generated for the nine months ended July 31, 2005.

Agilent completed its \$4.466 billion stock repurchase program and acquired approximately 125 million shares of its common stock under this program. Proceeds from issuance of common stock under employee stock plans were \$513 million and \$115 million for the nine months ended July 31, 2006 and 2005, respectively. The increase in the proceeds was primarily due to the modifications to the terms of the options held by employees of our semiconductor products business to effect the acceleration of vesting for all unvested options as part of its divestiture and increase in Agilent stock price.

During the third quarter of 2006, Verigy, a wholly owned subsidiary of Agilent, completed the initial public offering (*IPO*) of 8.7 million of its ordinary shares at a price of \$15 per share. Net proceeds from issuance of common stock were \$121 million net of issuance costs.

In January 2006, World Trade entered into a Master Repurchase Agreement and related Confirmation (together, the *Repurchase Agreement*) with a counterparty pursuant to which World Trade sold to the counterparty 15,000 Class A preferred shares having an aggregate liquidation

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preference of \$1.5 billion of its wholly owned subsidiary, which has its own assets and liabilities, and received \$1.5 billion in cash. Pursuant to the Repurchase Agreement, World Trade is obligated to repurchase from the counterparty the preferred shares for 100 percent of their aggregate liquidation preference in January 2011. The \$1.5 billion obligation of World Trade to repurchase the preferred shares has been treated as long-term debt on our condensed consolidated balance sheet.

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Other

We have contractual commitments for non-cancelable operating leases. We have no other material non-cancelable guarantees or commitments.

Our liquidity is affected by many factors, some of which are based on normal ongoing operations of our business and some of which arise from fluctuations related to global economics and markets. Our cash balances are generated and held in many locations throughout the world. Local government regulations may restrict our ability to move cash balances to meet cash needs under certain circumstances. We do not currently expect such regulations and restrictions to impact our ability to pay vendors and conduct operations throughout our global organization.

On April 13, 2005, Standard & Poor's Rating Services (S&P) raised its corporate credit and senior unsecured debt ratings of Agilent to BB+ from BB , revising their rating outlook to stable from positive . On August 15, 2005, S&P raised its rating outlook on Agilent to positive , but left the company's corporate credit and senior unsecured debt ratings unchanged. In December, 2005, Moody's Investors Service (Moody's) affirmed their credit ratings of Agilent, leaving unchanged the senior implied debt rating of Ba2 and outlook rating of stable . In June 2006, Moody's also affirmed the speculative grade liquidity rating of SGL-1 .

Off Balance Sheet Arrangements

There were no substantial changes to our off-balance sheet arrangements or contractual commitments in the third quarter of fiscal year 2006.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to foreign currency exchange rate risks inherent in our sales commitments, anticipated sales, and assets and liabilities denominated in currencies other than the functional currency of our subsidiaries. We hedge future cash flows denominated in currencies other than the functional currency using sales forecasts up to twelve months in advance. Our exposure to exchange rate risks is managed on an enterprise-wide basis. This strategy utilizes derivative financial instruments, including option and forward contracts, to hedge certain foreign currency exposures, with the intent of offsetting gains and losses that occur on the underlying exposures with gains and losses on the derivative contracts hedging them. We do not currently and do not intend to utilize derivative financial instruments for trading purposes.

The company's operations generate non-functional currency cash flows such as revenues, third party vendor payments and inter-company payments. In anticipation of these foreign currency cash flows and in view of volatility of the currency market, the Company enters into such foreign exchange contracts as are described above to manage its currency risk. Approximately 64 percent and 66 percent of our revenues were generated in U.S. dollars during the third quarter of 2006 and 2005, respectively.

We performed a sensitivity analysis assuming a hypothetical 10 percent adverse movement in foreign exchange rates to the hedging contracts and the underlying exposures described above. As of July 31, 2006, the analysis indicated that these hypothetical market movements would not have a material effect on our consolidated financial position, results of operations or cash flows.

Item 4. CONTROLS AND PROCEDURES

Changes in Internal Control over Financial Reporting

During the third quarter of fiscal 2006, as part of the separation of Verigy into a stand-alone company, Verigy implemented an enterprise resource planning (ERP) system. Until the distribution of Agilent's ownership interest in Verigy, Verigy remains a majority-owned subsidiary of Agilent, with all results of operations and financial position being consolidated into Agilent's financial statements. As a result, implementation of a new ERP by Verigy is a material change in Agilent's internal control over financial reporting. Pre-implementation testing and post-implementation reviews were conducted by management to ensure that internal controls surrounding the system implementation process, the applications, and closing process were properly designed to prevent material financial statement errors. Operating effectiveness of related key controls will continue to be evaluated during the fourth quarter. There have been no other changes in our internal control over financial reporting during the third quarter of 2006 that have materially affected, or are likely to materially affect, our internal control over financial reporting.

Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures as required by Exchange Act Rule 13a-15(b) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures are effective.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In November 2001, a securities class action, *Kassin v. Agilent Technologies, Inc., et al.*, Civil Action No. 01-CV-10639, was filed in United States District Court for the Southern District of New York (the Southern District Court of New York) against certain investment bank underwriters for our initial public offering (IPO), Agilent and various of our officers and directors at the time of the IPO. On February 19, 2003, the Southern District Court of New York granted Agilent's motion to dismiss the claims against the Company based on Section 10 of the Securities Exchange Act of 1934, as amended, but denied Agilent's motion to dismiss the claims based on Section 11 of the Securities Act of 1933, as amended. Agilent and more than 200 other issuer defendants have reached an agreement in principle for a settlement with plaintiffs. Under the settlement, plaintiffs' claims against the Company and its directors and officers would be released, in exchange for a contingent payment and an assignment of certain potential claims. On June 14, 2004, papers formalizing the settlement among the plaintiffs, issuer defendants and insurers were presented to the Southern District Court of New York. On February 15, 2005, the Court granted preliminary approval of the settlement conditioned upon the parties' modification of a proposed bar order contained in the settlement. On August 31, 2005, the Court confirmed its preliminary approval of the settlement. On April 24, 2006, the Court held a fairness hearing in connection with the motion for final approval of the settlement. The Court did not issue a ruling on the motion for final approval at the fairness hearing. Plaintiffs continue to prosecute their claims against the underwriter defendants, and discovery is now underway.

The settlement is subject to a number of conditions, including approval of the proposed settling parties and the court. Under our separation agreements with Hewlett-Packard, Hewlett-Packard agreed to indemnify us for a substantial portion of IPO-related liabilities. If the settlement does not occur, and the litigation against the company continues, Agilent believes it has meritorious defenses and intends to defend the case vigorously. In light of the proposed settlement, we do not expect this case to be material.

We are involved in lawsuits, claims, investigations and proceedings, including, but not limited to, patent, commercial and environmental matters, which arise in the ordinary course of business. Other than the matter described above, there are no matters pending that we expect to be material in relation to our business, consolidated financial condition, results of operations or cash flows.

ITEM IA. RISK FACTORS

Risks, Uncertainties and Other Factors That May Affect Future Results

Our operating results and financial condition could be harmed if the markets into which we sell our products decline or do not grow as anticipated.

Visibility into our markets is limited. Our quarterly sales and operating results are highly dependent on the volume and timing of orders received during the quarter, which are difficult to forecast. In addition, our revenues and earnings forecasts for future quarters are often based on the expected seasonality or cyclicity of our markets. However, the markets we serve do not always experience the seasonality or cyclicity that we expect. Any decline in our customers' markets or in general economic conditions would likely result in a reduction in demand for our products and services. For example, if the Asia Pacific market does not grow as anticipated, our results could suffer. In addition, we have not yet completed our proposed spin-off of Verigy, which is directly influenced by changes in the semiconductor market. Since the broader semiconductor market is one of the drivers for our electronic measurement business, a continued decrease in the semiconductor market could harm our electronic measurement business. Also, if our customers' markets decline, we may not be able to collect on outstanding amounts due to us. Such decline could harm our consolidated financial position, results of operations, cash flows and stock price, and could limit our ability to sustain profitability. Also, in such an environment, pricing pressures could intensify. Since a significant portion of our operating expenses is relatively fixed in nature due to sales, research and development and manufacturing costs, if we were unable to respond quickly enough these pricing pressures could further reduce our gross margins. Finally, we may be required to secure additional debt or equity financing at some time in the future, and we cannot assure you that such financing will be available on acceptable terms when required. If our corporate credit rating is downgraded, we could be required to pay a higher interest rate for future borrowing needs and we may have stricter terms.

The actions we are taking to focus our organization on our core businesses may cause disruption and increase expenses, which may affect our results of operations or financial condition.

The planned spin-off of Verigy, the recently completed divestiture of our semiconductor products business and our infrastructure costs reduction program, even after these efforts are completed, could involve a number of risks, including:

- the diversion of the attention of management and other key personnel
- the loss of talent; and
- restructuring, inventory and other charges which may affect our results of operations.

There can be no assurance that the sale of the semiconductor products business, which we completed on December 1, 2005, or the spin-off of Verigy will cause us to achieve our goal of successfully focusing on our core businesses. Also, there can there be no

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assurance that this strategic realignment will be beneficial to our Company or its financial condition.

In addition, we may fail to properly implement the spin-off or complete it on our intended timeline, which might adversely affect our financial condition and results of operations. Our decision to divest the semiconductor products business and to spin-off Verigy may result in the recording of special charges, such as inventory, goodwill and intangible-asset impairments, workforce reduction costs, pension and stock option costs, charges relating to consolidation of excess facilities, or claims from third parties who were resellers or users of discontinued products.

Our historical consolidated financial results may not necessarily reflect our future financial position, results of operations or cash flows. In addition, as a result of a spin-off or divestiture, our stock price may fluctuate. Prior to its divestiture, the semiconductor products business was a significant portion of our consolidated business. But its financial results are no longer included in our consolidated financial results on a continuing operations basis. We will not report the financial results of our semiconductor test solutions business, including net revenues and net income, after the expected distribution of all of Agilent's shares in Verigy. The result of omitting the semiconductor products business from our continuing operations has caused our net revenues to decline, and the result of omitting Verigy from our consolidated financial statements could cause our revenues and net operating income to decline.

We have retained contingent liabilities from the divestiture of our semiconductor products business, including designated tax and environmental liabilities. The resolution of these contingencies may have a material adverse effect on our continuing results of operations or financial condition.

We may not be successful in our efforts to maintain a reduced cost structure, and the actions that we take in order to reduce costs could have long-term adverse effects on our business.

We have taken, and continue to take, various actions to transition our company to a reduced cost structure. For example, in fiscal year 2005, we announced the restructuring of our global infrastructure organization to reduce costs by \$450 million.

There are several risks inherent in our efforts to maintain a reduced cost structure. These include the risks that we will not be able to reduce expenditures quickly enough and hold them at a level necessary to sustain or increase profitability and that we may have to undertake further restructuring initiatives that would entail additional charges. For example, our expenses were higher than anticipated during the second quarter of 2004, due to increases in demand for items like travel, training, consultants, manufacturing and operating supplies, which adversely affected our performance. If our current plan to reduce costs leads to similar increases in demand we could face the same situation in the future. As we transform our infrastructure, we expect to face ongoing pressure to control expenses. If we are not able to hold down expenses we may have to further reduce our workforce. There is also the risk that cost-cutting initiatives will impair our ability to effectively develop and market products, to remain competitive in the industries in which we compete and to operate effectively. Each of the above measures could have long-term effects on our business by reducing our pool of talent, decreasing or slowing improvements in our products, making it more difficult for us to respond to customers, limiting our ability to increase production quickly if and when the demand for our products increases and limiting our ability to hire and retain key personnel. These circumstances could cause our income to be lower than it otherwise might be, which would adversely affect our stock price.

If we do not introduce successful new products and services in a timely manner, our products and services will become obsolete, and our operating results will suffer.

We generally sell our products in industries that are characterized by rapid technological changes, frequent new product and service introductions and changing industry standards. In addition, many of the markets in which we operate are seasonal and cyclical. Without the timely introduction of new products, services and enhancements, our products and services will become technologically obsolete over time, in which case our revenue and operating results would suffer. The success of our new products and services will depend on several factors, including our ability to:

- properly identify customer needs;
- innovate and develop new technologies, services and applications;
- successfully commercialize new technologies in a timely manner;
- manufacture and deliver our products in sufficient volumes on time;
- differentiate our offerings from our competitors' offerings;

- price our products competitively;
- anticipate our competitors' development of new products, services or technological innovations; and
- control product quality in our manufacturing process.

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Dependence on contract manufacturing and outsourcing other portions of our supply chain may adversely affect our ability to bring products to market and damage our reputation. Dependence on outsourced information technology and other administrative functions may impair our ability to operate effectively.

As part of our efforts to streamline operations and to cut costs, we have been outsourcing aspects of our manufacturing processes and other functions and will continue to evaluate additional outsourcing. If our contract manufacturers or other outsourcers fail to perform their obligations in a timely manner or at satisfactory quality levels, our ability to bring products to market and our reputation could suffer. For example, during a market upturn, our contract manufacturers may be unable to meet our demand requirements, which may preclude us from fulfilling our customers' orders on a timely basis. The ability of these manufacturers to perform is largely outside of our control. In addition, we outsourced significant portions of our information technology (IT) function and other administrative functions. Since IT is critical to our operations, any failure to perform on the part of the IT providers could impair our ability to operate effectively. In addition to the risks outlined above, problems with manufacturing or IT outsourcing could result in lower revenues, unexecuted efficiencies, impact our results of operations and our stock price. Much of our outsourcing takes place in developing countries and, as a result, may be subject to geopolitical uncertainty.

Failure to adjust our purchases due to changing market conditions or failure to estimate our customers' demand could adversely affect our income.

Our income could be harmed if we are unable to adjust our purchases to market fluctuations, including those caused by the seasonal or cyclical nature of the markets in which we operate. The sale of our products and services are dependent, to a large degree, on customers whose industries are subject to seasonal or cyclical trends in the demand for their products. For example, the consumer electronics market is particularly volatile, making demand difficult to anticipate. During a market upturn, we may not be able to purchase sufficient supplies or components to meet increasing product demand, which could materially affect our results. In addition, some of the parts that require custom design are not readily available from alternate suppliers due to their unique design or the length of time necessary for design work. Should a supplier cease manufacturing such a component, we would be forced to reengineer our product. In addition to discontinuing parts, suppliers may also extend lead times, limit supplies or increase prices due to capacity constraints or other factors. In order to secure components for the production of products, we may continue to enter into non-cancelable purchase commitments with vendors, or at times make advance payments to suppliers, which could impact our ability to adjust our inventory to declining market demands. Prior commitments of this type have resulted in an excess of parts when demand for our communications, semiconductor and electronics products has decreased. If demand for our products is less than we expect, we may experience additional excess and obsolete inventories and be forced to incur additional charges.

Our income may suffer if our manufacturing capacity does not match our demand.

Because we cannot immediately adapt our production capacity and related cost structures to rapidly changing market conditions, when demand does not meet our expectations, our manufacturing capacity will likely exceed our production requirements. If, during a general market upturn or an upturn in one of our segments, we cannot increase our manufacturing capacity to meet product demand, we will not be able to fulfill orders in a timely manner. This inability could materially and adversely limit our ability to improve our results. By contrast, if during an economic downturn we had excess manufacturing capacity, then our fixed costs associated with excess manufacturing capacity would adversely affect our income.

Economic, political and other risks associated with international sales and operations could adversely affect our results of operations.

Because we sell our products worldwide, our business is subject to risks associated with doing business internationally. We anticipate that revenue from international operations will continue to represent a majority of our total revenue. In addition, many of our employees, contract manufacturers, suppliers, job functions and manufacturing facilities are increasingly located outside the U.S. Accordingly, our future results could be harmed by a variety of factors, including:

- interruption to transportation flows for delivery of parts to us and finished goods to our customers;
- changes in foreign currency exchange rates;
- changes in a specific country's or region's political, economic or other conditions;
- trade protection measures and import or export licensing requirements;
- negative consequences from changes in tax laws;

- difficulty in staffing and managing widespread operations;
- differing labor regulations;

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- differing protection of intellectual property;
- unexpected changes in regulatory requirements; and
- geopolitical turmoil, including terrorism and war.

We centralized most of our accounting processes to two locations: India and Malaysia. These processes include general accounting, cost accounting, accounts payable and accounts receivables functions. If conditions change in those countries, it may adversely affect operations, including impairing our ability to pay our suppliers and collect our receivables. Our results of operations, as well as our liquidity, may be adversely affected and possible delays may occur in reporting financial results.

Our business will suffer if we are not able to retain and hire key personnel.

Our future success depends partly on the continued service of our key research, engineering, sales, marketing, manufacturing, executive and administrative personnel. If we fail to retain and hire a sufficient number of these personnel, we will not be able to maintain or expand our business. The markets in which we operate are very dynamic, and our businesses continue to respond with reorganizations, workforce reductions and site closures. We believe our pay levels are very competitive within the regions that we operate. However, there is also intense competition for certain highly technical specialties in geographic areas where we continue to recruit, and it may become more difficult to retain our key employees.

Our acquisitions, strategic alliances, joint ventures and divestitures may result in financial results that are different than expected.

In the normal course of business, we frequently engage in discussions with third parties relating to possible acquisitions, strategic alliances, joint ventures and divestitures, and generally expect to complete several transactions per year. For example, we recently completed the divestiture of our semiconductor products business and intend to spin off Verigy by the end of 2006. As a result of such transactions, our financial results may differ from our own or the investment community's expectations in a given quarter, or over the long term. Such transactions often have post-closing arrangements including but not limited to post-closing adjustments, transition services, escrows or indemnifications, the financial results of which can be difficult to predict, or accurately accrue for. In addition, acquisitions and strategic alliances may require us to integrate a different company culture, management team and business infrastructure. We may have difficulty developing, manufacturing and marketing the products of a newly acquired company in a way that enhances the performance of our combined businesses or product lines to realize the value from expected synergies. Depending on the size and complexity of an acquisition, our successful integration of the entity depends on a variety of factors, including:

- the retention of key employees;
- the management of facilities and employees in different geographic areas;
- the retention of key customers;
- the compatibility of our sales programs and facilities within those of the acquired company; and
- the compatibility of our existing infrastructure with that of an acquired company.

A successful divestiture depends on various factors, including our ability to:

- effectively transfer liabilities, contracts, facilities and employees to the purchaser;
- identify and separate the intellectual property to be divested from the intellectual property that we wish to keep; and
- reduce fixed costs previously associated with the divested assets or business.

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Future impairment of the value of purchased assets and goodwill could have a significant negative impact on our future operating results. And, our inability to timely and effectively apply our systems of internal controls to an acquired business could harm our operating results or cause us to fail to meet our financial reporting obligations.

In addition, if customers of the divested business do not receive the same level of service from the new owners, this may adversely affect our other businesses to the extent that these customers also purchase other Agilent products. All of these efforts require varying levels of management resources, which may divert our attention from other business operations. Further, if market

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conditions or other factors lead us to change our strategic direction, we may not realize the expected value from such transactions. If we do not realize the expected benefits or synergies of such transactions, our consolidated financial position, results of operations, cash flows and stock price could be negatively impacted.

Environmental contamination from past operations could subject us to unreimbursed costs and could harm on-site operations and the future use and value of the properties involved and environmental contamination caused by ongoing operations could subject us to substantial liabilities in the future.

Some of our properties are undergoing remediation by Hewlett-Packard (HP) for subsurface contaminations that were known at the time of our separation from HP. HP has agreed to retain the liability for this subsurface contamination, perform the required remediation and indemnify us with respect to claims arising out of that contamination. The determination of the existence and cost of any additional contamination caused by us could involve costly and time-consuming negotiations and litigation. In addition, HP will have access to our properties to perform remediation. While HP has agreed to minimize interference with on-site operations at those properties, remediation activities and subsurface contamination may require us to incur unreimbursed costs and could harm on-site operations and the future use and value of the properties. We cannot be sure that HP will continue to fulfill its indemnification or remediation obligations.

We have agreed to indemnify HP for any liability associated with contamination from past operations at all other properties transferred from HP to us other than those properties currently undergoing remediation by HP. While we are not aware of any material liabilities associated with any potential subsurface contamination at any of those properties, subsurface contamination may exist, and we may be exposed to material liability as a result of the existence of that contamination.

Our semiconductor and other manufacturing processes involve the use of substances regulated under various international, federal, state and local laws governing the environment. We may still be subject to liabilities for environmental contamination, and these liabilities may be substantial. Although our policy is to apply strict standards for environmental protection at our sites inside and outside the U.S., even if the sites outside the U.S. are not subject to regulations imposed by foreign governments, we may not be aware of all conditions that could subject us to liability.

Our customers and we are subject to various governmental regulations, compliance with which may cause us to incur significant expenses, and if we fail to maintain satisfactory compliance with certain regulations, we may be forced to recall products and cease their manufacture and distribution, and we could be subject to civil or criminal penalties.

Our businesses are subject to various significant international, federal, state and local regulations, including but not limited to health and safety, packaging, product content, labor and import/export regulations. These regulations are complex, change frequently and have tended to become more stringent over time. We may be required to incur significant expenses to comply with these regulations or to remedy violations of these regulations. Any failure by us to comply with applicable government regulations could also result in cessation of our operations or portions of our operations, product recalls or impositions of fines and restrictions on our ability to carry on or expand our operations. In addition, because many of our products are regulated or sold into regulated industries, we must comply with additional regulations in marketing our products.

Our products and operations are also often subject to the rules of industrial standards bodies, like the International Standards Organization, as well as regulation by other agencies such as the U.S. Federal Communications Commission. We also must comply with work safety rules. If we fail to adequately address any of these regulations, our businesses could be harmed.

Some of our chemical analysis products are used in conjunction with chemicals whose manufacture, processing, distribution and notification requirements are regulated by the U.S. Environmental Protection Agency under the Toxic Substances Control Act, and by regulatory bodies in other countries with laws similar to the Toxic Substances Control Act. We must conform the manufacture, processing, distribution of and notification about these chemicals to these laws and adapt to regulatory requirements in all countries as these requirements change. If we fail to comply with these requirements in the manufacture or distribution of our products, then we could be made to pay civil penalties, face criminal prosecution and, in some cases, be prohibited from distributing our products in commerce until the products or component substances are brought into compliance.

We are subject to laws and regulations governing government contracts, and failure to address these laws and regulations or comply with government contracts could harm our business by leading to a reduction in revenue associated with these customers.

We have agreements relating to the sale of our products to government entities and, as a result, we are subject to various statutes and regulations that apply to companies doing business with the government. The laws governing government contracts differ from the laws governing private contracts. For example, many government contracts contain pricing terms and conditions that are not applicable to private contracts. We are also subject to investigation for compliance with the regulations governing government contracts. A failure to comply with these regulations might

result in suspension of these contracts, or administrative penalties.

Third parties may claim that we are infringing their intellectual property, and we could suffer significant litigation or licensing expenses or be prevented from selling products.

While we do not believe that any of our products infringe the valid intellectual property rights of third parties, we may be unaware of intellectual property rights of others that may cover some of our technology, products or services. Any litigation

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regarding patents or other intellectual property could be costly and time-consuming and could divert our management and key personnel from our business operations. The complexity of the technology involved and the uncertainty of intellectual property litigation increase these risks. Claims of intellectual property infringement might also require us to enter into costly license agreements, and we may not be able to obtain license agreements on terms acceptable to us, or at all. We also may be subject to significant damages or injunctions against development and sale of certain of our products.

We often rely on licenses of intellectual property useful for our businesses. We cannot ensure that these licenses will be available in the future on favorable terms or at all. Our intellectual property portfolio, which we use in negotiating licenses and asserting counterclaims, has changed as a result of our divestitures and the Verigy spin-off. Portions of that portfolio relevant to the buyer of our semiconductor products business or to Verigy are no longer available for our use except for a very limited ability to sublicense the divested and spunoff intellectual property. Accordingly, the amount of intellectual property that we may use in our defense or for negotiations has decreased. We may be unable to obtain agreements on terms as favorable as we may have been able to obtain if we could have included in our defense or negotiations the divested and spunoff intellectual property.

Third parties may infringe our intellectual property, and we may expend significant resources enforcing our rights or suffer competitive injury.

Our success depends in large part on our proprietary technology. We rely on a combination of patents, copyrights, trademarks, trade secrets, confidentiality provisions and licensing arrangements to establish and protect our proprietary rights. If we fail to successfully enforce our intellectual property rights, our competitive position could suffer, which could harm our operating results.

Our pending patent and trademark registration applications may not be allowed, or competitors may challenge the validity or scope of our patents, copyrights or trademarks. In addition, our patents may not provide us a significant competitive advantage.

We may be required to spend significant resources to monitor and police our intellectual property rights. We may not be able to detect infringement and our competitive position may be harmed before we do so. In addition, competitors may design around our intellectual property rights or develop competing technologies. Intellectual property rights and our ability to enforce them may also be unavailable or limited in some foreign countries, which could make it easier for competitors to capture market share and result in lost revenues. Furthermore, some intellectual property rights are licensed to other companies, allowing them to compete with us using that intellectual property.

If we suffer loss to our factories, facilities or distribution system due to catastrophe, our operations could be seriously harmed.

Our factories, facilities and distribution system are subject to catastrophic loss due to fire, flood, terrorism or other natural or man-made disasters. In particular, several of our facilities could be subject to a catastrophic loss caused by earthquake due to their locations. Our production facilities, headquarters and Agilent Technologies Laboratories in California, and our production facilities in Washington and Japan, are all located in areas with above average seismic activity. If any of these facilities were to experience a catastrophic loss, it could disrupt our operations, delay production, shipments and revenue and result in large expenses to repair or replace the facility. In addition, since we have recently consolidated our manufacturing facilities, we are more likely to experience an interruption to our operations in the event of a catastrophe in any one location. Although we carry insurance for property damage and business interruption, we do not carry insurance or financial reserves for interruptions or potential losses arising from earthquakes or terrorism.

Future changes in financial accounting standards may adversely affect our reported results of operations.

A change in accounting standards can have a significant effect on our reported results. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and may occur in the future. These new accounting pronouncements may adversely affect our reported financial results.

For example, under Statement of Financial Accounting Standards No. 123 (R), Share Based Payment (SFAS No. 123 (R)), we are now required to account for our stock-based awards as a compensation expense and our net income and net income per share have been reduced. Previously, we recorded compensation expense only in connection with option grants that had an exercise price below fair market value. For option grants that had an exercise price at fair market value, we calculated compensation expense and disclosed their impact on net income (loss) and net income (loss) per share, as well as the impact of all stock-based compensation expense in a footnote to the consolidated financial statements. SFAS No. 123 (R) required us to adopt the new accounting provisions beginning in our first quarter of 2006, and requires us to expense stock-based awards, including shares issued under our employee stock purchase plan, stock options, restricted stock and stock appreciation rights, as compensation cost.

If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial results or prevent fraud, which could harm our brands and operating results.

Effective internal controls are necessary for us to provide reliable and accurate financial reports and effectively prevent fraud.

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We have devoted significant resources and time to comply with the internal control over financial reporting requirements of the Sarbanes-Oxley Act of 2002. In addition, Section 404 under the Sarbanes-Oxley Act of 2002 requires that we assess and our auditors attest to the design and operating effectiveness of our controls over financial reporting. Our compliance with the annual internal control report requirement for each fiscal year will depend on the effectiveness of our financial reporting and data systems and controls across our operating subsidiaries. Furthermore, an important part of our growth strategy has been, and will likely continue to be, the acquisition of complementary businesses, and we expect these systems and controls to become increasingly complex to the extent that we integrate acquisitions and our business grows. Likewise, the complexity of our systems and controls may become more difficult to manage as we transform our operating structure and continue to reduce infrastructure costs. To effectively manage these changes, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. We cannot be certain that these measures will ensure that we design, implement and maintain adequate controls over our financial processes and reporting in the future, especially in light of likely future acquisitions of companies that are not in compliance with Section 404 of Sarbanes-Oxley Act of 2002. Any failure to implement required new or improved controls, difficulties encountered in their implementation or operation, or difficulties in the assimilation of acquired businesses into our control system could harm our operating results or cause it to fail to meet our financial reporting obligations. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our stock and our access to capital.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

ISSUER PURCHASES OF EQUITY SECURITIES

The table below summarizes information about the Company's purchases of its equity securities registered pursuant to Section 12 of the Exchange Act during the nine month period ended July 31, 2006.

Period	Total Number of Shares of Common Stock Purchased (1)	Weighted Average Price Paid per Share of Common Stock (2)	Total Number of Shares of Common Stock Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Approximate Dollar Value of Shares of Common Stock that May Yet Be Purchased Under the Plans or Programs (in millions)
	(a)	(b)	(c)	(d)
Nov. 1, 2005 through Nov. 30, 2005				\$ 4,176
Dec. 1, 2005 through Dec. 31, 2005	83,077,043	(1) \$ 36.00	(2) 83,077,043(1)	\$ 1,185
Jan. 1, 2006 through Jan. 31, 2006				\$ 1,185
Feb. 1, 2006 through Feb. 28, 2006	1,576,000	\$ 35.32	1,576,000	\$ 1,129
Mar. 1, 2006 through Mar. 31, 2006	5,671,100	\$ 36.89	5,671,100	\$ 920
Apr. 1, 2006 through Apr. 30, 2006	5,797,858	\$ 37.82	5,797,858	\$ 701
May 1, 2006 through May 31, 2006	8,979,900	\$ 36.55	8,979,900	\$ 372
Jun. 1, 2006 through Jun. 30, 2006	11,057,164	\$ 33.66	11,057,164	\$ 0
Jul. 1, 2006 through Jul. 31, 2006				\$ 0
Total	116,159,065	\$ 35.94	116,159,065	\$ 0

(1) On August 15, 2005, the Company announced its intention to repurchase \$4.0 billion of its common stock through any one or a combination of a variety of methods, including open-market purchases, block trades, self tenders, accelerated share repurchase transactions or otherwise. Subsequently, on September 22, 2005, the Company announced its intention to increase the size of its previously announced repurchase program to \$4.466 billion of its common stock. During the quarterly period ended January 31, 2006, the Company purchased a total of 83,077,043 shares of its common stock in an issuer self-tender.

(2) The weighted average price paid per shares of common stock does not include cost of commissions.

ITEM 6. EXHIBITS

(a) Exhibits:

A list of exhibits is set forth in the Exhibit Index found on page 41 of this report.

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AGILENT TECHNOLOGIES, INC.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: September 6, 2006

By: /s/ Adrian T. Dillon
Adrian T. Dillon
Executive Vice President,
Finance and Administration, Chief Financial Officer

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AGILENT TECHNOLOGIES INC.

EXHIBIT INDEX

Exhibit Number	Description
1.	Not applicable.
2.1	Master Separation and Distribution Agreement between Hewlett-Packard and the Company effective as of August 12, 1999. Incorporated by reference from Exhibit 2.1 of the Company's Registration Statement on Form S-1, Registration No. 333-85249 (S-1).
2.2	General Assignment and Assumption Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.2 of the Company's S-1.
2.3	Master Technology Ownership and License Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.3 of the Company's S-1.
2.4	Master Patent Ownership and License Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.4 of the Company's S-1.
2.5	Master Trademark Ownership and License Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.5 of the Company's S-1.
2.6	ICBD Technology Ownership and License Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.6 of the Company's S-1.
2.7	Employee Matters Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.7 of the Company's S-1.
2.8	Tax Sharing Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.8 of the Company's S-1.
2.9	Master IT Service Level Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.9 of the Company's S-1.
2.10	Real Estate Matters Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.10 of the Company's S-1.
2.11	Environmental Matters Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.11 of the Company's S-1.
2.12	Master Confidential Disclosure Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.12 of the Company's S-1.
2.13	Indemnification and Insurance Matters Agreement between Hewlett-Packard and the Company. Incorporated by reference from Exhibit 2.13 of the Company's S-1.
2.14	Non U.S. Plan. Incorporated by reference from Exhibit 2.14 of the Company's S-1.
2.15	Agreement and Plan of Merger, dated as of November 24, 2000, by and among Agilent Technologies, Inc., Tahoe Acquisition Corp. and Objective Systems Integrators, Inc. Incorporated by reference from Exhibit 99.1(A) of the Schedule 13D filed by Agilent Technologies, Inc. on December 4, 2000.
2.16	Tender and Voting Agreement, dated as of November 24, 2000, by and among Agilent Technologies, Inc., Tahoe Acquisition Corp. and Objective Systems Integrators, Inc. Incorporated by reference from Exhibit 99.1(B) of the Schedule 13D filed by Agilent Technologies, Inc. on December 4, 2000.

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- 2.17 Asset Purchase Agreement between the Company and Philips dated as of November 17, 2000. Incorporated by reference from Exhibit 2.17 of the Company s 10-Q filed on March 19, 2001.
- 2.18 Amendment and Supplemental Agreement dated as of August 1, 2001 between Agilent Technologies, Inc. and Koninklijke Philips Electronics N.V. Incorporated by reference from Exhibit 2.2 of the Company s 8-K filed August 15, 2001.
- 2.19 Master Service Level Agreement dated as of August 1, 2001 between Agilent Technologies, Inc. and Koninklijke Philips Electronics N.V. Incorporated by reference from Exhibit 2.3 of the Company s 8-K filed August 15, 2001.
- 2.20 Asset Purchase Agreement, dated as of August 14, 2005, by and between Agilent Technologies, Inc. and Argos Acquisition Pte. Ltd. Incorporated by reference from Exhibit 2.1 of the Company s 8-K filed August 15, 2005.
- 2.21 Share Purchase Agreement, dated as of August 12, 2005, by and among Agilent Technologies, Inc. and Agilent LED International, Philips Lumileds Holding B.V. and Koninklijke Philips Electronics N.V. Incorporated by reference from Exhibit 2.2 of the Company s 8-K filed August 15, 2005.
- 3.1 Amended and Restated Certificate of Incorporation. Incorporated by reference from Exhibit 3.1 of the Company s S-1.
- 3.2 Amended and Restated Bylaws. Incorporated by reference from Exhibit 4.2 of the Company s S-3/A filed April 10, 2002.
- 4.1 Preferred Stock Rights Agreement between the Company and Harris Trust and Savings Bank dated as of May 12, 2000. Incorporated by reference from Exhibit 1 of the Company s 8-A, filed on May 17, 2000.
- 4.2 Registration Rights Agreement between the Company and Credit Suisse First Boston Corporation, J.P. Morgan Securities, Inc. and Salomon Smith Barney, Inc, dated November 27, 2001. Incorporated by reference from Exhibit 99.3 of the Company s 8-K filed on November 27, 2001.
- 5-8. Not applicable.
- 9. None.
- 10.1 Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.2 of the Company s S-1.*
- 10.2 Agilent Technologies, Inc. 1999 Stock Plan (restatement, effective September 17, 2001). Incorporated by reference from Exhibit 10.13 of the Company s 10-K/A filed on February 1, 2002.*
- 10.3 Agilent Technologies, Inc. 1999 Stock Plan (Amended and Restated Effective May 21, 2002). Incorporated by reference from the Company s S-8 filed May 23, 2002.*
- 10.4 Agilent Technologies, Inc. 1999 Stock Plan, as amended and restated, and Amendment No. 1 thereto dated March 5, 2003. Incorporated by reference from Exhibit (d)(1) of the Company s Schedule TO filed on May 20, 2003.*
- 10.5 Amendment No. 2 to Agilent Technologies, Inc. 1999 Stock Plan dated May 20, 2003. Incorporated by reference from Exhibit 10.18 of the Company s 10-Q filed June 4, 2003.*
- 10.6 Agilent Technologies, Inc. 1999 Stock Plan (Amendment and Restatement, Effective November 18, 2003). Incorporated by reference from Exhibit 10.19 of the Company s 10-Q filed March 4, 2004.*
- 10.7 Agilent Technologies, Inc. 1999 Stock Plan (Amendment and Restatement, effective July 19, 2005). Incorporated by reference from Exhibit 10.54 of Company s 10-Q filed September 7, 2005.*
- 10.8 Form of Award Agreement (U.S.) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.1 of the Company s 8-K filed November 12, 2004.*
- 10.9 Form of Award Agreement (Non-U.S.) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.2 of the Company s 8-K filed November 12, 2004.*

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- 10.10 Form of Award Agreement (Belgium) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.29 of the Company s 10-K filed December 21, 2004.*
- 10.11 Form of Award Agreement (Brazil) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.30 of the Company s 10-K filed December 21, 2004.*
- 10.12 Form of Award Agreement (China) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.29 of the Company s 10-K filed December 21, 2004. Incorporated by reference from Exhibit 10.31 of the Company s 10-K filed December 21, 2004.*
- 10.13 Form of Award Agreement (France) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.32 of the Company s 10-K filed December 21, 2004.*
- 10.14 Form of Award Agreement (Germany) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.33 of the Company s 10-K filed December 21, 2004.*
- 10.15 Form of Award Agreement (India) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.34 of the Company s 10-K filed December 21, 2004.*
- 10.16 Form of Award Agreement (Italy) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.35 of the Company s 10-K filed December 21, 2004.*
- 10.17 Form of Award Agreement (Japan) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.36 of the Company s 10-K filed December 21, 2004.*
- 10.18 Form of Award Agreement (SAR) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.37 of the Company s 10-K filed December 21, 2004.*
- 10.19 Form of Award Agreement (Switzerland) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.38 of the Company s 10-K filed December 21, 2004.*
- 10.20 Form of Award Agreement (restricted stock) for grants under the Agilent Technologies, Inc. 1999 Stock Plan. Incorporated by reference from Exhibit 10.39 of the Company s 10-K filed December 21, 2004.*
- 10.21 Agilent Technologies, Inc. Employee Stock Purchase Plan. Incorporated by reference from Exhibit 4.1 of the Company s Form S-8 filed September 29, 2000.*
- 10.22 Agilent Technologies, Inc. Employee Stock Purchase Plan (Amended and Restated, Effective November 1, 2004). Incorporated by reference from Exhibit 10.23 of the Company s 10-Q filed September 2, 2004.*
- 10.23 Agilent Technologies, Inc. Employee Stock Purchase Plan (Amended and Restated, effective November 1, 2005). Incorporated by reference from Exhibit 10.55 of Company s 10-Q filed September 7, 2005.*
- 10.24 1999 Non-Employee Director Stock Plan. Incorporated by reference from Exhibit 10.3 of the Company s S-1.*
- 10.25 1999 Non-Employee Director Stock Plan (Amended and Restated Effective January 20, 2004). Incorporated by reference from Exhibit 10.19 of the Company s 10-Q filed June 3, 2004.*
- 10.26 Agilent Technologies, Inc. 1999 Non-Employee Director Stock Plan (Amended and Restated, Effective July 20, 2004). Incorporated by reference from Exhibit 10.24 of the Company s 10-Q filed September 2, 2004.*
- 10.27 Form of Stock Option Agreement for grants under the Agilent Technologies, Inc. 1999 Non-Employee Director Stock Plan. Incorporated by reference from Exhibit 10.3 of the Company s 8-K filed November 12, 2004.*
- 10.28 Agilent Technologies, Inc. Excess Benefit Retirement Plan. Incorporated by reference from Exhibit 10.7 of the Company s Form 10-K filed January 22, 2002. Amendment to the Agilent Technologies, Inc. Excess Benefit Retirement Plan adopted effective May 1, 2000.*

10.29 Agilent Technologies, Inc. Long-Term Performance Program Description for Section 16 Officers, effective

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- November 1, 2003. Incorporated by reference from Exhibit 10.18 of the Company's 10-Q filed March 4, 2004.*
- 10.30 Agilent Technologies, Inc. Deferred Compensation Plan for Non-Employee Directors (Effective as of March 1, 2004). Incorporated by reference from Exhibit 10.21 of the Company's 10-Q filed June 3, 2004.*
- 10.31 Agilent Technologies, Inc. 2005 Deferred Compensation Plan for Non-Employee Directors. Incorporated by reference from Exhibit 10.2 of the Company's 8-K filed November 19, 2004.*
- 10.32 Agilent Technologies, Inc. Deferred Compensation Plan (Amended and Restated as of March 1, 2004). Incorporated by reference from Exhibit 10.22 of the Company's 10-Q filed June 3, 2004.*
- 10.33 Agilent Technologies, Inc. 2005 Deferred Compensation Plan. Incorporated by reference from Exhibit 10.1 of the Company's 8-K filed November 19, 2004.*
- 10.34 Form of Indemnification Agreement entered into by the Company with each of its directors and board-appointed officers. Incorporated by reference from Exhibit 10.5 of the Company's S-1.*
- 10.35 Offer letter from the Company to Adrian T. Dillon as incoming Executive Vice President and Chief Financial Officer, dated November 6, 2001. Incorporated by reference from Exhibit 10.15 of the Company's 10-Q filed on March 6, 2002.
- 10.36 Form of Change of Control Severance Agreement entered into by the Company with Dick M. Chang, Adrian T. Dillon, Jean M. Halloran, D. Craig Nordlund, Jack P. Trautman, Chris van Ingen and Thomas E. White. Incorporated by reference from Exhibit 10.15 of the Company's 10-Q filed March 12, 2003.*
- 10.37 Form of Amendment #1 to Change of Control Severance Agreement dated April 2, 2004, entered into by the Company with Adrian T. Dillon, Jean M. Halloran, D. Craig Nordlund, Jack P. Trautman, Chris van Ingen and Thomas E. White. Incorporated by reference from Exhibit 10.20 of the Company's 10-Q filed June 3, 2004.*
- 10.38 Amended and Restated Change of Control Severance Agreement entered into by the Company with Edward W. Barnholt. Incorporated by reference from Exhibit 10.2 of the Company's 8-K filed March 21, 2005.*
- 10.39 Change of Control Severance Agreement between Agilent Technologies, Inc. and Patrick J. Byrne. Incorporated by reference from Exhibit 10.1 of the Company's 8-K filed February 4, 2005.*
- 10.40 Agilent Technologies, Inc. Indemnification Agreement between Agilent Technologies, Inc. and Patrick J. Byrne. Incorporated by reference from Exhibit 10.2 of the Company's 8-K filed February 4, 2005.*
- 10.41 Agilent Technologies, Inc. Performance-Based Compensation Plan for Covered Employees, Amended and Restated effective November 1, 2004. Incorporated by reference from Exhibit 10.1 of the Company's 8-K filed March 7, 2005.*
- 10.42 Summary of Compensation Arrangement between Agilent Technologies, Inc. and William P. Sullivan, effective March 1, 2005. Incorporated by reference from Exhibit 10.2 of the Company's 8-K filed March 7, 2005.*
- 10.43 Change of Control Severance Agreement between Agilent Technologies, Inc. and William P. Sullivan. Incorporated by reference from Exhibit 10.1 of the Company's 8-K filed September 14, 2005.*
- 10.44 Amended and Restated Change of Control Severance Agreement between Agilent Technologies, Inc. and Agilent's Named Executive Officers, other than the Chief Executive Officer. Incorporated by reference from Exhibit 10.2 of the Company's 8-K filed September 14, 2005.*
- 10.45 Summary of Compensation Arrangement between Agilent Technologies, Inc. and Edward W. Barnholt. Incorporated by reference from Exhibit 10.48 of the Company's 10-Q filed March 10, 2005.*
- 10.46 Summary of Compensation Arrangement between Agilent Technologies, Inc. and Edward W. Barnholt. Incorporated by reference from Exhibit 10.1 of the Company's 8-K filed March 21, 2005.*
- 10.47

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Summary of Compensation Arrangement between Agilent Technologies, Inc. and Adrian T. Dillon. Incorporated by reference from Exhibit 10.49 of the Company's 10-Q filed March 10, 2005.*

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- 10.48 Summary of Compensation Arrangement between Agilent Technologies, Inc. and Chris van Ingen. Incorporated by reference from Exhibit 10.50 of the Company s 10-Q filed March 10, 2005.*
- 10.49 Summary of Compensation Arrangement between Agilent Technologies, Inc. and James G. Cullen, effective March 1, 2005. Incorporated by reference from Exhibit 10.4 of the Company s 8-K filed March 7, 2005.*
- 10.50 Summary of Compensation Arrangement between Agilent and Each of the Non-Employee Directors. Incorporated by reference from Exhibit 10.52 of the Company s 10-Q filed March 10, 2005*
- 10.51 Settlement Agreement and General Release between Agilent Technologies, Inc. and Young K. Sohn. Incorporated by reference from Exhibit 10.53 of the Company s 10-Q filed March 10, 2005*
- 10.52 Change of Control Severance Agreement between Agilent Technologies, Inc. and David B. Cooper, Jr., dated May 3, 2005. Incorporated by reference from Exhibit 10.1 of the Company s 8-K filed May 3, 2005.*
- 10.53 Agilent Technologies, Inc. Indemnification Agreement between Agilent Technologies, Inc. and David B. Cooper, Jr., dated May 3, 2005. Incorporated by reference from Exhibit 10.2 of the Company s 8-K filed May 3, 2005.*
- 10.54 Asset Purchase Agreement, dated September 29, 2000, between Agilent Technologies, Inc. and CIT Group/Equipment Financing, Inc. Incorporated by reference from Exhibit 10.10 of the Company s 10-Q filed on March 19, 2001.
- 10.55 Purchase and Sale Agreement dated February 1, 2001, between Agilent Technologies, Inc. and BEA Systems, Inc. Incorporated by reference from Exhibit 10.11 of the Company s 10-Q filed on June 14, 2001.
- 10.56 English summary of lease between Shanghai WaiGaoQiao Free Trade Zone Dev. Co. Ltd. and Agilent dated June 29, 2001. Incorporated by reference from Exhibit 10.19 of the Company s 10-K filed December 22, 2003.
- 10.57 Asset Purchase Agreement dated October 27, 2004 between Flextronics Sales and Marketing (A-P) Ltd. and Agilent Technologies, Inc. Incorporated by reference from Exhibit 10.40 of the Company s 10-K filed December 21, 2004. First Amendment to Asset Purchase Agreement, dated January 4, 2005, between Flextronics Sales and Marketing (A-P) Ltd. and Agilent Technologies, Inc. Incorporated by reference from Exhibit 10.39 of the Company s 10-Q filed March 10, 2005. Second Amendment to the Asset Purchase Agreement dated February 3, 2005, between Flextronics Sales and Marketing (A-P) Ltd. and Agilent Technologies, Inc. Incorporated by reference from Exhibit 10.40 of the Company s 10-Q filed June 6, 2005.
- 10.58 Agilent Technologies, Inc. 1999 Non-Employee Director Stock Plan (Amended and Restated Effective November 1, 2005). Incorporated by reference from Exhibit 10.58 of the Company s 10-K filed January 17, 2006.
- 10.59 Agilent Technologies, Inc. 2005 Deferred Compensation Plan for Non-Employee Directors (Amended and Restated Effective as of November 1, 2005). Incorporated by reference from Exhibit 10.59 of the Company s 10-K filed January 17, 2006.*
- 10.60 Summary Sheet for Named Executive Officers for Fiscal 2006. Incorporated by reference from Exhibit 10.60 of the Company s 10-K filed January 17, 2006.*
- 10.61 Master Repurchase Agreement (including Annexes and related Confirmation), dated as of January 27, 2006, between Agilent Technologies World Trade, Inc. and Fenway Capital, LLC. Incorporated by reference from Exhibit 99.1 of the Company s 8-K filed February 1, 2006.
- 10.62 Guaranty of Agilent Technologies, Inc. to Fenway Capital, LLC dated, as of January 27, 2006. Incorporated by reference from Exhibit 99.2 of the Company s 8-K filed February 1, 2006.
- 10.63 Agilent Technologies, Inc. Long-Term Performance Program (Amended and Restated through November 1, 2005). Incorporated by reference from Exhibit 10.63 of the Company s 10-Q filed on March 9, 2006.*
- 10.64 Offer Letter to Keith Barnes, Chief Executive Officer of Verigy Pte. Ltd. dated April 4, 2006. Incorporated by reference from Exhibit 10.1 of the Company s 8-K filed on April 12, 2006.*

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- 10.65 Compromise Agreement and General Release with Thomas E. White, dated May 10, 2006. Incorporated by reference from Exhibit 10.1 of the Company's 8-K filed on May 12, 2006. *
- 10.66 Master Separation and Distribution Agreement between Agilent Technologies, Inc. and Verigy Ltd., dated as of May 31, 2006. Incorporated by reference from Exhibit 10.66 of the Company's 10-Q filed on June 6, 2006.
- 10.67 General Assignment and Assumption Agreement between Agilent Technologies, Inc. and Verigy Ltd., dated as of June 1, 2006. Incorporated by reference from Exhibit 10.67 of the Company's 10-Q filed on June 6, 2006.
- 10.68 Intellectual Property Matters Agreement between Agilent Technologies, Inc., Verigy Ltd., and Verigy (Singapore) Pte. Ltd., dated as of June 1, 2006. Incorporated by reference from Exhibit 10.68 of the Company's 10-Q filed on June 6, 2006.
- 10.69 Employee Matters Agreement between Agilent Technologies, Inc. and Verigy Ltd., dated as of June 1, 2006. Incorporated by reference from Exhibit 10.69 of the Company's 10-Q filed on June 6, 2006.
- 10.70 Tax Sharing Agreement by and between Agilent Technologies, Inc. and Verigy Ltd., dated as of June 1, 2006. Incorporated by reference from Exhibit 10.70 of the Company's 10-Q filed on June 6, 2006.
- 10.71 Transition Services Agreement by and between Agilent Technologies, Inc. and Verigy Ltd., dated as of June 1, 2006. Incorporated by reference from Exhibit 10.71 of the Company's 10-Q filed on June 6, 2006.
- 10.72 Manufacturing Trademark License Agreement between Agilent Technologies, Inc. and Verigy Ltd. effective as of June 1, 2006. Incorporated by reference from Exhibit 10.72 of the Company's 10-Q filed on June 6, 2006.
- 10.73 Lease Agreement dated May 17, 2006 by and between Whisman Ventures, LLC, a California limited liability company and Agilent Technologies, Inc.
- 10.74 Asset Purchase Agreement, dated as of August 14, 2005 by and between Agilent Technologies, Inc. and Argos Acquisition Pte. Ltd. Incorporated by reference from Exhibit 2.1 of the Company's 8-K filed on August 15, 2005.
- 10.75 Share Purchase Agreement, dated as of August 12, 2005, by and among Agilent Technologies, Inc. and Agilent LED International, Philips Lumileds Holding B.V. and Koninklijke Philips Electronics N.V. Incorporated by reference from Exhibit 2.2 of the Company's 8-K filed on August 15, 2005.
- 11.1 See Note 5 Net Income per Share in Notes to Condensed Consolidated Financial Statements on page 8.
- 12-14 Not applicable.
- 15. None.
- 16-17 Not applicable.
- 18. None.
- 19. None
- 20-21 Not applicable.
- 22. None.
- 23. None.
- 24. None.
- 25-30 Not applicable.
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 33-98 Not applicable.
- 99. None.

* Indicates management contract or compensatory plan, contract or arrangement.

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