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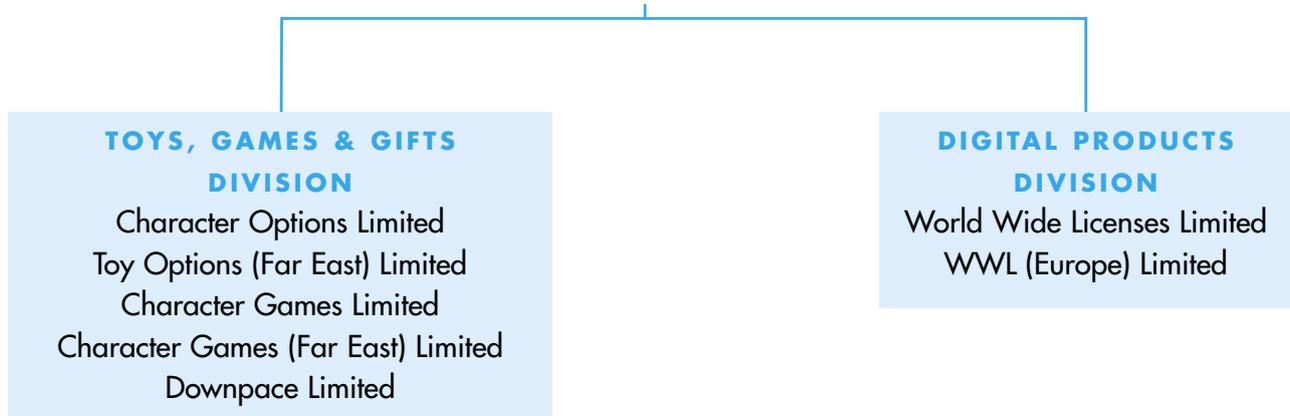
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## DIRECTORS AND ADVISERS

<i>Directors</i>	<i>Registered office</i>	<i>Stockbrokers</i>	<i>Registrars</i>
R King	5th Floor	Collins Stewart Limited	Neville Registrars Limited
E Preziosi	4 Chiswell Street	9th Floor	Neville House
K P Shah	London EC1Y 4UP	88 Wood Street	18 Laurel Lane
J J P Kissane		London EC2V 7QR	Halesowen
J J Diver	<i>Solicitors</i>		West Midlands B63 3DA
I S Fenn	Duane Morris		
Lord Birdwood	5th Floor	<i>Bankers</i>	
A G Horvat	4 Chiswell Street	National Westminster Bank plc	
D Harris	London EC1Y 4UP	Standard Chartered Bank plc	
		The Hongkong and Shanghai Banking Corporation Limited	
<i>Secretary</i>	<i>Auditors</i>	Banca Nazionale del Lavoro S.p.A.	
K P Shah FCCA	Baker Tilly	KBC Bank N.V.	
	Registered Auditors &		
<i>Company registration number</i>	Chartered Accountants		
3033333	Marlborough House		
	Victoria Road South		
	Chelmsford		
	Essex CM1 1LN		

## GROUP STRUCTURE

### THE CHARACTER GROUP PLC



[www.charactergroup.plc.uk](http://www.charactergroup.plc.uk)

The year under review has been, to say the least, very challenging, with many factors taking their toll on our sales and profits.

As reported, in April 2004, we started the year under review with poor 2003 Christmas trading in the UK, closely followed by the unexpected termination by our distributor of our distribution agreement for Polaroid digital cameras in the USA. With no distributor in the USA and a generally lack-lustre toy, game and gift line up of product for the early part of 2004 as well as a difficult trading environment in all our markets, we were facing an uphill battle to get back to a growth pattern.

However, for the 2005 financial year, I am pleased to report that, despite the on-going challenging markets, our confidence in our new product introductions (such as the well documented Robosapien) has proven to be justified in the current run up to Christmas.

### Results

Although our 2004 financial results were disappointing when compared with the previous year, the Directors believe that they were satisfactory when the factors I have already touched on are taken into account.

Without the benefit of the settlement from Uniden America Corporation, which we announced to the market on 29 November 2004, the Directors expected the profit before tax for the year ended 31 August 2004 to be in line with market expectations. As a result of the Uniden settlement, the total profit before tax has risen to £3.2 million of which approximately £0.5 million is exceptional. It should also be noted that the Group has

incurred substantial additional expenses associated with the settlement agreement.

On our normal business excluding exceptional items, our gross margin was maintained at last year's level at 30.8% (2003: 31.3%). Stocks increased from £8.1 million to £12.2 million, mainly as a result of slower than anticipated sales of digital products in the USA.

At the interim stage, the Group had unused bank and trade finance facilities of £2.9 million and the Company was ungeared following the conversion of the Convertible Unsecured Loan Note by Valtidone SpA. By the year-end, the Group had cash at bank of £4.18 million (2003: £3.93 million) and unused bank and trade finance facilities of £1.52m (2003: £1.86 million) and remained ungeared.

Net assets at the end of the period were £11.8 million against £5.3 million in 2003.

### Dividend

The Board is proposing a final dividend of 0.7 pence per share. This, together with the interim dividend of 1.10 pence per share makes the total dividend for the year 1.8 pence per share, a decrease of 40% on the previous year, which is broadly in line with the fall in pre-tax profits.

The dividend is covered 3.41 times by earnings and the shares go ex-dividend on 5 January 2005. Subject to approval by shareholders at the Company's Annual General Meeting on 19 January 2005, the final dividend will be paid on 28 January 2005 to shareholders on the Register as at 7 January 2005.  
continued...

### Review and Prospects

We announced in April that we intended to integrate Downpace to form a single Toys, Games and Gifts division within the Group in order to rationalise the use of the Group's resources. However, to ensure that our long term strategy of developing a significantly larger proportion of our product line-up was working to our satisfaction, we decided to implement the restructuring plans later than originally anticipated.

We are currently in the process of consultation regarding our integration plans with the Directors of Downpace. We would expect the process of integration to be completed by the end of March 2005.

### Digital Products Division

World Wide Licensing Limited ("WWL") is operating in a market where, although there is growth in revenue by our major competitors, there is little evidence of growth in profits and where the market has become very competitive with non-branded cameras finding it ever more difficult to get retail placement.

Against this background and the loss of our US distributor at a critical point in the year, WWL did not meet its targets for the year ended 31 August 2004. The set back we experienced in the US has had adverse repercussions throughout our digital business with greater costs being absorbed into lower than anticipated sales. Since the year-end, I am pleased to report that we have begun to see some positive signs from the US market and we believe that we shall start to see our product placed in a growing number of major US retailers from early next year.

On a positive note, our Research and Development Centre in the HiTech Park in Shenzhen, China is growing and becoming very effective in allowing us to create a creditable position in the digital camera category. We are committed to introducing engineers from the United States and Japan into the staffing mix in China to further enhance our R&D and technical abilities. We have also taken a strategic initiative with the Polaroid Corporation to engage with their technical team to be part of our development process.

Although as we have previously reported we have experienced some problems in bringing new products to the market on time, our development team has continued to build on its experience and has enhanced its skills base with every new camera that comes to the market. Today we have many products that are designed and developed by WWL and, with the imminent introduction of our Foveon x530 digital camera, we shall have reached a higher level in camera design and technical expertise which is a credit to the team in the Far East.

Our Polaroid agreement is entering its third year and we have engaged in an extensive review process with them to establish a new long term agreement. It has become apparent that the close relationship between WWL and Polaroid should set the tone for a very competitive and dynamic range of products for the world market-place.

Our distribution of digital products has now stabilised and we are active in over 30 markets.

continued...

With the introduction of a new distributor in the United States and strong growth in Canada and various European Markets we believe that we are well placed to grow the business in 2005.

Our current digital business is trading in line with our expectations and we anticipate that we will increase its contribution to Group revenue both in the 2005 financial and calendar years.

### Toys, Games and Gifts Division

In our interim report, we stated that the difficult trading experienced at Christmas had continued into the second half and that we were expecting that new product introductions would begin to impact on our sales only in the last quarter of the 2004 financial year.

In the period under review, whilst trading was disappointing, we have nevertheless made progress as an organisation. We have expanded our development programme, and of our current sales both in the UK and internationally, the percentage of our own developed products continues to increase.

The success of Robosapien has been well documented and we believe that, by the time Christmas has finished, we will have placed approximately 180,000 pieces into the market and we are expecting a total sell through at retail. We are also very happy with our GR8 Gear range where our in-house developed fashion centre has sold out in the UK and where we have supplied seven overseas territories, with good sales reports from each. We are experiencing another good year for Scooby Doo, which has all but sold out for the

year, and Magic Sand range is having another successful year. In games, Spin the Bottle is selling well in its 8th year and Slapz, Pin the Tail on the Donkey and Hungry Huey are all worthy of mention as they turn into perennial favourites.

In general, we have strengthened and expanded our distribution base. For example our trading with Gadget Shop, our joint launch partner with Hamley's for Robosapien, has increased substantially and we have developed our business with more E-business, stationery and non toy outlets.

New product introductions for 2005 include: a new line up of Robosapien related products and a broad range of Batman products to be launched with the release of the new film in 2005. The Batman range has been developed with our trading partner and investor Giochi Preziosi SpA and, from initial reactions, should provide substantial sales, both domestically and internationally, next calendar year. We are also launching a new chess set and other products under a Star Wars license as well as working with Disney in launching the Disney Princess dolls which will be co-ordinated with the release of the Cinderella DVD in October 2005. After a gap of ten years, we shall also be relaunching Sky Dancers, which sold over a million units on its last outing in the UK, while in the Spring, we will launch Go Yo's, where we have high hopes of a significant early sell through.

It is refreshing to be turning the year with so many toy and games products and ranges with such potential going through to next year. continued...

On the gift side, we are not as advanced in the cycle; however, we have high hopes for the Talking Mug range which has just gone to market and where early sales have been very encouraging. In addition to finalising some exciting new gift licenses we shall be introducing some of our own-developed products which is a result of utilising the wider Group's internal resources and capabilities.

Overall, in this 2005 financial year we have introduced some very exciting new products which have already had good sell through to Christmas and we will end 2004 with clean stocks. This, together with the exciting reaction to next year's products at previews from our major customers, underpins our belief that, although the retail environment will remain competitive and challenging across the sector, the Group's current momentum will continue through both the next financial and calendar year.

### People

No business can survive and prosper without the individual effort and input from its employees and, during the difficult year we have just endured, that effort has had to be even more focused.

It is therefore very gratifying that over this period, we have received many calls and compliments for the high standard of service that we have achieved in satisfying the ever increasing demands of our valued customers.

The Board is truly grateful for the effort and support of our employees throughout the world.

### Summary

We have made substantial progress in our product line-up and we expect that as we focus on our product offering throughout the Group, we shall achieve improved sales from a smaller number of individual products. This strength in our product line-up gives us confidence that, despite the market conditions, we are looking forward to a year of significant growth.



**Richard King**  
Chairman

## DIRECTORS' BIOGRAPHIES

**Richard King** (aged 59), Executive Chairman, has extensive experience in the toy industry and has been involved in importing consumer products from the Far East since 1969. He established the original business of The Character Group plc jointly with Mr Kissane and Mr Shah in 1991 and works in close association with the management of each division to develop and implement Group strategies.

**Enrico Preziosi** (aged 56), Chief Executive Officer and Managing Director, was appointed to the Board as a Non-Executive Director in August 2000 and as Chief Executive and Managing Director in May 2001. He is the Chairman of, and is interested in a majority of the issued shares of, Giochi Preziosi S.p.A. He founded Giochi Preziosi S.p.A. in 1984 and has since been instrumental in growing its business.

**Kiran Shah** (aged 50), Group Finance Director, is a member of the Chartered Association of Certified Accountants. After initially working in private accountancy practice, he moved into industry and since 1978 has been involved extensively in the toy industry, notably in his role in jointly heading up a successful management buyout of Merit Toys Limited in 1981 and its subsequent sale to Bluebird Toys plc in 1988. He jointly established the original business of The Character Group plc with Mr King and Mr Kissane in April 1991.

**Joe Kissane** (aged 52), Managing Director of Character Options Limited, has considerable sales expertise in and outside the toy industry, gained over a period of 30 years, notably with such companies as Nabisco, Lego and Tonka. He is one of the founders of the Group.

**Jon Diver** (aged 40), Group Marketing Director, joined the Group in September 1991 from Rainbow Toys Limited, where he was Senior Marketing Executive. He became Group Marketing Director in August 1994, and has developed close working relationships with the Group's suppliers. He has played a key role in the development and implementation of the Group's marketing strategy.

**Ian Fenn** (aged 61), Senior Independent Non-Executive Director, joined the Board in May 1995. He has extensive experience in corporate finance gained over many years in stockbroking and merchant banking in the City of London. He is a Director of ARM Corporate Finance Limited which is authorised and regulated by the Financial Services Authority Limited.

**Lord Birdwood** (aged 66), Independent Non-Executive Director, was appointed to the Board in September 1995. He has experience as a Director of quoted and private companies. He has particular interests in executive placement and recruitment.

**Aldo Horvat** (aged 62), Non-Executive Director, was appointed to the Board in November 2002. He is a consultant to Giochi Preziosi S.p.A. and has considerable experience in the toy industry gained over more than 30 years.

**David Harris** (aged 54), Independent Non-Executive Director, was appointed to the board in May 2004. He has considerable financial experience gained over a 30 year career in both executive and non-executive capacities. He is currently a non-executive director of Small Companies Dividend Trust PLC, Zero Dividend Recovery Fund Limited and Osprey Small Companies Income Fund Limited, all of which are quoted companies.

## REPORT OF THE DIRECTORS

The directors present their report together with the accounts for the year ended 31 August 2004.

### Directors

The following are the directors that served during the year:

Richard King (Executive Chairman)  
 Enrico Preziosi (Chief Executive Officer and Managing Director)  
 Kirankumar Premchand Shah FCCA (Group Finance Director)  
 Joseph John Patrick Kissane (Managing Director, Character Options Limited)  
 Jonathan James Diver (Group Marketing Director)  
 Ian Stanley Fenn (Senior Independent Non-Executive Director)  
 Lord Birdwood (Independent Non-Executive Director)  
 Aldo Gianfranco Horvat (Non-Executive Director)  
 David Harris (Independent Non-Executive Director – appointed 1 May 2004)

Biographies of the directors are set out on page 7.

### Principal activity

The Group is engaged in the design, development and international distribution of digital cameras, toys, games and giftware.

### Business review, results and dividend

A review of the business is contained in the Chairman's Statement on pages 3 to 6 and the results are detailed in the consolidated profit and loss account on page 20, the consolidated balance sheet on page 21 and the consolidated cash flow statement on page 23. There was a profit for the year, after taxation, amounting to £3,727,000.

An interim dividend of 1.1pence per share was paid on 30th July 2004. The directors recommend a final dividend of 0.7pence per share making a total dividend of 1.8pence per ordinary share (2003: 3.0 pence). If approved, the final dividend will be payable on 28 January 2005, to shareholders on the register on 7 January 2005.

### Directors and their interests in shares

The directors and their interests (all of which are beneficial) in the shares of The Character Group plc as at 6 December 2004 were as follows:

Directors	Number of ordinary shares	31 August 2004 Ordinary shares under option	Number of ordinary shares	31 August 2003 Ordinary shares under option
R King	5,345,428	–	5,270,428	–
E Preziosi	11,885,898	–	11,885,898	–
K P Shah	5,645,000	–	5,620,000	–
J J P Kissane	1,462,300	185,000	1,462,300	185,000
J J Diver	1,690,640	185,000	1,690,640	185,000
I S Fenn	9,000	–	9,000	–
Lord Birdwood	8,750	–	8,750	–
A G Horvat	–	–	–	–
D Harris	14,097	–	–	–
TOPS Pension Scheme*	1,600,000	–	1,600,000	–

(\*each of R King, K P Shah and J J Diver is a trustee and a beneficiary under such pension scheme arrangements.)

There were no other changes in the directors' beneficial interests between 31 August 2004 and 6 December 2004.

Included in the interests of R King are his interests in shares held by Cedarberg Investments Limited, being 1,885,428 ordinary shares at 31 August 2004 and at 31 August 2003. There is also included in the interests of R King his interests in shares held by his spouse, Mrs M H King, being 320,000 shares at 31 August 2004 and at 31 August 2003.

## REPORT OF THE DIRECTORS CONTINUED

Included in the interests of E Preziosi are his interests in shares held by Giochi Preziosi S.p.A., being 11,885,898 ordinary shares at 31 August 2004 and at 31 August 2003.

Included in the interests of K P Shah are his interests in shares held by Sarissa Holdings Limited, being 5,620,000 ordinary shares at 31 August 2004 and at 31 August 2003.

Further, Orbis Pension Trustees Limited, the trustee of the Company's employee share ownership trust ("the Trust"), held 285,000 ordinary shares at 31 August 2004 and at 31 August 2003. Each of R King, K P Shah, J J P Kissane and J J Diver is deemed to be interested in such holding by virtue of being within the class of beneficiaries defined by the Trust.

Pursuant to the requirements of their appointment letters, Lord Birdwood, Mr Fenn, Mr Horvat and Mr Harris retire at the Annual General Meeting and, being eligible, offer themselves for re-election or (as appropriate) re-appointment.

### Employment policies

The Group depends on the skills and commitment of its employees in order to achieve its objectives. Group staff at every level are encouraged to make their fullest possible contribution to the Group's success.

The Group's selection, training, development and promotion policies ensure equal opportunities for all employees regardless of gender, marital status, race, age or disability. All decisions are based on merit.

It is the Group's policy not to discriminate between employees or potential employees on any grounds. Full and fair consideration is given to the recruitment, training and promotion of disabled people and should staff become disabled during the course of their employment, efforts would be made to provide appropriate re-training. The Group places enormous importance on the contributions of its employees and aims to keep them informed of developments in the Group by way of regular meetings, newsletters and publications, together with distribution of the Annual Report.

Employees are encouraged to become involved in the financial performance of the Group through participation in the Group's share option schemes.

### Research and development

The Group's research and development activities are concentrated on the development of new products, new processes and improvements to or developments of existing products.

### Policy and practice on payment of creditors

The Group does not follow any standard code of practice for paying its suppliers but, instead, agrees with each principal supplier the terms of payment for each transaction or series of transactions. The Group's policy is then to abide by those pre-arranged terms for payment. At 31 August 2004, trade creditors of the Group represented an average of 99 days credit in relation to total purchases for the year.

### Statement of directors' responsibilities

We are required under company law to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Group and the Company, and of the Group profit or loss for that year.

In preparing these accounts we are required to:

- select suitable accounting policies and apply them consistently
- make reasonable and prudent judgements and estimates
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts
- prepare the accounts on a going concern basis unless, in our view, the Group and the Company will be unable to continue in business.

We are also responsible for:

- keeping proper accounting records
- safeguarding the Group's and the Company's assets
- taking reasonable steps for the prevention and detection of fraud.

## REPORT OF THE DIRECTORS CONTINUED

### Substantial shareholders other than directors

At 1 December 2004 the following, other than the directors and their family interests, had notified the Company of an interest in 3% or more of the Company's ordinary shares:

Name	Number of ordinary shares	Shareholding %
Mittel Generale Investments S.p.A	5,221,000	9.91%
Sweet Briar Investments Limited	1,790,000	3.40%

### Changes in Share Capital

On 11 November 2003, the Company issued and allotted 4,000,000 new ordinary shares of 5 pence each in the Company to Valtidone S.p.A., the holder of the Company's £4,600,000 (nominal) convertible loan note (the "Loan Note"), following a partial exercise by Valtidone S.p.A. of its rights of conversion in respect of £1,600,000 (nominal) of the Loan Note, at a conversion price of 40 pence per ordinary share.

On 3rd December 2003, the Company issued and allocated a further 7,500,000 new ordinary shares of 5 pence each to Valtidone S.p.A following the due exercise by Valtidone S.p.A of the remainder of its rights of conversion in respect of the outstanding £3,000,000 (nominal) of the Loan Note at the conversion price of 40 pence per ordinary share.

On 1 April 2004 and 16 June 2004 respectively, 8,600 and 16,400 ordinary shares of 5 pence each in the Company were issued at a price of 24.25 pence per ordinary share to an ex-employee on exercise of his share options.

On 29 April 2004, the Company purchased 40,000 ordinary shares of 5 pence each in the Company for cancellation at a price of 100 pence per share. This represented 0.08% of the issued share capital at the date of cancellation.

On 30 April 2004, the Company purchased 60,000 ordinary shares of 5 pence each in the Company for cancellation at a price of 100 pence per share. This represented 0.1% of the issued share capital at the date of cancellation.

On 25 May 2004, the Company purchased 25,000 ordinary shares of 5 pence each in the Company for cancellation at a price of 81 pence per share. This represented 0.05% of the issued share capital at the date of cancellation.

### Share option schemes

Details of the share option schemes are given in note 17 to the accounts.

### Charitable and political donations

Payments of a charitable nature made during the year amounted to £16,000 (2003: £28,000). There were no political contributions.

### Annual General Meeting

Notice convening the tenth annual general meeting of the Company is set out on pages 40 to 41 of this document. Full details of the business to be transacted at that meeting is set out in that notice. The business of the meeting will include special business proposing the consideration of resolutions to:

- renew the directors' general authority to allot unissued shares in the capital of the Company up to an aggregate nominal amount of £878,130 (17,562,600 ordinary shares of 5 pence each in the capital of the Company) This authority will expire on whichever is the earlier of the conclusion of the annual general meeting of the Company to be held in 2006 or the date falling 15 months following the passing of this resolution. The directors have no present intention of exercising this authority, which represents approximately 33.3% per cent of the issued share capital of the Company at 31 August 2004 and at 3 December 2004;
- authorise the directors to offer to allot shares to shareholders who elect to accept the same in lieu of any cash dividend entitlement;
- authorise the directors to make purchases of the Company's issued ordinary shares in the market for cancellation, or to be held in treasury, if and when the directors consider that it would be in the best interest of the Company and shareholders generally to do so, up to 7,903,180 shares (representing approximately 15 per cent of the current issued share capital of the Company). The price at which an ordinary share in the Company may be purchased in exercise of this authority is subject to a maximum price of 105% of the average middle market values of an issue share in the Company in the five business days prior to purchase and a minimum of 5pence, being the nominal value of an issued share in the Company. There is no present intention on the part of the directors to exercise this authority. If all options granted by the Company (pursuant to the Group's share option schemes particularised in note 17 to the accounts) and subsisting as at 3 December 2004 were exercised a total of 2,056,000 of new ordinary shares would be allotted, representing approximately 3.75% of the enlarged issued share capital of the Company following such exercise. If the authority proposed for the buy back of shares by the Company was to be exercised in full, then the number of shares to be issued on exercise of the said options would constitute 4.39% of the issued share capital as enlarged by such allotments of shares;
- approve a disapplication of shareholder pre-emption rights to enable the issue of equity securities in connection with any rights issues made by the Company, with certain adjustments to shareholder entitlements to be made for practical purposes to deal with fractional entitlements and overseas restrictions on offers of shares in UK companies and a further limited disapplication of those pre-emption rights on the allotments for cash of up to an aggregate nominal amount of £131,710 (2,634,200 ordinary shares of 5 pence each in the capital of the Company), representing approximately 5% of the nominal value of the issued ordinary share capital of the Company as at 31 August 2004 and 3 December 2004

### Auditors

A resolution to re-appoint Baker Tilly as auditors to the Company will be proposed at the Annual General Meeting.

### Corporate Governance Statement

The directors have considered the provisions set out in the Principles of Good Governance and Code of Best Practice (“the Combined Code”) appended to the Listing Rules of the Financial Services Authority.

#### Directors

The Board of directors comprises five executive directors and four non-executive directors, as detailed on page 8. The independent non-executive directors are Lord Birdwood, Mr Fenn (who is the senior independent non-executive director) and Mr Harris. The Board is structured so that no one individual or group dominates the decision-making process.

Board meetings are held four times a year and at other times as required to address requirements arising between these scheduled meetings. A formal schedule of matters specifically reserved to the Board, including (inter alia) overall strategy and monitoring of financial performance, has been adopted.

The Board has established an Audit Committee, a Remuneration Committee and a Nominations Committee with duties and responsibilities formally delegated to them.

#### Audit Committee

I S Fenn (Chairman), Lord Birdwood, D Harris

The Audit Committee is responsible for ensuring that the financial performance of the Group is properly measured and reported and for reviewing reports from the auditors relating to Group accounts and the Group’s internal control systems. The committee is also responsible for the development, implementation and monitoring of the Company’s policy on external audit. The committee reserves oversight responsibility for monitoring the independence, objectivity and compliance with ethical and regulatory requirements. The committee also ensures that key partners within the external auditors are rotated from time to time in accordance with UK rules.

#### Remuneration Committee

Lord Birdwood (Chairman), I S Fenn, D Harris

The Remuneration Committee is responsible for setting the remuneration of the executive directors and the senior management and for the operation of the Company’s share option schemes. The Directors’ Remuneration Report is shown on pages 15 to 17.

#### Nominations Committee

R King (Chairman), Lord Birdwood, I S Fenn, D Harris

The Nominations Committee is responsible for considering and recommending to the Board changes in the Board’s composition and membership.

All non-executive directors of the Company who are members of these committees are entitled to seek, at the Company’s expense, independent professional advice in connection with their roles on these committees.

#### Internal Control

The Board is ultimately responsible for the Group’s system of internal control and for reviewing its effectiveness. However, such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can provide only reasonable and not absolute assurance against material misstatement or loss.

Following publication of the guidance for directors on internal control “Internal Control: Guidance for Directors on the Combined Code” (“the Turnbull Guidance”), the Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group. This process has been in place throughout the year under review and up to the date of approval of the annual report and accounts and is regularly reviewed by the Board and accords with the guidance.

The Board has reviewed the effectiveness of the system of internal control. In particular it has reviewed and updated the process for identifying and evaluating the significant risks affecting the business and the policies

## REPORT OF THE DIRECTORS CONTINUED

and procedures by which these risks are managed.

Key elements of the Group's system of internal control are as follows:

### Control environment

- the setting of appropriate levels of authorisation which must be adhered to as the Group conducts its business
- the implementation of a recognised organisational and management reporting structure within which individual executive directors have responsibility for the day-to-day running of the business
- established and detailed procedures for the setting of annual budgets and monthly forecasts and the ongoing monitoring of actual financial performance against these targets, on a monthly basis, both at operational and Board level and
- a clearly defined and well-established set of accounting policies which ensure that the financial performance is recorded on a consistent and appropriate basis throughout the Group's reporting entities.

### Monitoring and corrective action

There are ongoing procedures in place for monitoring the system of internal financial controls. The remit of the Audit Committee includes meeting to review the effectiveness of the Group's system of internal financial controls, and considering reports made to it by the Group's auditors. The Group does not have an internal audit function. During the year the Board have reviewed the need for an internal audit function and continues to believe that the current size of the Group does not warrant the establishment of an internal audit function. The need for an internal audit function will continue to be reviewed on an annual basis.

### Risk management

Management are responsible for the identification and evaluation of significant risks applicable to their areas of the business together with the design and operation of suitable internal controls. These risks are assessed on a continual basis and may be associated with a variety of internal or external sources, including control breakdowns, disruption in information systems, natural catastrophe and regulatory requirements.

Management report to the Board regularly on their review of risks and how they have managed the risks. The Board reviews the key risks inherent in the business and the system of control necessary to manage such risks.

### Liquidity risk

The Group finances itself through a combination of equity and short term debt. The Group satisfied its liquidity requirements during the period under review. The Group's main working capital facility is provided by factoring. There was also continued use of short term bank facilities during the period under review. As at 31 August 2004, the Group had committed bank facilities of £7.25 million, of which £1.52 million was undrawn.

### Foreign currency risk

The Group faces foreign currency exposures on translation of the net assets and results of its overseas subsidiaries and on trading transactions undertaken mainly in US dollars. The Group seeks to mitigate the effect of its currency exposures by buying currency forward when appropriate. The Group does not hedge its resulting translation exposures as these are accounting rather than cash exposures.

## REPORT OF THE DIRECTORS CONTINUED

### Relations with shareholders

The Board supports the principle of clear reporting of financial performance to shareholders. Each year shareholders receive a full annual report and an interim report, with supplementary trading statements issued from time to time where appropriate.

Members of the Board will be available at the forthcoming Annual General Meeting to answer any questions from the shareholders.

### Compliance statement

Throughout the year the Group has fully complied with the provisions of the Combined Code with the following exceptions:

- Code provision D.3.1 states that the Audit Committee should consist of at least three directors, all of which should be non executive. Until 30 April 2004, the Audit Committee only consisted of two non-executive directors and R King, which the Board considered appropriate, given the method of operation of the Group. On 1 May 2004, D Harris was appointed as a non-executive director and as a member of the Audit Committee. On the same day, R King ceased to be a member of the Audit Committee. As a result the Group now fully complies with code provision D.3.1.
- Code provision A.6.2 states that all directors should be subject to re-election at intervals of no more than three years. The executive directors' service contracts were prepared before the Combined Code was issued, and as such do not contain such re-election provisions. An amendment cannot be made unilaterally by the Company to an executive director's service contract and any such amendment would, accordingly, have to be negotiated in turn with each executive director. Given the significant shareholdings of the executive directors, and the potential cost to the Company of compensating the executive directors for any such amendment to their contracts, the Board considers that the existing arrangements with the executive directors should, for the time being, remain undisturbed in this respect.

### Going Concern

After making enquiries, the Board considers that the Group has adequate resources to continue operating for the foreseeable future and has therefore adopted the going concern basis in preparing the accounts.

By Order of the Board

**K P Shah** FCCA  
Secretary

Registered Office:  
5th Floor, 4 Chiswell Street  
London EC1Y 4UP

9 December 2004

### Directors' Remuneration Report

The Board presents the Remuneration Report for the year ended 31 August 2004.

#### The Remuneration Committee

The Remuneration Committee consists of three independent non-executive directors, Lord Birdwood, Mr Fenn and Mr Harris. The policy of the Remuneration Committee is framed to give consideration to the provisions as to best practice set out in the Combined Code.

#### Remuneration of Directors

Each executive director is paid a basic salary and is entitled to benefits, namely payments of pension contributions to a suitable scheme of his choice, the option of the use of a company car, fuel and/or mileage allowance and participation in a private health care scheme.

Each of the executive directors is also entitled under the terms of his service contract to a bonus of an amount up to his basic salary in the event that specified performance targets are met or exceeded. These targets require increases in earnings per share in each financial year of the Group, adjusted to exclude certain exceptional non-trading items.

The basic salaries referred to above are reviewed every year by the Remuneration Committee. The service contracts of the executive directors incorporate notice periods of 12 months.

These arrangements were originally agreed by the Board of Directors in May 1995, just prior to the flotation of the Company on the London Stock Exchange, in consultation with their legal and financial advisers and have recently been reviewed by the Remuneration Committee. In originally establishing these arrangements, and in the recent review, due account was taken of other listed companies of comparable size and business complexity, and in particular of the need to put in place incentive arrangements for each executive director which would be challenging and compatible with sustainable growth in shareholder value, whilst not being over-complicated or manipulable. The Board's policy on pension arrangements is to favour money purchase schemes rather than defined benefit ("final salary") schemes.

The Company believes that share ownership by executive directors and senior executives strengthens the links between their personal interests and those of the shareholders. Executive directors holding less than 10% of the Company's issued share capital are eligible to participate in the Company's Inland Revenue approved executive share option scheme, details of which can be found in note 17 to the accounts. All executive directors are entitled to participate in the Company's unapproved executive share option scheme and in the Company's Enterprise Management Incentive Share Option Scheme, details of which may also be found in note 17 to the accounts.

The non-executive directors are appointed for a fixed term expiring at each Annual General Meeting of the Company, when they may offer themselves for re-election. Lord Birdwood, Mr Fenn, Mr Harris and Mr Horvat are each entitled to fees, currently at the rate of £20,000 per annum (2003: £20,000), plus expenses, without any right to compensation on early termination. Mr E Preziosi does not receive any remuneration.

## REPORT OF THE DIRECTORS CONTINUED

The following table shows a breakdown of the remuneration of the directors for the year ended 31 August 2004 and the year ended 31 August 2003. The table has been audited, including the information in respect of the Directors' share options, as referred to in the Independent Auditors' Report.

Year ended 31 August 2004

	Salary/fees £	Performance bonus £	Benefits in kind £	Pension contribution £	Total £
R King	167,625	–	3,907	58,668	230,200
E Preziosi	–	–	–	–	–
K P Shah	165,600	–	3,306	41,400	210,306
J J P Kissane	145,180	–	2,587	36,600	184,367
J J Diver	145,180	–	4,486	29,036	178,702
I S Fenn (non-executive)	20,000	–	–	–	20,000
Lord Birdwood (non-executive)	20,000	–	–	–	20,000
A G Horvat (non-executive)	20,000	–	–	–	20,000
D Harris (non-executive)	6,667	–	–	–	6,667
	690,252	–	14,286	165,704	870,242

Year ended 31 August 2003

	Salary/fees £	Performance bonus £	Benefits in kind £	Pension contribution £	Total £
R King	149,000	149,000	4,902	52,150	355,052
E Preziosi	–	–	–	–	–
K P Shah	144,000	144,000	3,969	36,000	327,969
J J P Kissane	122,000	122,000	2,582	36,600	283,182
J J Diver	122,000	122,000	6,626	24,400	275,026
I S Fenn (non-executive)	17,033	–	–	–	17,033
Lord Birdwood (non-executive)	17,033	–	–	–	17,033
A G Horvat (non-executive)	13,333	–	–	–	13,333
M F Cellai (non-executive)	–	–	–	–	–
	584,399	537,000	18,079	149,150	1,288,628

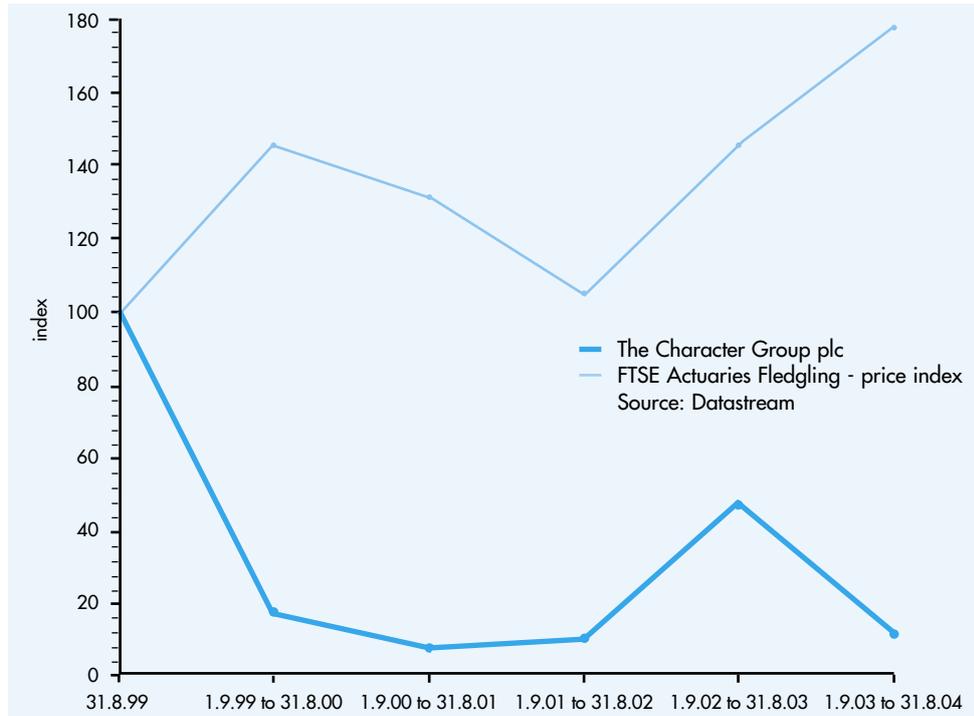
On 5 February 2003, options over 185,000 new ordinary shares in the Company were granted to each of J J P Kissane and J J Diver. These options have been granted pursuant to the Enterprise Management Incentive Share Option Scheme which was approved by shareholders on 22 January 2003. The options are exercisable at a price of 54 pence per share normally no earlier than three and not later than ten years from the date of grant, subject to the achievement of a predetermined profit related performance target, which target has been achieved.

R King, K P Shah, J J P Kissane and J J Diver are the only directors to whom retirement benefits are accruing under a money purchase pension scheme.

At 31 August 2004 the mid-market price of an issued ordinary share in The Character Group plc was 50 pence and during the year the price ranged from 168 pence to 45 pence.

The Performance Graph below compares the Total Shareholder Return performance of the Company with the FTSE Fledgling Index over the last five years. The FTSE Fledgling Index has been selected as it includes UK quoted companies of similar size to the Company.

**Total Shareholder Return 31 August 1999 to 31 August 2004**



On behalf of the Board

**Lord Birdwood**  
 Chairman, Remuneration Committee  
 9 December 2004

## INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF THE CHARACTER GROUP PLC

We have audited the accounts which comprise the Consolidated Profit and Loss Account, the Consolidated Balance Sheet, the Parent Company Balance Sheet, the Consolidated Cash Flow Statement and the related notes. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration disclosure as set out in the Directors' Remuneration Report and the accounts in accordance with applicable law and United Kingdom Accounting Standards are set out in the Statement of directors' responsibilities.

Our responsibility is to audit the accounts and the part of the Directors' Remuneration Report required to be audited in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the accounts give a true and fair view and whether the accounts and the part of the Directors' Remuneration Report that is described as having been audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the accounts, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listings Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control covers all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited accounts. This other information comprises only the Report of the Directors, the unaudited part of the Directors' Remuneration Report, the Chairman's Statement and the Corporate Governance Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

### Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts and the part of the Directors' Remuneration Report required to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts and the part of the Directors' Remuneration Report required to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts and the part of the Directors' Remuneration Report required to be audited.

## INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE CHARACTER GROUP PLC CONTINUED

### Opinion

In our opinion:

- the accounts give a true and fair view of the state of affairs of the Company and the Group at 31 August 2004 and of the Group profit for the year then ended; and
- the accounts and part of the Directors' Remuneration Report required to be audited have been properly prepared in accordance with the Companies Act 1985.

### **Baker Tilly**

Registered Auditor

Chartered Accountants

Marlborough House, Victoria Road South,

Chelmsford, Essex CM1 1LN

9 December 2004

## CONSOLIDATED PROFIT AND LOSS ACCOUNT

for the year ended 31 August 2004

	note	Other 2004 £000	Exceptional 2004 (note 3) £000	Total 2004 £000's	2003 (as re-stated) £000's
<b>Turnover</b>	2	74,653	1,393	<b>76,046</b>	85,308
Cost of sales		(51,675)	(2,657)	(54,332)	(58,610)
<b>Gross profit</b>		22,978	(1,264)	<b>21,714</b>	26,698
<b>Net operating expenses</b>					
Selling and distribution costs		(9,131)	(278)	(9,409)	(9,138)
Administration expenses		(10,919)	(470)	(11,389)	(11,967)
Other operating income		257	2,504	2,761	526
<b>Operating profit</b>	3	3,185	492	<b>3,677</b>	6,119
Interest	5	(453)	–	(453)	(563)
<b>Profit on ordinary activities before taxation</b>		2,732	492	<b>3,224</b>	5,556
Taxation	6	589	(86)	503	(287)
<b>Profit on ordinary activities after taxation</b>		3,321	406	<b>3,727</b>	5,269
<b>Dividend</b>	7			<b>(1,093)</b>	(1,310)
<b>Retained profit for the year</b>	18			<b>2,634</b>	3,959
<b>Earnings per share</b>	8				
– basic				7.48p	12.85p
– fully diluted				7.31p	10.11p
<b>Dividend per share</b>	7			<b>1.80p</b>	3.00p
<b>EBITDA (earnings before interest, tax, depreciation and amortisation)</b>				<b>4,444</b>	7,128

All activity has arisen from continuing operations.

## STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

	note	12 months to 31 August 2004 £000's	12 months to 31 August 2003 (as restated) £000's
Profit for the financial period		2634	3,959
Foreign exchange differences	18	(541)	(185)
<b>Total recognised gains and losses relating to the financial period</b>		<b>2,093</b>	3,774
Prior period adjustment	1	569	
<b>Total recognised gains and losses since last annual report</b>		<b>2,662</b>	

## CONSOLIDATED BALANCE SHEET

as at 31 August 2004

	note	2004 £000's	2003 £000's (as restated)
<b>Fixed assets</b>			
Intangible assets	9	692	737
Tangible assets	10	1,599	1,876
Investments	11	2	2
		<b>2,293</b>	<b>2,615</b>
<b>Current assets</b>			
Stocks	12	12,227	8,143
Trade debtors subject to finance arrangements		8,319	7,302
Factor advances		(6,785)	(5,401)
		<b>1,534</b>	<b>1,901</b>
Debtors – including non-factored trade debtors	13	16,024	16,776
Cash at bank and in hand		4,183	3,932
		<b>33,968</b>	<b>30,752</b>
Creditors: amounts falling due within one year:	14		
Convertible loan note		–	(4,600)
Other creditors		(24,484)	(23,504)
<b>Net current assets</b>		<b>9,484</b>	<b>2,648</b>
<b>Total assets less current liabilities</b>		<b>11,777</b>	<b>5,263</b>
Creditors: amounts falling due after more than one year:	15	–	(4)
<b>Net assets</b>		<b>11,777</b>	<b>5,259</b>
<b>Capital and reserves</b>			
Called up share capital	17	2,634	2,064
Investment in own shares	24	(908)	(908)
Capital redemption reserve	18	40	15
Share premium	18	11,794	7,843
Merger reserve	18	651	651
Profit and loss account	18	(2,434)	(4,406)
<b>Equity shareholders' funds</b>	16	<b>11,777</b>	<b>5,259</b>

The accounts on pages 20 to 39 were approved by the Board of Directors on 9 December 2004.

**R King**  
Director

**K P Shah**  
Director

## PARENT COMPANY BALANCE SHEET

as at 31 August 2004

	note	2004 £000's	2003 £000's (as restated)
<b>Fixed assets</b>			
Tangible assets	10	921	995
Investments	11	3,195	3,195
		<b>4,116</b>	<b>4,190</b>
<b>Current assets</b>			
Debtors	13	9,656	13,347
Cash at bank and in hand		1,065	296
		<b>10,721</b>	<b>13,643</b>
Creditors: amounts falling due within one year:	14		
Convertible loan note		–	(4,600)
Other creditors		(704)	(1,969)
		<b>10,017</b>	<b>7,074</b>
<b>Net current assets</b>		<b>10,017</b>	<b>7,074</b>
<b>Total assets less current liabilities</b>		<b>14,133</b>	<b>11,264</b>
<b>Capital and reserves</b>			
Called up share capital	17	2,634	2,064
Investment in own shares	24	(908)	(908)
Capital redemption reserve	18	40	15
Share premium	18	11,794	7,843
Profit and loss account	18	573	2,250
<b>Equity shareholders' funds</b>	16	<b>14,133</b>	<b>11,264</b>

The accounts on pages 20 to 39 were approved by the Board of Directors on 9 December 2004.

**R King**  
Director

**K P Shah**  
Director

## CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 August 2004

	note	2004 £000's	2003 £000's
<b>Cash inflow from operating activities</b>	20	3,326	3,817
<b>Returns on investment and servicing of finance</b>			
Interest received		7	12
Interest paid		(460)	(574)
Interest element of finance lease rental payments		–	(1)
<b>Net cash outflow for returns on investments and servicing of finance</b>		(453)	(563)
<b>Taxation</b>		(315)	(285)
<b>Capital expenditure and financial investment</b>			
Payments to acquire tangible fixed assets		(510)	(1,038)
Sale of tangible fixed assets		9	24
Purchase of business and assets	9	–	(902)
<b>Net cash outflow for capital expenditure and financial investment</b>		(501)	(1,916)
Equity dividends paid		(1,626)	(410)
Cash inflow before financing		431	643
Issue of new shares		6	–
Purchase of own shares		(121)	–
Capital element of finance lease rentals		(5)	5
Expenses in relation to the conversion of loan note		(60)	–
<b>Net cash (outflow)/inflow from financing</b>		(180)	5
<b>Increase in cash in the year</b>		251	648
<b>Decrease in net debt in the year</b>	21	256	643

# NOTES TO THE ACCOUNTS

## 1 PRINCIPAL ACCOUNTING POLICIES

### Basis of accounting

The accounts have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules.

The principal accounting policies of the Group are set out below:

### Basis of consolidation

The Group accounts for the year ended 31 August 2004 comprise the accounts of the Company and its subsidiaries, all of which are made up to the end of the Company's financial year.

Where part of the purchase consideration for an acquisition is dependent on future profits of the acquired company or business, and can be satisfied, at the Group's option, by the issue of new shares, provision is made for the estimated future consideration and shown in the balance sheet as 'shares to be issued' in accordance with the requirement of FRS 7.

The profit and loss account for the parent Company has not been included, as permitted by Section 230 of the Companies Act 1985. The result of the Company for the financial year dealt with in the consolidated accounts is disclosed in note 19 to the accounts.

### Goodwill

Goodwill arising on acquisitions of businesses and subsidiary undertakings is calculated as the excess of the fair value of the consideration given and costs of acquisition over the fair value of the separable net assets acquired. Goodwill arising on acquisitions before 1 September 1998 was written off against reserves immediately on acquisition. In accordance with FRS 10, goodwill arising on acquisitions on or after 1 September 1998 is capitalised as an intangible fixed asset and amortised over its estimated useful economic life. The goodwill carried in the balance sheet is written off over 20 years. Goodwill previously written off directly to reserves has not been reinstated on the balance sheet, but written off against the profit and loss reserve in accordance with the transitional provisions of FRS 10.

On the subsequent disposal or termination of a previously acquired business, the profit or loss on disposal or termination is calculated after charging the amount of any related goodwill taken directly to reserves on acquisition and the net book value of any related goodwill capitalised in the balance sheet.

### Investments

Shares in subsidiary undertakings are valued at the lower of cost and recoverable amount, where recoverable amount is the higher of net realisable value and value in use. Provision is made against investments where the diminution in value is considered to be permanent.

### Depreciation

Depreciation is provided on all tangible fixed assets, except freehold land, at rates calculated to write off the cost of each asset evenly over its expected useful life. The following principal rates per annum are used:

Freehold buildings	4%
Short leasehold improvements	over the unexpired term of the lease
Tooling	50 – 100%
Fixtures, fittings and equipment	20 – 33%
Motor vehicles	20 – 25%

### Stocks

Stocks are stated at the lower of cost and net realisable value. Net realisable value is based on estimated selling price less the estimated cost of disposal.

### Factoring arrangements

Certain subsidiaries have factoring agreements under which debts approved by the factor company are assigned to them without recourse. Non-refundable advances are made by the factor company. The Company has no obligation and the directors do not intend that the company will support any losses from factored debts. A linked presentation of the relevant balances is therefore shown on the face of the balance sheet in accordance with the requirements of FRS 5. The factor company has a debenture over the assets of the Company and certain subsidiary companies. The factoring charges are charged to the profit and loss account as they accrue. The amount charged to the profit and loss in the year was £280,000 (2003: £302,000). Of this amount £107,000 (2003: £122,000) has been charged as interest (see note 5), with the remainder being charges made by the factor company which have been included within administration expenses.

## NOTES TO THE ACCOUNTS CONTINUED

### 1 PRINCIPAL ACCOUNTING POLICIES CONTINUED

#### Foreign currencies

In the accounts of individual group undertakings, transactions in foreign currencies are recorded in the local currency using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains and losses on translation are included in the profit and loss account. In the consolidated accounts, the results and the balance sheets of overseas subsidiary undertakings are translated at the year end exchange rates. Exchange differences resulting from the re-translation of opening net assets are dealt with in reserves. All other exchange differences are dealt with in the profit and loss account.

#### Leasing and hire purchase contracts

Assets held under finance leases and hire purchase contracts are capitalised in the balance sheet and are depreciated over their useful lives. The interest element of the rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding. Rentals paid under operating leases are charged to income as incurred.

#### Financial instruments

Financial assets are recognised on the balance sheet at the lower of cost and net realisable value. Discounts and premiums are charged or credited to the profit and loss account over the life of the asset or liability to which they relate. The Group has taken advantage of the exemption available for short term debtors and creditors.

#### Deferred taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Group's taxable profits and its results as stated in the accounts that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the accounts.

Deferred tax is recognised in respect of the retained earnings of overseas subsidiaries and associates only to the extent that, at the balance sheet date, dividends have been accrued as receivable or a binding agreement to distribute past earnings in future has been entered into by the subsidiary or associate.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date. Deferred tax is measured on a non-discounted basis.

#### Pension contributions

The Group operates defined contribution pension schemes. Contributions are allocated to the profit and loss account when due.

#### Research and development

Research and development costs represent expenditure that is directly attributable to the development of products, and are written off as an expense in the year incurred.

#### Prior year adjustment

UITF 38, 'Accounting for ESOP trusts' has been adopted in preparing these accounts, resulting in the transfer of the Group's investment in its own shares from fixed asset investments to shareholders funds. In accordance with UITF 38, the investment in own shares is recorded at cost.

The effect of this change in accounting policy on the profit and loss reserve of the Group and the Company is set out below.

	Group £000's	Company £000's
Profit and loss reserve as previously reported at 31 August 2003	(4,975)	1,681
Prior period adjustment	569	569
Profit and loss reserve as restated 31 August 2003	(4,406)	2,250

The prior period adjustment resulted in a reduction in the Group's reported profit for the year ended 31 August 2003 of £267,000.

## NOTES TO THE ACCOUNTS CONTINUED

### 2 TURNOVER

Turnover represents the amount derived from the provision of goods and services which arise from the Group's ordinary activities, stated net of value added tax.

Analysis of turnover by geographical market by destination	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
United Kingdom	52,347	51,781
Rest of the world	23,699	33,527
<b>Total</b>	<b>76,046</b>	<b>85,308</b>

Analysis of turnover by division	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
Toys, Games and Gifts	44,989	51,375
Digital	31,057	33,933
<b>Total</b>	<b>76,046</b>	<b>85,308</b>

All the Group's activities during the 12 months ended 31 August 2004 are classed as continuing. The directors consider that the disclosure of further disaggregated information would be seriously prejudicial to the commercial interests of the Group.

### 3 OPERATING PROFIT

	note	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
Operating profit is stated after charging:			
Staff costs	4	6,185	6,686
Auditors' remuneration			
– Statutory audit services		97	97
– Financial reporting advisory services		60	14
– Tax compliance services		8	12
– Tax advisory services		8	17
– Further assurance services		9	–
– Total fees payable to auditors		182	140
Operating leases – land and buildings		343	291
Research and development costs		1,971	1,023
Depreciation of tangible fixed assets			
– owned assets		718	975
– assets held under finance leases and HP contracts		4	4
		722	979
Goodwill amortisation		45	30

## NOTES TO THE ACCOUNTS CONTINUED

### Exceptional item

As announced on 29 November 2004, World Wide Licences Limited (“WWL”) has settled its dispute with Uniden America Corporation (“Uniden”) which commenced when Uniden terminated its distribution agreement with WWL. Under the settlement, Uniden has agreed to pay to WWL the sum of US\$4.5million by two equal instalments.

WWL has incurred substantial costs since Uniden terminated its distribution agreement. The settlement as well as the associated costs incurred have been classified as an exceptional item.

The exceptional income and costs, as set out on the face of the consolidated profit and loss account, are explained below.

Turnover is the sale of products which had to be sold elsewhere at lower prices.

Cost of sales are the costs of those products, as well as a write off of royalties paid which are unlikely to be recoverable.

Selling and distribution costs represent an additional amount of commission payable under the terms of WWL’s contract with a USA company as a consequence of the settlement.

Administration expenses comprise the legal costs incurred.

Other operating income is the settlement from Uniden.

### 4 DIRECTORS AND EMPLOYEES

	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
Staff costs including directors' emoluments		
Wages and salaries	5,377	5,856
Social security costs	477	522
Other pension costs	331	308
	<b>6,185</b>	<b>6,686</b>
The average number of employees during the year was:	Number	Number
Management and administration	81	73
Selling and distribution	149	130
	<b>230</b>	<b>203</b>

The amount payable to pension schemes as at the balance sheet date was £56,000 (2003: £88,000).

Details of directors' remuneration and share options are given in the Directors' Remuneration Report on pages 15 to 17.

### 5 INTEREST

	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
Total interest receivable	7	12
Total interest payable:		
On bank overdraft and similar charges	(296)	(222)
Convertible loan note interest	(56)	(230)
Finance leases and hire purchase contracts	(1)	(1)
Factor advances	(107)	(122)
	<b>(453)</b>	<b>(563)</b>

## NOTES TO THE ACCOUNTS CONTINUED

### 6 TAXATION

	12 months to 31 August 2004 £000's	12 months to 31 August 2003 (as restated) £000's
<b>UK Corporation Tax</b>		
Tax on profit for the period	–	–
Adjustments to tax charge in respect of previous periods	(241)	–
Total UK corporation tax	(241)	–
<b>Foreign Tax</b>		
Tax on profit for the period	444	552
Adjustments to tax charge in respect of previous periods	17	–
Total foreign tax	461	552
Total current tax	220	552
<b>Deferred Tax</b>		
Tax losses	(764)	(473)
Origination and reversal of timing differences	41	208
Total deferred tax	(723)	(265)
Tax on profit on ordinary activities	(503)	287
<b>Factors affecting tax charge for the period</b>		
Profit on ordinary activities before taxation	3,224	5,556
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2003: 30%)	967	1,667
Effects of:		
Expenses not deductible for tax purposes	301	244
Capital allowances less than/(in excess of) depreciation	16	(212)
Other temporary differences between taxable and accounting profit	162	(481)
Lower tax rate on overseas earnings	(252)	(413)
Utilisation of tax losses	(1,003)	(445)
Tax losses not utilised	253	192
Adjustments to tax charge in respect of previous periods	(224)	–
Current tax charge for the year	220	552

The deferred tax credit for the year includes a value for tax losses previously unrecognised. These losses were previously unrecognised as the Directors did not consider that there was sufficient evidence to support the recognition of a deferred tax asset. Having considered the results of the subsidiary companies for the year ended 31 August 2004, and prepared forecasts for the period ahead, the Directors are of the opinion that some of the tax losses within the Group will now be recovered against future taxable profits within a time horizon that the directors consider more likely than not to occur.

### 7 DIVIDEND

	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
On equity shares:		
Interim dividend paid – 1.1pence (2003: 1pence) per share	726	410
Final dividend proposed – 0.7pence (2003: 2pence) per share	367	900
Total	1,093	1,310

## NOTES TO THE ACCOUNTS CONTINUED

### 8 EARNINGS PER SHARE

	12 months to 31 August 2004			12 months to 31 August 2003		
	Profit after taxation	Weighted average number of ordinary shares	Pence per share	Profit after taxation	Weighted average number of ordinary shares	Pence per share
Basic earnings per share	3,727,000	49,811,576	7.48	5,269,000	41,002,909	12.85
Impact of share option schemes	–	1,190,106	(0.17)	–	1,224,118	(0.37)
Impact of convertible loan note	–	–	–	161,000	11,500,000	(2.37)
Diluted earnings per share	3,727,000	51,001,682	7.31	5,430,000	53,727,027	10.11

### 9 INTANGIBLE FIXED ASSETS - GOODWILL

#### The Group

Cost	£000's
1 September 2003 and 31 August 2004	902
<b>Amortisation</b>	
1 September 2003	165
Charge for the year	45
<b>31 August 2004</b>	<b>210</b>
<b>Net book value</b>	
<b>31 August 2004</b>	<b>692</b>
31 August 2003	737

## NOTES TO THE ACCOUNTS CONTINUED

### 10 TANGIBLE FIXED ASSETS

#### The Group

Cost	Freehold land and buildings £000's	Short leasehold improvements £000's	Tooling £000's	Fixtures fittings and equipment £000's	Motor vehicles £000's	Total £000's
1 September 2003	1,182	97	1,190	1,813	395	4,677
Additions	–	7	155	266	82	510
Disposals	–	–	–	(10)	(50)	(60)
Differences on exchange	–	(8)	(142)	(57)	–	(207)
<b>31 August 2004</b>	<b>1,182</b>	<b>96</b>	<b>1,203</b>	<b>2,012</b>	<b>427</b>	<b>4,920</b>
<b>Depreciation</b>						
1 September 2003	248	59	853	1,460	181	2,801
Charge for the year	27	24	387	200	84	722
Disposals	–	–	–	(10)	(48)	(58)
Exchange rate movement	–	(4)	(101)	(39)	–	(144)
<b>31 August 2004</b>	<b>275</b>	<b>79</b>	<b>1,139</b>	<b>1,611</b>	<b>217</b>	<b>3,321</b>
<b>Net book value</b>						
<b>31 August 2004</b>	<b>907</b>	<b>17</b>	<b>64</b>	<b>401</b>	<b>210</b>	<b>1,599</b>
31 August 2003	934	38	337	353	214	1,876

The net book value of fixed assets includes £7,000 (2003: £2,000) in respect of assets held under finance leases and hire purchase contracts, the depreciation of which is shown in note 3.

#### The Company

Cost	Freehold land and buildings £000's	Fixtures fittings and equipment £000's	Motor vehicles £000's	Total £000's
1 September 2003	1,182	130	26	1,338
Additions	–	3	–	3
Disposals	–	(10)	–	(10)
<b>31 August 2004</b>	<b>1,182</b>	<b>123</b>	<b>26</b>	<b>1,331</b>
<b>Depreciation</b>				
1 September 2003	248	74	21	343
Charge for the year	27	45	5	77
Disposals	–	(10)	–	(10)
<b>31 August 2004</b>	<b>275</b>	<b>109</b>	<b>26</b>	<b>410</b>
<b>Net book value</b>				
<b>31 August 2004</b>	<b>907</b>	<b>14</b>	<b>–</b>	<b>921</b>
31 August 2003	934	56	5	995

## NOTES TO THE ACCOUNTS CONTINUED

### 11 FIXED ASSET INVESTMENTS

#### The Group

Cost	Own shares £000's	Shares listed in the UK £000's	Total £000's
1 September 2003	908	2	910
Prior year adjustment	(908)	–	(908)
<b>1 September 2003 (as restated) and 31 August 2004</b>	<b>–</b>	<b>2</b>	<b>2</b>
<b>Amortisation and Provisions</b>			
1 September 2003	(569)	–	(569)
Prior year adjustment	569	–	569
<b>1 September 2003 (as restated) and 31 August 2004</b>	<b>–</b>	<b>–</b>	<b>–</b>
<b>Net book value</b>			
31 August 2004	–	2	2
31 August 2003 (as restated)	–	2	2

The market value of the listed investments is £1,141 (2003: £2,206).

#### The Company

Cost	Shares in subsidiary undertakings £000's	Joint venture £000's	Own shares £000's	Total £000's
1 September 2003	3,537	1	908	4,446
Prior year adjustment	–	–	(908)	(908)
<b>1 September 2003 (as restated) and 31 August 2004</b>	<b>3,537</b>	<b>1</b>	<b>–</b>	<b>3,538</b>
<b>Amortisation and Provisions</b>				
1 September 2003	(342)	(1)	(569)	(912)
Prior year adjustment	–	–	569	569
<b>1 September 2003 (as restated) and 31 August 2004</b>	<b>(342)</b>	<b>(1)</b>	<b>–</b>	<b>(343)</b>
<b>Net book value</b>				
31 August 2004	3,195	–	–	3,195
31 August 2003 - restated	3,195	–	–	3,195

### 12 STOCKS

	The Group 2004 £000's	The Group 2003 £000's
Raw materials	5,197	1,237
Finished goods for resale	7,030	6,906
	<b>12,227</b>	<b>8,143</b>

## NOTES TO THE ACCOUNTS CONTINUED

### 13 DEBTORS

	The Group 2004 £000's	The Group 2003 £000's	The Company 2004 £000's	The Company 2003 £000's
Due from subsidiary undertakings	–	–	8,984	12,770
Trade debtors (non-factored)	7,918	13,695	–	–
Other debtors	4,541	876	2	304
Prepayments and accrued income	2,093	1,456	670	166
Other taxation and social security	–	–	–	107
Deferred tax	1,472	749	–	–
	<b>16,024</b>	<b>16,776</b>	<b>9,656</b>	<b>13,347</b>

#### Deferred Tax

The elements of deferred tax are as follows:

	2004 £000's	2003 £000's
Difference between accumulated depreciation and tax depreciation	143	197
Other timing differences	(259)	(272)
Tax losses	1,588	824
	<b>1,472</b>	<b>749</b>

The movements in deferred tax are as follows:

	2004 £000's	2003 £000's
At 1 September 2003	749	484
Profit and loss account	723	265
<b>At 31 August 2004</b>	<b>1,472</b>	<b>749</b>

The deferred tax asset of £1,472,000 (2003: £749,000) is recoverable against future forecast taxable profits within a time horizon that the directors consider more likely than not to occur.

Deferred tax assets have not been recognised in respect of tax losses of £2,653,000 (2003: £5,271,000). At a tax rate of 30%, these losses represent a potential tax asset of £796,000 (2003: £1,581,000). These losses would be recoverable in the event of taxable profits arising in certain subsidiary companies.

## NOTES TO THE ACCOUNTS CONTINUED

### 14 CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	The Group 2004 £000's	The Group 2003 £000's	The Company 2004 £000's	The Company 2003 £000's
Trade creditors	14,795	17,313	–	–
Bills of exchange payable	2,670	–	–	–
Due to subsidiary undertakings	–	–	83	86
Corporation tax	617	712	–	–
Other taxation and social security	559	803	14	137
Accruals and deferred income	5,839	4,671	607	1,746
Finance leases and hire purchase contracts	4	5	–	–
Convertible loan note	–	4,600	–	4,600
	<b>24,484</b>	<b>28,104</b>	<b>704</b>	<b>6,569</b>

A bank has a debenture over the assets and undertakings of the Company and certain subsidiary companies. Also, some subsidiaries pledge cash deposits with some banks which provide mainly trade finance facilities, and such amounts are included in cash at bank and in hand. At 31 August 2004, the pledged deposits amounted to £722,000 (2003: £362,000). Further, a major trade creditor who offers trade finance is secured by a debenture over the assets and undertakings of a subsidiary company. As at 31 August 2004 the amount outstanding to the secured trade creditor amounted to £1,164,000 (2003: £1,487,000).

### 15 CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	The Group 2004 £000's	The Group 2003 £000's
<b>Other creditors</b>		
Finance leases and hire purchase contracts repayable in less than five years	–	4

### 16 RECONCILIATION OF EQUITY SHAREHOLDERS' FUNDS

	The Group 12 months to 31 August 2004 £000's	The Group 12 months to 31 August 2003 £000's	The Company 12 months to 31 August 2004 £000's	The Company 12 months to 31 August 2003 £000's
Profit/(loss) for the financial period	2,634	4,226	(1,556)	(118)
Prior year adjustment	–	(267)	–	(267)
Profit/(loss) for the financial period - as restated	2,634	3,959	(1,556)	(385)
Exchange difference taken to reserves	(541)	(185)	–	–
Movement in shares to be issued	–	(908)	–	(908)
Shares issued	4,546	–	4,546	–
Shares purchased	(121)	–	(121)	–
Net addition to/(subtraction from) shareholders funds	<b>6,518</b>	<b>2,866</b>	<b>2,869</b>	<b>(1,293)</b>
Opening shareholders' funds	5,598	2,465	11,603	12,629
Prior year adjustment	(339)	(72)	(339)	(72)
Opening shareholders' funds - restated	5,259	2,393	11,264	12,557
Closing shareholders' funds	<b>11,777</b>	<b>5,259</b>	<b>14,133</b>	<b>11,264</b>

**17 CALLED UP SHARE CAPITAL (EQUITY)**

	2004 £000's	2003 £000's
<b>Authorised</b>		
110,000,000 (2003: 110,000,000) ordinary shares of 5 pence each	5,500	5,500
<b>Allotted called up and fully paid</b>		
52,687,909 (2003: 41,287,909) ordinary shares of 5 pence each	2,634	2,064

**Share Capital movements in the year**

During the year 11,500,000 ordinary shares of 5 pence each (total nominal value £575,000) were issued as a result of the exercise of rights of conversion of a loan note. The conversion price was 40 pence per share.

25,000 ordinary shares of 5 pence each (total nominal value of £1,250) were also issued during the year, at a price of 24.25 pence per share, to an ex-employee on exercise of his share options.

During the year, a total of 125,000 ordinary shares of 5 pence each were purchased for cancellation.

Further details of changes in share capital including the share purchase by the Company of its own shares can found on page 10 in the directors' report

**Share options**

The Company adopted the rules of an Inland Revenue approved executive share option scheme on 3 May 1995.

At 1 September 2003, options to acquire up to a total of 522,000 new ordinary shares remained outstanding under this scheme. As at 31 August 2004, options to acquire up to a total of 425,000 new ordinary shares in the Company remained outstanding under this scheme details of which were as follows:

No. of shares	Date granted	Exercise period	Exercise price
24,000	5 March 1997	5 March 2000 to 4 March 2007	101.0p
18,000	5 December 1997	5 December 2000 to 4 December 2007	136.5p
383,000	15 February 2002	15 February 2005 to 14 February 2012	24.25p

The Company adopted the rules of its unapproved executive share option scheme on 2 June 1997. At 1 September 2003 options to acquire up to a total of 688,000 new ordinary shares remained outstanding under this scheme. As at 31 August 2004, options to acquire up to a total of 688,000 new ordinary shares in the Company remained outstanding under this scheme, details of which were as follows:

No. of shares	Date granted	Exercise period	Exercise price
128,500	5 December 1997	5 December 2000 to 4 December 2004*	136.5p
207,000	15 February 2002	15 February 2005 to 14 February 2009	24.25p
352,500	6 February 2003	6 February 2006 to 5 February 2010	54.0p

\*These options remain unexercised at 4 December 2004, and therefore lapsed on 5 December 2004.

The Company adopted the rules of an Inland Revenue qualifying Enterprise Management Incentive share option scheme with the sanction of shareholders following an extraordinary general meeting of the Company on 22 January 2003. On 5 February 2003, options over a total of 1,131,250 new ordinary shares in the Company were granted to Group employees at an exercise price of 54 pence per share, all of which options remained outstanding as at 1 September 2003. As at 31 August 2004, options to acquire a total of 1,071,500 new ordinary shares in the Company remained outstanding under this scheme. These options are exercisable during the period from 5 February 2006 until 4 February 2013.

No amount is payable by any grantee of an option at the time of grant under any of the Company's share option schemes.

## NOTES TO THE ACCOUNTS CONTINUED

### 18 SHARE CAPITAL AND RESERVES

	Called up share capital £000's	Capital redemption reserve £000's	Share premium account £000's	Merger reserve £000's	Profit and loss account £000's
<b>The Group</b>					
1 September 2003	2,064	15	7,843	651	(4,975)
Prior year adjustment	–	–	–	–	569
<b>1 September 2003 - as restated</b>	<b>2,064</b>	<b>15</b>	<b>7,843</b>	<b>651</b>	<b>(4,406)</b>
Exchange Differences	–	–	–	–	(541)
Profit Retained	–	–	–	–	2,634
Shares issued	576	–	3,970	–	–
Shares repurchased	(6)	25	(19)	–	(121)
<b>31 August 2004</b>	<b>2,634</b>	<b>40</b>	<b>11,794</b>	<b>651</b>	<b>(2,434)</b>
<b>The Company</b>					
1 September 2003	2,064	15	7,843	–	1,681
Prior year adjustment	–	–	–	–	569
<b>1 September 2003 - as restated</b>	<b>2,064</b>	<b>15</b>	<b>7,843</b>	<b>–</b>	<b>2,250</b>
Loss absorbed	–	–	–	–	(1,556)
Shares issued	576	–	3,970	–	–
Shares repurchased	(6)	25	(19)	–	(121)
<b>31 August 2004</b>	<b>2,634</b>	<b>40</b>	<b>11,794</b>	<b>–</b>	<b>573</b>

In accordance with FRS 10, goodwill previously written off against reserves has not been reinstated and the goodwill has been offset against the profit and loss account reserve. The cumulative amount of positive goodwill written off against reserves is £5,645,000 (31 August 2003: £5,645,000). The goodwill has been eliminated as a matter of accounting policy and would be charged to the profit and loss account on the subsequent disposal of the business to which it related.

#### The Company

At 31 August 2004 the Company held more than 10% of the equity of the following principal undertakings:

Subsidiaries	Country of incorporation and operation	Class of share capital held	Proportion held by the parent undertaking	Nature of business
Character Options Limited	United Kingdom	Ordinary	100%	Design and distribution of toys and games
Toy Options (Far East) Limited	Hong Kong	Ordinary	100%	Design and distribution of toys and games
Character Games Limited	United Kingdom	Ordinary	100%	Design and distribution of games and puzzles
Character Games (Far East) Limited	Hong Kong	Ordinary	100%	Design and distribution of games and puzzles
Downpace Limited	United Kingdom	Ordinary	100%	Gift importer and distributor
World Wide Licenses Limited	Hong Kong	Ordinary	100%	Design and distribution of digital cameras
WWL (Europe) Limited	United Kingdom	Ordinary	100%	Distribution of digital cameras

All of the subsidiary undertakings have been included in these consolidated accounts.

## NOTES TO THE ACCOUNTS CONTINUED

### 19 GUARANTEES AND OTHER FINANCIAL COMMITMENTS

a. Financial commitments under non-cancellable operating leases will result in the following payments falling due in the year to 31 August 2004

	2004 Land and buildings £000's	2003 Land and buildings £000's
Expiring within one year	121	241
Expiring between one and five years	204	225
Expiring after five years or more	–	–
	325	466

b. The Group has entered into contracts for minimum royalties in the amounts set out below which are contracted to be paid to licensors irrespective of sales and are not provided for in the accounts as the directors believe that the required level of future sales will be achieved:

	2004 £000's	2003 £000's
Within one year	1,681	1,843
Between one and two years	164	1,632
Between two and five years	–	–
	1,845	3,475

c. The future minimum hire purchase and finance lease payments to which the Group was committed at 31 August 2004 are:

	2004 £000's	2003 £000's
Net amounts payable within one year	4	5
Net amount payable between two and five years	–	4
	4	9

## NOTES TO THE ACCOUNTS CONTINUED

### 20 RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	12 months to 31 August 2004 £000's	12 months to 31 August 2003 (as restated) £000's
Operating profit	3,677	6,119
Depreciation, impairment and amortisation	767	1,009
(Profit) on disposal of fixed assets	(7)	(3)
(Increase) in stocks	(4,084)	(3,161)
Decrease/(increase) in debtors	1,843	(6,659)
Increase in creditors	1,671	6,697
Exchange movement	(541)	(185)
Net cash inflow from operating activities	3,326	3,817

### RECONCILIATION OF EXCEPTIONAL PROFIT TO NET CASH OUTFLOW FROM EXCEPTIONAL ACTIVITIES

	12 months to 31 August 2004 £000's
Exceptional profit	492
Increase in debtor	(2,504)
Increase in creditors	926
Net cash outflow from operating activities	(1,086)

There was no cash flow relating to taxation in respect of the exceptional items.

### 21 RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT

	12 months to 31 August 2004 £000's	12 months to 31 August 2003 £000's
Increase in cash in the period	251	648
Cash inflow/(outflow) from movement in debt and lease financing	5	(5)
Movement in net debt resulting from cash flows	256	643
Net debt at 1 September 2003	3,923	3,280
Net debt at 31 August 2004	4,179	3,923

### 22 ANALYSIS OF NET DEBT

	Cash at bank and in hand £000's	Lease finance £000's	Total £000's
1 September 2002	3,284	(4)	3,280
Cash flow	648	(5)	643
31 August 2003	3,932	(9)	3,923
Cash flow	251	5	256
31 August 2004	4,183	(4)	4,179

## NOTES TO THE ACCOUNTS CONTINUED

### 23 FINANCIAL INSTRUMENTS

The Group's use of financial instruments is explained under the heading of 'Risk Management' in The Corporate Governance Statement starting on page 12. As permitted by FRS 13 short term debtors and creditors have been excluded from all financial instrument disclosures.

#### a. Exchange risk

The tables below show the Group's currency exposures; in other words those transactional exposures that give rise to the net currency gains and losses recognised in the profit and loss account. Such exposures comprise the monetary assets and monetary liabilities of the Group that are not denominated in the operating currency of the operating company involved.

These currency exposures were as follows:

Net foreign currency monetary assets	At 31 August 2004			At 31 August 2003		
	Functional currency of group operation			Functional currency of group operation		
	Sterling £000's	HK\$ £000's	Total £000's	Sterling £000's	HK\$ £000's	Total £000's
Sterling	–	5	5	–	7	7
US\$	700	1,280	1,980	(117)	988	871
Euro	(43)	–	(43)	15	–	15
Total	657	1,285	1,942	(102)	995	893

#### b. Fair values

The fair value of all financial instruments at 31 August 2004 and 31 August 2003 was not materially different from their book value

#### c. Maturity of financial liabilities

The maturity profile of the Group's financial liabilities at 31 August 2004 was as follows:

	2004 £000's	2003 £000's
In one year or less, or on demand	4	4,600
In more than one year, but not more than two years	–	4
In more than two years, but not more than five years	–	–
In more than five years	–	–
Total	4	4,604

#### d. Borrowing facilities

The Group has various available borrowing facilities. The undrawn committed facilities available in respect of which all conditions had been met at 31 August 2004, were as follows:

	2004 £000's	2003 £000's
Expiring within one year	1,523	1,860
Expiring between one year, but not more than two years	–	–
Expiring in more than two years	–	–
Total	1,523	1,860

## NOTES TO THE ACCOUNTS CONTINUED

### 23 FINANCIAL INSTRUMENTS CONTINUED

#### e. Interest rate risk profile of financial assets and financial liabilities

##### Financial assets

Financial assets comprise cash at bank.

Currency	At 31 August 2004			Total £000's	At 31 August 2003			Total £000's
	Floating rate financial assets £000's	Fixed rate financial assets £000's	Financial assets on which no interest received £000's		Floating rate financial assets £000's	Fixed rate financial assets £000's	Financial assets on which no interest received £000's	
Sterling	2,386	–	–	2,386	2,043	–	–	2,043
US\$	1,980	–	–	1,980	871	–	–	871
Euro	–	–	–	–	15	–	–	15
HK\$	–	–	–	–	1,003	–	–	1,003
<b>Total</b>	<b>4,366</b>	<b>–</b>	<b>–</b>	<b>4,366</b>	<b>3,932</b>	<b>–</b>	<b>–</b>	<b>3,932</b>

##### Financial liabilities

Currency	At 31 August 2004			Total £000's	At 31 August 2003			Total £000's
	Floating rate financial liabilities £000's	Fixed rate financial liabilities £000's	Financial liabilities on which no interest is paid £000's		Floating rate financial liabilities £000's	Fixed rate financial liabilities £000's	Financial liabilities on which no interest is paid £000's	
Sterling	–	–	–	–	–	4,600	–	4,600
Euro	43	–	–	43	–	–	–	–
HK\$	140	4	–	144	–	4	–	4
<b>Total</b>	<b>183</b>	<b>4</b>	<b>–</b>	<b>187</b>	<b>–</b>	<b>4,604</b>	<b>–</b>	<b>4,604</b>

The floating rate financial liabilities comprise:

- Sterling denominated bank borrowings and overdrafts that bear interest at rates based on LIBOR or NatWest bank base rates.
- Obligations under finance leases and hire purchase contracts.

### 24 THE CHARACTER GROUP PLC EMPLOYEE SHARE OWNERSHIP TRUST

The Company's Employee Share Ownership Trust ("the Trust") is governed by a Trust Deed dated 19 June 1998. The Trustees may grant options over such shares in the Company acquired by them or otherwise provide benefits to the beneficiaries, as defined in the Trust Deed. The Trust is required to meet its own costs out of the trust fund but if such fund is insufficient such costs will be borne by the Company. At 31 August 2004 the Trust held 285,000 shares (2003:285,000) which had a market value of £142,500 (2003: £339,000), and has waived its right to dividend income thereon. The cost of these shares was £908,000. At 31 August 2004, no options had been granted by the Trust.

### 25 CONTINGENT LIABILITIES

The Company has guaranteed the obligations of certain subsidiary companies to their factor companies, trade finance companies, certain banks and others in the normal course of business. The factor company has a fixed and floating charge over the assets of the Company and some subsidiaries. The Company is a member of a Group registration for Value Added Tax purposes.

### 26 RELATED PARTY TRANSACTIONS

During the year the Company entered into transactions with Giochi Preziosi S.p.A., a company of which E Preziosi is a director. Giochi Preziosi S.p.A. held approximately 22.6% of the issued share capital of The Character Group plc at 31 August 2004.

Trade was carried out on an arms length basis and is summarised below:

	2004 £000's	2003 £000's
Total net sales to Giochi Preziosi S.p.A.	1,756	1,374
Total net purchases from Giochi Preziosi S.p.A.	1,103	2,862
Balance due from Giochi Preziosi S.p.A.	928	175

## NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the tenth Annual General Meeting of The Character Group plc will be held at 26 Finsbury Square, London EC2A 1DS on 19 January 2005 at 10 a.m. to transact the following business:

### Ordinary business

- 1 To approve the Directors' Remuneration Report for the year ended 31 August 2004.
- 2 To receive and adopt the directors' report and the accounts of the Company for the year ended 31 August 2004 and the report of the auditors thereon.
3. To declare a final dividend on the ordinary shares in the capital of the Company for the year ended 31 August 2004 of 0.7 pence per share.
- 4 To re-elect Lord Birdwood, who retires in accordance with the terms of his appointment, as a director of the Company.
- 5 To re-elect Mr I S Fenn, who retires in accordance with the terms of his appointment, as a director of the Company.
- 6 To re-elect Mr A G Horvat, who retires in accordance with the terms of his appointment, as a director of the Company.
- 7 To re-appoint Mr D Harris, who retires in accordance with the terms of his appointment, as as director of the Company.
- 8 To re-appoint Baker Tilly as auditors of the Company to hold office from the conclusion of this meeting until the conclusion of the next Annual General Meeting at which accounts are laid before the Company and to authorise the directors to fix their remuneration.

### Special business

To consider and, if thought fit, pass the following resolutions which in the cases of resolutions numbered 9, 10 and 11 will be proposed as ordinary resolutions of the Company and in the case of resolution numbered 12 shall be proposed as a special resolution of the Company:

- 9 That for the purposes of Section 80 of the Companies Act 1985 (the "Act") the directors be and are hereby generally and unconditionally authorised to exercise all powers of the Company to allot relevant securities (as defined in that section) up to an aggregate nominal amount of £878,130 such authority to expire on the earlier of fifteen months following the date upon which this resolution was passed and the conclusion of the Annual General Meeting of the Company next following the date upon which this resolution was passed unless renewed, varied or revoked by the Company in general meeting provided that the Company may at any time before the expiry, variation or revocation of such authority make offers or agreements which will or might require relevant securities to be allotted after the expiry, variation or revocation of such authority and the directors may allot relevant securities pursuant to such offer or agreement as if such authority had not expired or been varied or revoked. This authority shall replace all existing authorities conferred on the directors in respect of the allotment of relevant securities to the extent that the same have not previously been utilised.
- 10 That the directors be and are hereby authorised for the purposes of Article 147 of the Articles of Association of the Company, to offer to members of the Company, in accordance with the provisions of the said Article, the right to elect to receive ordinary shares, credited as fully paid, in whole or in part instead of cash in respect of all or any dividends declared or paid by the Company or the directors pursuant to the Articles of Association of the Company at any time after the date of the passing of this resolution was passed and the conclusion of the Annual General Meeting of the Company next following the date upon which this resolution was passed and that the directors be and are hereby authorised to make any such offer on such terms and conditions to such members of the Company, subject always to the provisions of the Articles of Association of the Company, as they shall in their absolute discretion determine.
- 11 That the Company be and is hereby generally and unconditionally authorised for the purposes of section 166 of the Act to make market purchases (as defined in section 163(3) of the Act) of ordinary shares of 5p each in the capital of the Company provided that:
  - (A) the maximum number of ordinary shares 5p each in the capital of the Company hereby authorised to be acquired 7,903,180;
  - (B) the minimum price (exclusive of all expenses) which may be paid for such shares is 5p per share;
  - (C) the maximum price which may be paid for such shares is, in respect of a share contracted to be purchased on any day, an amount equal to 105 per cent of the average of the middle-market prices shown in the quotations for ordinary shares of the Company in the Daily Official List of the London Stock Exchange on the five business days immediately preceding the day on which the share is contracted to be purchased;

## NOTICE OF ANNUAL GENERAL MEETING CONTINUED

- (D) the authority hereby conferred shall expire at the earlier of the conclusion of the next Annual General Meeting following the date upon which this resolution was passed, or 15 months following the date upon which this resolution was passed; and
- (E) the Company may contract to purchase its own shares under the authority hereby conferred prior to the expiry of such authority, which will or may be executed wholly or partly after the expiry of such authority, and may make a purchase of its own shares in pursuance of any such contract.

### 12 That:

- (A) the directors be and are hereby empowered pursuant to Section 95 of the Companies Act 1985 ("the Act") to allot equity securities (as defined in Section 94 of the Act) pursuant to the authority conferred on them for the purposes of Section 80 of the Act by an ordinary resolution of the Company of even date herewith as if Section 89(1) of the Act did not apply to any such allotment, provided that this power shall be limited:
  - (i) to the allotment of equity securities in connection with any offer by way of rights to holders of ordinary shares in the capital of the Company notwithstanding that, by reason of such exclusions or other arrangements as the directors may deem necessary or desirable to deal with legal or other problems arising in any overseas territory, in connection with fractional entitlements, record dates or otherwise howsoever, the equity securities to be allotted are not offered to all such holders in proportion to the respective number of ordinary shares held by them;
  - (ii) the allotment (otherwise than pursuant to paragraphs (i) and (ii) above) of equity securities up to an aggregate nominal value of £131,710 (being approximately 5% of the nominal value of the issued ordinary share capital of the Company as at 31 August 2004);
- (B) the power hereby conferred shall expire at the earlier of the conclusion of the next Annual General Meeting following the date on which this resolution was passed or fifteen months following the date upon which this resolution was passed;
- (C) the power hereby conferred shall enable the Company to make an offer or agreement that would or might require equity securities to be allotted after such power expires and the directors may allot equity securities in pursuance of any such offer or agreement made within the limits prescribed in paragraph (A) above as if the power hereby conferred had not expired; and
- (D) this power shall replace all existing powers granted to the directors to allot equity securities as if the said Section 89(1) of the Act did not apply to the extent that the same have not been previously utilised.

### Other business

13 To transact any other business which may lawfully be transacted at the Annual General Meeting.

By order of the Board

**K P Shah** FCCA, Secretary  
22 December 2004

Registered Office

5th Floor  
4 Chiswell Street  
London EC1Y 4UP

## NOTICE OF ANNUAL GENERAL MEETING CONTINUED

### Notes:

1. The register of directors' interests and copies of the directors' service agreements will be available for inspection at the registered office during normal business hours from the date of this notice until the date of the Annual General Meeting and on that day will be available for inspection at the place of the meeting from 9 a.m. until the conclusion of the meeting.
2. A member entitled to attend and vote at the Annual General Meeting convened by the Notice above is entitled to appoint a proxy to attend and, on a poll, vote in his place. A proxy need not be a member of the Company.
3. To be valid, forms of proxy must be lodged with Neville Registrars Limited, 18 Laurel Lane, Halesowen, West Midlands, B63 3DA not less than 48 hours before the time appointed for holding the Annual General Meeting. A form of proxy is set out on page 43.
4. Completion of a form of proxy does not prevent a member from attending and voting at the Annual General Meeting should he or she so wish.
5. In order to have the right to attend and vote at the Annual General Meeting, a person must be entered on the register of members at 5.00 pm on 17 January 2005 or, in the case of an adjournment of the Annual General Meeting, at the time which is 48 hours before the time appointed for the adjourned meeting.

# FORM OF PROXY

## THE CHARACTER GROUP PLC

For use at the Annual General Meeting of the Company on 19 January 2005

I/We \_\_\_\_\_  
(please use block capitals)

of \_\_\_\_\_ (being (a)  
holders(s) of ordinary shares in the above named company) hereby appoint the Chairman of the meeting

\_\_\_\_\_ (note 1)

as my/our proxy to vote on my/our behalf at the Annual General Meeting to be held at the offices of Citigate Dewe Rogerson, 26 Finsbury Square, London EC2A 1DS on 19 January 2005 at 10 a.m. and any adjournment thereof.

Please indicate with a ✓ in the spaces below in either the for or against column how you wish your vote to be cast.

	FOR	AGAINST
1. Ordinary resolution – approval of the Directors’ Remuneration Report		
2. Ordinary resolution – adoption of accounts for year ended 31 August 2004		
3. Ordinary resolution – declaration of final dividend of 0.7p per share		
4. Ordinary resolution – re-election of Lord Birdwood as a director		
5. Ordinary resolution – re-election of Mr I S Fenn as a director		
6. Ordinary resolution – re-election Mr A G Horvat as a director		
7. Ordinary resolution – re-appointment of Mr D Harris as a director		
8. Ordinary resolution – re-appointment of Baker Tilly as auditors		
9. Ordinary resolution – authority to allot shares		
10. Ordinary resolution – authority to allot shares in lieu of cash dividends		
11. Ordinary resolution – authority to purchase own shares in the market		
12. Special resolution – disapplication of pre-emption rights		

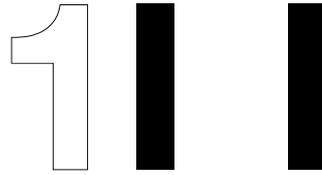
Dated \_\_\_\_\_ Signature \_\_\_\_\_

### Notes:

- You may if you wish delete the words “Chairman of the meeting” and insert the name of the proxy or proxies of your choice in the space provided. Please initial such alteration.
- If no indication is given as to how you wish your proxy to vote, your proxy will vote or abstain as he/she thinks fit. On any other business arising at the meeting (including any motion to adjourn the meeting) the proxy will act at his/her discretion.
- In the case of joint holders, the signature of any one of them will be accepted but the signature of the senior of the joint holders shall be accepted to the exclusion of the others, seniority being determined by the order in which the names appear in the register of members of the Company.
- In the case of a corporation, this Form of Proxy should be executed under its common seal or under the hand of an officer, attorney of other person duly authorised on its behalf.
- Forms of Proxy signed by other than the registered holder will not be valid unless accompanied by the power of attorney (if any) or other authority under which it is signed or a notarially certified copy thereof.
- To be effective, Forms of Proxy must be lodged with Neville Registrars Limited, 18 Laurel Lane, Halesowen, West Midlands, B63 3BR not less than 48 hours before the time appointed for the meeting. Completion of this form of proxy will not prevent the holder from attending and voting at the meeting in person should he so wish.
- As permitted by Regulation 41 of the Uncertificated Securities Regulations 2001, members must be entered on the Company’s register of members at 5 pm on 17 January 2005 in order to be entitled to attend and/or vote at the meeting in respect of the number of shares registered in their name at such time. Changes to entries on the register of members after that time will be disregarded in determining the rights of any person to attend and/or vote at the meeting.

SECOND FOLD

BUSINESS REPLY SERVICE  
Licence No: 3865



Neville Registrars Limited  
18 Laurel Lane  
Halesowen  
West Midlands  
B63 3BR

FIRST FOLD

THIRD FOLD, THEN TUCK IN FLAP & TAPE ALONG EDGE

