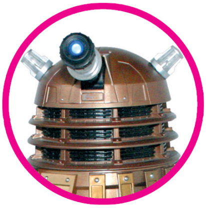
the
CHARACTER
group plc

Interim Report
six months ended
28 February 2006



DIRECTORS AND ADVISORS

Directors
R King
K P Shah
J J P Kissane
J J Diver
I S Fenn
Lord Birdwood
A G Horvat
D Harris

Secretary
K P Shah FCCA

Company registration number
3033333

Registered office
35th Floor
4 Chiswell Street
London EC1Y 4UP

Solicitors
Duane Morris
5th Floor
4 Chiswell Street
London EC1Y 4UP

Auditors
HLB Vantis Audit plc
82 St. John Street
London EC1M 4JN

Stockbrokers
Charles Stanley Securities
25 Luke Street
London EC2A 4AR

Bankers
National Westminster Bank plc
Standard Chartered Bank plc
The Hongkong and Shanghai Banking
Corporation Limited
Banca Nazionale del Lavoro S.p.A.

Registrars
Neville Registrars Limited
Neville House
18 Laurel Lane
Halesowen
West Midlands B63 3DA

CONTENTS

www.thecharacter.com

HIGHLIGHTS

- Continuing business (Toys, Games and Gifts)

	6 months to 28 February 2006 £m	6 months to 28 February 2005 £m	
Turnover	**40.7**	27.2	+50%
Operating profit	**3.7**	(1.0)	
Earnings per share	**5.69p**	(2.45p)	

- Dividend

1.65 pence, up from 1.1 pence (an increase of 50%)

- Group results (including discontinued operation)

	6 months to 28 February 2006 £m	6 months to 28 February 2005 £m	
Turnover	**66.6**	43.4	+53%
Operating profit	**1.1**	(1.5)	
Profit before tax	**3.0**	(1.9)	
Earnings per share	**5.04p**	(3.8p)	

- Cash at bank

£10.3 million, up from £3.9 million (an increase of 164%)

- Approaches regarding possible offers terminated.

Introduction

During the first six months of the current financial year the Group underwent a major reorganisation with the disposal of its Digital Business in February 2006.

The structure of the Group is now designed to maximise the strength of, and focus on, the core business of Toys, Games and Gifts. This core business, which now is our sole area of trading, has made very substantial progress, both operationally and in terms of sales.

We are aware that the Group is operating in, and expects to continue to operate in, a very competitive marketplace where our product offering is all important. We are delighted that not only is the Group's current portfolio of products seen to be our strongest for some time but we also have strong products in the pipeline for introduction later in this, as well the next, financial year and we look forward to achieving further successful trading and growth.

Your Directors are pleased to be able to report that the operating profit of the on-going business for the period to 28 February 2006 was £3.7 million, against a £1.0 million loss for the comparable period last year. This was achieved on turnover up nearly 50% from £27.2 million to over £40.7 million.

We believe that this excellent improvement in sales and profitability bodes well for the future of the Group.

Financials for the six months ended 28 February 2006

In the six months ended 28 February 2006, Group revenues, including discontinued activities, were up 53% to £66.6 million (2005: £43.4 million), resulting in an operating profit of £1.1 million, compared to a loss of £1.5 million in 2005. Profit before taxation, including the exceptional item relating to the disposal of the Digital Business, was £3.0 million (2005: £1.9 million loss).

Revenues on a like-for-like basis from our continuing business were £40.7 million, (2005: £27.2 million) producing an operating profit of £3.7 million, a significant turnaround from the operating losses of £1.0 million in the comparable 2005 period.

Revenues from the Digital Business in the period were £25.9 million (2005: £16.2 million), whilst this division's operating losses amounted to £2.6 million, compared with a £0.6 million loss last time.

Basic earnings per share amounted to 5.04 pence, against a loss per share of 3.8 pence in 2005.

Adjusted earnings per share related to the on-going business are 5.69 pence, against a loss of 2.45 pence in 2005.

Cash at bank on 28 February was £10.3 million (2005: £3.9 million).

Dividend

In view of the Board's confidence in the future direction of the Group, the Directors are declaring an interim dividend of 1.65 pence (2005: 1.10 pence), an increase of 50%. This dividend is covered 3 times by earnings.

The interim dividend will be paid on 28 July 2006, to shareholders on the Register as at 7 July 2006. The shares go ex-dividend on 5 July 2006.

Business Overview for the six months ended 28 February 2006

Digital Business

Our Digital Business operated in a highly competitive environment and since the expiry of the Polaroid licence agreements last year, this business had become even higher risk and cash intensive. As a result, the Board looked at a number of opportunities for this operation and concluded that a larger specialist player in the electronics sector would be better placed to take it to the next level in its development.

On 17 February 2006, the Group completed the sale of the digital products division based in Hong Kong of World Wide Licenses Limited ("WWL") and related assets (the "Digital Business") to Flextronics Sales and Marketing (A-P) Limited ("Flextronics"). The total sale price was approximately US$17.98 million (£10.3 million), of which approximately US$1.8 million (£1.0 million) has been retained by Flextronics until the first anniversary of completion as security in respect of any warranty or indemnity claims against WWL.

Due to the higher than expected write-down of non-current inventory of finished goods and parts (approximately £3.4 million) not included in the digital sale agreement, the out-turn of all aspects of the sale of the digital business was disappointing. In addition, the digital management team was heavily involved in the sale process and, as a consequence, trading had deteriorated severely during the extended negotiating period, which impacted on the Group's result from this operation for this period.

The exceptional gain of £2.4 million from the disposal of the Digital Business is after charging previously written-off goodwill of £1.9 million in accordance with FRS10. This goodwill charge has been made to the profit and loss account and has no negative impact on the Group's reserves. Whilst in profit terms the return was disappointing, I am pleased to report that, in cash flow terms, the disposal has had a very positive effect on the Group, which is now in a stronger position to finance its expected growth, with the net effect of the disposal being an increase in net assets of £4.3 million.

The sale of the Digital Business will allow the Group to focus entirely upon the development of its Toys, Games and Gifts business.

Toy, Games and Gifts Business

The results from the on-going Toys, Games and Gifts business have been very positive and follow the strong sales of our product ranges in the 2005 Christmas trading period. It is pleasing to note that, according to NPD Group, Character Options had the Number 1 and 2 best selling toys in December, namely ***The Dalek*** from Dr Who and the ***Roboraptor*** from our robotic range.

The reaction from our customers to our current product ranges continues to be very encouraging and we expect that trading will prove to be exciting for the financial year as a whole and will continue through Christmas 2006, thereby providing a solid foundation to deliver good prospects for growth both for this and the next financial year.

Notable new products which we expect to perform strongly, include:

- ***Dr Who*** – products based on the new series, including the much awaited Cyberman;
- ***Roboreptile*** – following on this year from the very successful Roboraptor;
- ***Scooby Doo*** – where we have a European licence;
- ***Superman Returns*** – toys based on the new film to be released in July 2006;
- ***Pirates of the Caribbean 2*** – a race set and vehicles based on the new film, which is also to be released in July 2006;
- ***Biker Mice From Mars*** – which, will have the debut of its new series on GMTV this August;
- ***Disney Princess*** – which will be supported by a DVD release featuring the popular character theme ***Ariel*** in October 2006;
- ***Carol Vorderman*** – further Sudoku products endorsed under licence;
- ***Peppa Pig*** – as seen on both Nick Junior and Channel 5.

In addition, we have recently re-launched ***Trolls***, where we have both a European and Australian licence, as well as building our in-house developed brands, including ***Gr8 Gear Kit*** and our ranges of games.

The Group continues to have a presence in Hong Kong, which, together with its recently established facilities in Shenzhen, China, will allow the Group to continue the growth of its Toys, Games and Gifts business.

Termination of Third Party approaches

On 15 February 2006, the Group announced that it had received approaches which may or may not lead to an offer or offers being made for the Company. Discussions are no longer on-going but the Board will keep shareholders informed of any future developments.

Pursuant to the Company having been authorised to purchase back up to 25% of its issued shares at the AGM in February, the Directors will consider a buy-back of shares at an appropriate time or times where it is felt that it would be in the interests of the Company and shareholders in general.

Summary

The Board is delighted with the progress made by the remaining core business and, providing we see no further erosion in economic confidence generally and, in particular, in the retail sector, we see no reason why the Group's excellent recent progress will not be maintained

Richard King
Chairman

26 April 2006

CONSOLIDATED PROFIT AND LOSS ACCOUNT

	Notes	6 months to 28 February 2006 (unaudited) £'000	6 months to 28 February 2005 (unaudited) restated (note 1) £'000	12 months to 31 August 2005 (audited) restated (note 1) £'000
Turnover – continuing		40,718	27,201	48,670
– discontinued		25,851	16,162	50,121
		66,569	43,363	98,791
Cost of sales		(49,735)	(31,932)	(75,110)
Gross profit		16,834	11,431	23,681
Net operating expenses				
Selling and distribution costs		(7,477)	(6,123)	(9,750)
Administration expenses		(8,468)	(6,922)	(12,867)
Administration expenses – exceptional		—	—	(643)
Other operating income		204	89	443
Operating profit/(loss) – continuing		3,667	(955)	(511)
– discontinued		(2,574)	(570)	1,375
Operating profit/(loss)		1,093	(1,525)	864
Exceptional item – discontinued activity	1			
Gain before goodwill write back		4,300	—	—
Goodwill charge		(1,897)	—	—
		2,403	—	—
Profit/(loss) on ordinary activities before interest		3,496	(1,525)	864
Interest		(538)	(405)	(703)
Profit/(loss) on ordinary activities before taxation		2,958	(1,930)	161
Taxation	2	(308)	(64)	(365)
Profit/(loss) on ordinary activities after taxation		2,650	(1,994)	(204)
Earnings/(loss) per share	5			
basic – continuing		5.69p	(2.45p)	(2.11p)
– discontinued		(0.65p)	(1.35p)	1.72p
		5.04p	(3.80p)	(0.39p)
– fully diluted		4.91p	(3.80p)	(0.39p)
Dividend per share		1.65p	1.10p	2.0p
EBITDA (earnings before interest, tax, depreciation and amortisation)		3,888	(1,245)	1,492

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

	6 months to 28 February 2006 (unaudited) £'000	6 months to 28 February 2005 (unaudited) £'000	12 months to 31 August 2005 (audited) £'000
Profit/(loss) for the financial period	**2,650**	(1,994)	(204)
Write back of goodwill previously written off	**1,897**	—	—
Foreign exchange differences	**122**	(383)	(64)
Total recognised gains and losses relating to the financial period	**4,669**	(2,377)	(268)

CONSOLIDATED BALANCE SHEET

	Note	28 February 2006 (unaudited) £'000	28 February 2005 (unaudited) £'000	31 August 2005 (audited) £'000
Fixed assets				
Intangible assets		**624**	669	646
Tangible assets		**1,553**	1,680	1,849
Investments		**2**	2	2
		2,179	2,351	2,497
Current assets				
Stocks		**8,667**	8,923	9,810
Trade debtors subject to finance arrangements		**5,223**	4,297	9,053
Factor advances		**(3,685)**	(3,778)	(6,937)
		1,538	519	2,116
Trade and other debtors		**8,155**	8,291	21,803
Cash at bank and in hand		**10,298**	3,901	3,748
		28,658	21,634	37,477
Creditors: amounts falling due within one year		**(15,675)**	(14,553)	(29,009)
Net current assets		**12,983**	7,081	8,468
Total assets less current liabilities		**15,162**	9,432	10,965
Net assets		**15,162**	9,432	10,965
Capital and reserves				
Called up share capital		**2,642**	2,641	2,641
Investment in own shares		**(908)**	(908)	(908)
Capital redemption reserve		**40**	40	40
Share premium account		**11,821**	11,819	11,821
Merger reserve		**651**	651	651
Profit and loss account	3	**916**	(4,811)	(3,280)
Equity shareholders' funds		**15,162**	9,432	10,965

CONSOLIDATED CASH FLOW STATEMENT

	Notes	6 months to 28 February 2006 (unaudited) £'000	6 months to 28 February 2005 (unaudited) £'000	12 months to 31 August 2005 (audited) £'000
Cash flow from operating activities	6	4,101	1,486	2,870
Returns on investment and servicing of finance				
Interest paid (net)		(538)	(405)	(703)
Net cash outflow for returns on investments and servicing of finance		(538)	(405)	(703)
Taxation		(458)	(678)	(844)
Capital expenditure and financial investment				
Payments to acquire tangible fixed assets		(658)	(376)	(868)
Sale of tangible fixed assets		432	28	25
Net cash outflow for capital expenditure and financial investment		(226)	(348)	(843)
Acquisitions and disposals				
Sale of business – exceptional item		4,143	—	—
Equity dividend paid		(473)	(367)	(945)
Cash inflow/(outflow) before use of liquid resources and financing		6,549	(312)	(465)
Issue of new shares		1	32	34
Capital element of finance lease rentals		—	(2)	(4)
Net cash inflow from financing		1	30	30
Increase/(decrease) in cash in the period	7	6,550	(282)	(435)
Decrease/(increase) in net debt in the period	8	6,550	(280)	(431)

NOTES TO THE ACCOUNTS

1 BASIS OF PREPARATION

The financial information for the six months ended 28 February 2006 has not been audited, nor has the financial information for the six months ended 28 February 2005. However, the interim report includes a review report signed by the auditors. The comparative figures for the year ended 31 August 2005 do not constitute the company's statutory accounts for that year, but have been extracted from the statutory accounts filed with the Registrar of Companies, and which carried an unqualified audit report. The report has been prepared in accordance with the applicable accounting standards on a consistent basis using the accounting policies set out in the 2005 Annual Report.

The Company has adopted Financial Reporting Standard 21 'Events after the balance sheet date' for the results to 28 February 2006. As a result of this, dividends declared for an accounting period after the balance sheet date are no longer recognised as a liability at that balance sheet date.

Profit and loss reserves as at 31 August 2004 have been restated from (£2,434,000) by the value of the final dividend proposed for the year of £367,000 resulting in restated reserves of (£2,067,000).

The dividend recognised in the results for the six months to 28 February 2005 is restated to be the final dividend declared and paid for the year ended 31 August 2004 of £367,000 and profit and loss reserves are restated accordingly (note 3).

The dividend recognised in the results for the year ended 31 August 2005 is restated to be the final dividend declared and paid for the year ended 31 August 2004 of £367,000 together with the interim dividend declared and paid for the six months ended 28 February 2005 of £578,000 and profit and loss reserves have been restated accordingly (note 3).

The dividend recognised in the results for the six months ended 28 February 2006 is the final dividend declared and paid for the year ended 31 August 2005 of £473,000. The dividend for the six months ended 28 February 2006 has been declared after the balance sheet date and is disclosed in note 4.

EXCEPTIONAL ITEM

The exceptional gain of £2,403,000 is stated after charging goodwill previously written off of £1,897,000 and associated costs on the termination of the digital operation amounting to £4,885,000. The goodwill charge is an accounting entry required by FRS 10, Goodwill and intangible assets, and a corresponding amount has been credited to profit and loss account reserves.

NOTES TO THE ACCOUNTS

CONTINUED

2 TAXATION

The tax charge for the half year is estimated on the basis of the anticipated tax rates applying for the full year.

3 PROFIT AND LOSS ACCOUNT

	£'000
At 1 September 2005 as previously reported	(3,753)
Final dividend proposed for the year ended 31 August 2005	473
At 1 September 2005 restated	(3,280)
Write back of goodwill previously written off	1,897
Exchange difference	122
Profit after tax for the period	2,650
Dividends	(473)
At 28 February 2006	916

The profit and loss account for prior periods is restated in accordance with FRS 21 as follows:

	6 months ended 28 February 2005 (unaudited) £'000	12 months ended 31 August 2005 (audited) £'000
At 1 September 2004 as previously reported	(2,434)	(2,434)
Final dividend proposed for the year ended 31 August 2004	367	367
At 1 September 2004 restated	(2,067)	(2,067)
Exchange difference	(383)	(64)
Deficit for the period	(2,361)	(1,149)
Profit and loss account restated	(4,811)	(3,280)

4 DIVIDENDS

The interim dividend declared for the six months ended 28 February 2006 is 1.65p per ordinary share and is expected to be paid on 28 July 2006 to those shareholders on the register at the close of business on 7 July 2006. This dividend was declared after 28 February 2006 and the liability of £867,000 has not been recognised in the interim results in accordance with FRS21 (note 1).

The interim dividend paid for the six months ended 28 February 2005 was 1.1p per ordinary share and the final dividend paid for the year ended 31 August 2005 was 0.9p per ordinary share making a total of 2.0p per ordinary share.

5 EARNINGS PER SHARE

Earnings per share have been calculated in accordance with FRS 14 Earnings per share.

The calculations are based on the following:

	Profit/ (loss) after taxation £	Weighted average number of ordinary shares	Pence per share
	6 months to 28 February 2006		
Basic earnings per share	2,650,000	52,543,290	5.04
Impact of share options	—	1,406,700	(0.13)
Diluted earnings per share	2,650,000	53,949,990	4.91
	6 months to 28 February 2005		
Basic earnings per share	(1,994,000)	52,407,183	(3.80)
Diluted earnings per share	(1,994,000)	52,407,183	(3.80)
	12 months to 31 August 2005		
Basic earnings per share	(204,000)	52,475,156	(0.39)
Diluted earnings per share	(204,000)	52,475,156	(0.39)

6 RECONCILIATION OF OPERATING PROFIT/(LOSS) TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	6 months to 28 February 2006 (unaudited) £'000	6 months to 28 February 2005 (unaudited) £'000	12 months to 31 August 2005 (audited) £'000
Operating profit/(loss)	**1,093**	(1,525)	864
Depreciation, impairment and amortisation	**392**	280	628
Loss on disposal of tangible fixed assets	**161**	7	11
Decrease in stocks	**1,143**	3,304	2,417
Decrease in debtors	**15,260**	8,755	(6,347)
(Decrease) in creditors	**(14,070)**	(8,952)	5,361
Exchange differences	**122**	(383)	(64)
Net cash inflow from operating activities	**4,101**	1,486	2,870

RECONCILIATION OF EXCEPTIONAL PROFIT / (LOSS) TO NET CASH INFLOW FROM EXCEPTIONAL ITEM

	6 months to 28 February 2006 (unaudited) £'000	6 months to 28 February 2005 (unaudited) £'000	12 months to 31 August 2005 (audited) £'000
Exceptional profit/(loss)	**2,403**	—	(643)
Write back of goodwill previously written off	**1,897**	—	—
(Increase)/Decrease in debtor	**(1,027)**	—	2,504
Increase/(Decrease) in creditors	**870**	—	(551)
Net cash inflow from exceptional item	**4,143**	—	1,310

7 RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT

	6 months to 28 February 2006 (unaudited) £'000	6 months to 28 February 2005 (unaudited) £'000	12 months to 31 August 2005 (audited) £'000
Increase/(decrease) in cash in the period	**6,550**	(282)	(435)
Cash inflow from movement in debt and lease financing	**—**	2	4
Movement in net debt resulting from cash flows	**6,550**	(280)	(431)
Net debt at 1 September 2005	**3,748**	4,179	4,179
Net debt at 28 February 2006	**10,298**	3,899	3,748

8 ANALYSIS OF NET DEBT

	Cash at bank and in hand £'000	Lease finance £'000	Total £'000
1 September 2004	4,183	(4)	4,179
Cash flow	(282)	2	(280)
28 February 2005	3,901	(2)	3,899
Cash flow	(153)	2	(151)
31 August 2005	3,748	—	3,748
Cash flow	6,550	—	6,550
28 February 2006	10,298	—	10,298

INDEPENDENT REVIEW REPORT TO THE CHARACTER GROUP PLC

Introduction

We have been instructed by the company to review the financial information for the six months ended 28 February 2006, which comprises the consolidated profit and loss account, the consolidated statement of recognised gains and losses, the consolidated balance sheet, the consolidated cash flow statement and the notes to the accounts. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report, including the conclusion, has been prepared for and only for the Company for the purposes of its interim report. We do not, therefore, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by, the directors. The AIM Rules require that the accounting policies and presentation applied to the interim figures should be consistent with those that will be adopted in the annual accounts having regard to the accounting standards applicable to such annual accounts, except where any changes, and the reasons for them, are disclosed.

Review work performed

We conducted our review in accordance with guidance contained in Bulletin 1999/4 issued by the Auditing Practices Board for use in the United Kingdom. A review consists principally of making enquiries of management and applying analytical procedures to the financial information and underlying financial data and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with International Standards on Auditing (UK and Ireland) and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 28 February 2006.

HLB Vantis Audit plc
Chartered Accountants
London

26 April 2006

NOTES

NOTES

The Character Group plc
2nd Floor, 86-88 Coombe Road,
New Malden, Surrey KT3 4QS

T 020 8949 5898
F 020 8336 2585
E info@charactergroup.plc.uk