Management's Discussion and Analysis of Financial Condition and Results of Operations

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors. You should read this section in conjunction with our consolidated financial statements and the related notes.

CRITICAL ACCOUNTING POLICIES

The accompanying consolidated financial statements and supplementary information were prepared in accordance with accounting principles generally accepted in the United States of America. Significant accounting policies are discussed in Footnote 2 to the Consolidated Financial Statements. Inherent in the application of many of these accounting policies is the need for management to make estimates and judgments in the determination of certain revenues, expenses, assets and liabilities. As such, materially different financial results can occur as circumstances change and additional information becomes known. The policies with the greatest potential effect on our results of operation and financial position include:

The allowance for doubtful accounts is based on our assessment of the collectibility of specific customer accounts and the aging of the accounts receivable. If there were a deterioration of a major customer's creditworthiness, or actual defaults were higher than our historical experience, our estimates of the recoverability of amounts due to us could be overstated, which could have an adverse impact on our operating results.

Our revenue recognition policy is significant because our revenue is a key component of our results of operations. In addition, our revenue recognition determines the timing of certain expenses, such as commissions and royalties. We follow very specific and detailed guidelines in measuring revenues; however, certain judgments affect the application of our revenue policy. Revenue results are difficult to predict, and any shortfall in revenue or delay in recognizing revenue could cause our operating results to vary significantly from quarter to quarter.

We assess the impairment of long-lived assets and goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets or the strategy for our overall business; and
- significant negative industry or economic trends.

When we determine that the carrying value of long-lived assets and goodwill may not be recoverable based upon the existence of one or more of the above indicators of impairment, we measure any impairment based on a projected discounted cash flow method using a discount rate determined by our management to be commensurate with the risk inherent in our current business model. Net long-lived assets and goodwill amounted to $222.0 million as of December 31, 2002.

RECENT DEVELOPMENTS

On March 11, 2002, we purchased a controlling interest in Toymax. On October 25, 2002, we completed that acquisition by acquiring the remaining outstanding common shares. The total purchase price of approximately $62.2 million consisted of 1,166,360 shares of our common stock, 598,697 stock options and approximately $41.0 million in cash and resulted in additional goodwill of $64.9 million. Our results of operations have included Toymax from March 12, 2002, however for the period March 12, 2002 through October 25, 2002 the minority interest's share of Toymax's earnings were excluded.

On November 27, 2002, we purchased certain product lines, assets and assumed certain liabilities from Trendmasters. The total purchase price of approximately $19.0 million consisted of all cash and resulted in goodwill of $26.2 million. Our results of operations have included Trendmasters from the date of acquisition.

RESULTS OF OPERATION

The following table sets forth, for the periods indicated, certain statement of operations data as a percentage of net sales.

Years Ended December 31,	1998	1999	2000	2001	2002
Net sales	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of sales	61.0	58.6	59.4	57.8	57.9
Gross profit	39.0	41.4	40.6	42.2	42.1
Selling, general and administrative expenses	28.2	27.8	31.9	31.5	29.6
Acquisition shut-down and product recall costs	—	—	0.5	0.4	2.2
Income from operations	10.8	13.6	8.2	10.3	10.3
Profit from joint venture	—	(2.0)	(6.3)	(2.3)	(2.6)
Interest, net	0.4	(0.9)	(1.5)	(0.7)	(0.4)
Other (income) expense, net	0.7	—	—	—	—
Income before income taxes and minority interest	9.7	16.5	16.0	13.3	13.3
Provision for income taxes	2.2	4.5	4.6	3.4	2.9
Income before minority interest	7.5	12.0	11.4	9.9	10.4
Minority interest	—	—	—	—	0.3
Net income	7.5%	12.0%	11.4%	9.9%	10.1%

YEARS ENDED DECEMBER 31, 2002 AND 2001

Net Sales. Net sales increased $25.7 million, or 9.0%, to $310.0 million in 2002 from $284.3 million in 2001. The growth in net sales was due primarily to the addition of the Toymax products and continuing growth in sales of our Flying Colors and Doll products which was offset in part by a decrease in sales of our Wheels division, consisting primarily of our Road Champs die-cast toy and collectible vehicles with its extreme sports products.

Gross Profit. Gross profit increased $10.5 million, or 8.7%, to $130.6 million in 2002, or 42.1% of net sales, from $120.1 million, or 42.2% of net sales, in 2001. The overall increase in gross profit was attributable to the increase in net sales. Gross profit margin was compatible to last year as lower margins for Toymax products were offset by the decrease in royalty expense as a percentage of net sales due to changes in the product mix resulting from the sale of more products with lower royalty rates or proprietary products with no royalties.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were $91.8 million in 2002 and $89.6 million in 2001, constituting 29.6% and 31.5% of net sales, respectively. The overall increase of $2.2 million in such costs was due to costs incurred in support of our Kidz Biz and Toymax acquisitions and increased media buys, offset in part by a decrease in Goodwill amortization expense based on the implementation of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets." The decrease as a percentage of net sales is primarily attributable to the relative fixed nature of certain expenses with a concurrent increase in net sales. We produced and aired television commercials in support of several of our products, including World Wrestling Entertainment action figures and Flying Colors products, in 2001 and 2002. From time to time, we may increase our advertising efforts, if we deem it appropriate for particular products.

Acquisition Shut-down and Recall Costs. Acquisition shut-down costs in 2002 relate to shut-down costs, including lease termination, fixed asset abandonment and other costs, of certain operations of Toymax and Kidz Biz. Such costs in 2001 relate to shut-down costs of certain operations of Pentech, acquired in 2000. Operations impacted by these shut-downs were sales, design, distribution and administration. The integration of Pentech was completed in 2001 and the integration of Toymax and Kidz Biz was completed in 2002. In 2002, we accrued $2.2 million for the recall of one of our products.

The components of the acquisition shut-down and recall costs are as follows:

	Accrued Balance December 31, 2001	Accrual	Actual	Accrued Balance December 31, 2002
Lease abandonment costs	$ —	$3,723,481	$(1,413,681)	$2,309,800
Fixed asset write-off	—	260,142	(260,142)	—
Other	—	558,995	(558,995)	—
Recall	—	2,175,087	(2,175,087)	—
Total acquisition shut-down and recall costs	$ —	$6,717,705	$(4,407,905)	$2,309,800

Profit from Joint Venture. Profit from joint venture increased by $1.3 million in 2002 due to the joint venture having sales of only carryover titles in 2001 compared to releasing a new Microsoft Xbox title in addition to having sales of carryover titles in 2002. New releases typically generate higher unit sales resulting in higher overall sales as compared to carryover titles. Profit from the joint venture contributed significantly to our pre-tax profit, representing 17.6% of pre-tax income in 2001 and 19.5% in 2002. We expect to continue to receive a preferred return over the remaining term of the license agreement ending December 31, 2009, although we cannot predict with certainty what levels of return will be achieved and, in any case, we anticipate substantial fluctuations in the amount of the preferred return distributed to us from year to year.

Interest, Net. Interest income decreased in 2002 compared to 2001 in spite of higher average cash balances due to lower interest rates.

Provision for Income Taxes. Provision for income taxes included Federal, state and foreign income taxes in 2001 and 2002, at effective tax rates of 25.8% in 2001 and 22% in 2002, benefiting from a flat 16.5% Hong Kong Corporation Tax on our income arising in, or derived from, Hong Kong. The decrease in the current year effective rate net results primarily from certain permanently non-taxable items in addition to a continued shift in profits to more favorable tax jurisdictions. As of December 31, 2002, we had net deferred tax assets of approximately $3.9 million for which no allowance has been provided since, in the opinion of management, realization of the future benefit is probable. In making this determination, management considered all available evidence, both positive and negative, as well as the weight and importance given to such evidence.

YEARS ENDED DECEMBER 31, 2001 AND 2000

Net Sales. Net sales increased $32.0 million, or 12.7%, to $284.3 million in 2001 from $252.3 million in 2000. The growth in net sales was due primarily to the continuing growth in sales of our Flying Colors products and an increase in sales of our World Wrestling Entertainment wrestling products, as well as the addition of Pentech products, which began contributing to operations in August 2000, and the introduction of our products based on the Battlebots television show though offset by a decrease in sales of our Doll products and our Wheels products, consisting primarily of our Road Champs die-cast toy and collectible vehicles including BXS die-cast bicycle, MXS die-cast motorcycles and other extreme sports products.

Gross Profit. Gross profit increased $17.7 million, or 17.3%, to $120.1 million in 2001, or 42.2% of net sales, from $102.4 million, or 40.6% of net sales, in 2000. The overall increase in gross profit was attributable to the increase in net sales and the increase in the gross profit margin. The increase in gross profit margin of 1.6% of net sales is primarily attributable to the decrease in royalty expense as a percentage of net sales due to changes in the product mix and lower product costs, which was partially offset by an increase in amortization expense relating to molds and tools used in the manufacture of our products.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were $89.6 million in 2001 and $80.4 million in 2000, constituting 31.5% and 31.9% of net sales, respectively. The overall increase of $9.2 million in such costs in 2001 was due in large part to a $5.0 million dollar reserve on accounts receivable relating to the Chapter 11 bankruptcy filing of Kmart, which was filed in January of 2002, and the increase in net sales with its proportionate impact on variable selling costs such as freight and shipping related expenses, sales commissions, cooperative advertising and travel expenses, among others. The decrease as a percentage of net sales is primarily attributable to the fixed nature of certain of these expenses with a concurrent increase in net sales. We produced and aired television commercials in support of several of our products, including World Wrestling Entertainment action figures, Road Champs extreme sports products and Flying Colors products in 2000 and 2001. From time to time, we may increase our advertising efforts, if we deem it is appropriate for particular products.

Acquisition Shut-down and Other Costs. Acquisition shut-down and other costs in 2001 relate to shut-down costs, including lease termination, relocation and consulting fees and expenses, of certain operations of Pentech, acquired in 2000, and such costs in 2000 relate to shut-down costs, including lease termination, relocation, and consulting fees and expenses of certain operations of Flying Colors, acquired in 1999. Operations impacted by both shut-downs were sales, design, distribution, and administration. Total Pentech costs are comprised of $0.3 million relating to lease terminations and abandonments, $0.2 million in consulting fees and expenses incurred to facilitate the integration, $0.4 million relating to relocation expense, and $0.1 million relating to the abandonments of other assets. Twenty-one Pentech employees received severance totaling $0.4 million, that was accrued in the fourth quarter of 2000 and was fully paid out by June 30, 2001. The integration of Pentech was substantially completed in the second quarter of 2001 and related costs are expected to be nominal in future quarters. In 2000, total Flying Colors costs is comprised of $0.2 million relating to lease terminations and abandonments and $0.3 million relating to relocation expense. The integration of Flying Colors was completed in 2000. Additionally, 2000 includes $0.6 million relating to the recall of one of our products.

Profit from Joint Venture. Profit from our joint venture with THQ decreased in 2001 due to a decrease in our preferred return resulting from fewer releases of *World Wrestling Entertainment* video games by our joint venture in 2001 than in 2000. In 2001, the joint venture released two Nintendo GameBoy titles, which have lower unit sales and sales prices than the other game platforms, and one Sony PlayStation 2 title along with modest carryover sales of titles released in 2000 and earlier, as compared to 2000, in which the joint venture released a total of four new titles consisting of two Sony PlayStation titles, one Nintendo 64 title and one Sega Dreamcast title in addition to strong carryover sales of the two 1999 releases. Profit from the joint venture contributed significantly to our pre-tax profit, representing 39.4% of pre-tax income in 2000 and 17.6% in 2001. Through June 30, 2006, we are entitled to receive a guaranteed preferred return at varying rates of net sales of the video games depending on the cumulative unit sales and platform of each particular game, and after June 30, 2006, the amount of the preferred return is subject to renegotiation between THQ and us. The minimum preferred return to be distributed to us by the joint venture during each of the years in the period ending December 31, 2003 is $2.6 million per year. We expect our aggregate return over the remaining term of the license agreement ending December 31, 2009 to be significantly in excess of this amount, although we cannot predict with certainty that expected levels of return will be achieved and, in any case, we anticipate substantial fluctuations in the amount of the preferred return distributed to us from year to year.

Interest, Net. Interest income decreased in 2001 due to lower average cash balances during 2001 than in 2000 as a result of significant disbursements made in the third and fourth quarters of 2000 related to the acquisition of Pentech and the repurchase by the Company of its common stock. Interest expense was nominal in 2000 and 2001.

Provision for Income Taxes. Provision for income taxes included Federal, state and foreign income taxes in 2000 and 2001, at effective tax rates of 29% in 2000 and 25.8% in 2001, benefiting from a flat 16.5% Hong Kong Corporation Tax on our income arising in, or derived from, Hong Kong. As of December 31, 2001, we had deferred tax assets of approximately $0.4 million for which no allowance has been provided since, in the opinion of management, realization of the future benefit is probable. In making this determination, management considered all available evidence, both positive and negative, as well as the weight and importance given to such evidence.

QUARTERLY FLUCTUATIONS AND SEASONALITY

We have experienced significant quarterly fluctuations in operating results and anticipate these fluctuations in the future. The operating results for any quarter are not necessarily indicative of results for any future period. Our first quarter is typically expected to be the least profitable as a result of lower net sales but substantially similar fixed operating expenses. This is consistent with the performance of many companies in the toy industry.

The following table presents our unaudited quarterly results for the years indicated. The seasonality of our business is reflected in this quarterly presentation.

	2000				2001				2002			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
(in thousands, except per share data)												
Net sales	$50,782	$50,578	$91,838	$59,090	$59,962	$70,141	$92,768	$61,438	$59,895	$78,992	$102,640	$68,489
As a % of full year	20.1%	20.1%	36.4%	23.4%	21.1%	24.7%	32.6%	21.6%	19.3%	25.5%	33.1%	22.1%
Gross profit	$20,104	$21,748	$37,672	$22,883	$24,468	$32,609	$39,056	$23,953	$26,470	$35,192	$ 41,812	$27,077
As a % of full year	19.7%	21.2%	36.8%	22.3%	20.4%	27.2%	32.5%	19.9%	20.3%	27.0%	32.0%	20.7%
As a % of net sales	39.6%	43.0%	41.0%	38.7%	40.8%	46.5%	42.1%	39.0%	44.2%	44.6%	40.7%	39.5%
Income (loss) from operations	$ 3,552	$ 6,095	$11,201	$ (345)	$ 7,267	$ 8,879	$14,562	$ (1,410)	$ 1,420	$ 9,912	$ 18,895	$ 1,758
As a % of full year	17.3%	29.8%	54.6%	(1.7)%	24.8%	30.3%	49.7%	(4.8)%	4.4%	31.0%	59.1%	5.5%
As a % of net sales	7.0%	12.1%	12.2%	(0.6)%	12.7%	12.1%	15.7%	(2.3)%	2.4%	12.5%	18.4%	2.6%
Income before income taxes and minority interest	$ 9,715	$ 8,877	$13,615	$ 8,127	$ 8,480	$ 9,478	$15,250	$ 4,822	$ 2,985	$10,849	$ 19,944	$ 7,352
As a % of net sales	19.1%	17.6%	14.8%	13.8%	14.1%	13.5%	16.4%	7.8%	5.0%	13.7%	19.4%	10.7%
Net income	$ 6,603	$ 6,237	$ 9,769	$ 6,028	$ 6,021	$ 6,873	$10,949	$ 4,390	$ 2,156	$ 7,832	$ 13,954	$ 7,329
As a % of net sales	13.0%	12.3%	10.6%	10.2%	10.0%	9.8%	11.8%	7.1%	3.6%	9.9%	13.6%	10.7%
Diluted earnings per share	$ 0.32	$ 0.31	$ 0.48	$ 0.32	$ 0.32	$ 0.36	$ 0.56	$ 0.22	$ 0.11	$ 0.36	$ 0.58	$ 0.30
Weighted average shares and equivalents outstanding	20,374	20,371	20,330	18,621	18,920	19,259	19,586	19,763	20,236	21,953	24,059	24,800

During the second quarter of 2000, we recorded a charge which impacted operating income by approximately $1.4 million relating to the recall of one of our products.

During the fourth quarter of 2001, we recorded a charge of $5.0 million to bad debt impacting operating income relating to the bankruptcy filing of one of our customers, Kmart.

During the first quarter of 2002, we recorded a charge which impacted operating income by approximately $6.6 million relating to the restructuring of Toymax and Kidz Biz.

During the second quarter of 2002, we recorded a charge which impacted operating income by approximately $1.5 million relating to the recall of one of our products.

During the fourth quarter of 2002, we reversed $2.1 million of the restructuring charge recorded in the first quarter of 2002 and recorded an additional charge of approximately $0.7 million relating to the recall of one of our products, the net of which favorably impacted operating income by approximately $1.4 million. In addition, our effective tax rate for the year 2002 was reduced from 26% to 22%.

RECENT ACCOUNTING STANDARDS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). The objective of SFAS 143 is to establish an accounting standard for the recognition and measurement of an asset retirement obligation on certain long-lived assets. The retirement obligation must be one that results from the acquisition, construction or normal operation of a long-lived asset. SFAS 143 requires the legal obligation associated with the retirement of a tangible long-lived asset to be recognized at fair value as a liability when incurred, and the cost to be capitalized by increasing the carrying amount of the related long-lived asset. SFAS 143 will be effective for the Company's fiscal year beginning January 1, 2003. The adoption of this statement will have no material impact on the consolidated financial statements.

In October 2001, the FASB issued Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 supersedes Statements of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" ("SFAS 121") and retains the basic requirements of SFAS 121 regarding when and how to measure an impairment loss. SFAS 144 provides additional implementation guidance on accounting for an impairment loss. SFAS 144 is effective for all fiscal years beginning after December 15, 2001. The Company adopted SFAS 144 beginning in fiscal 2002, the adoption of which did not have a material effect on the Company's financial position or results of operations.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Correction" ("SFAS 145"). SFAS 145 eliminates extraordinary accounting treatment for reporting gains or losses on debt extinguishments, and amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. The provisions of this SFAS are effective for fiscal years beginning after May 15, 2002; however, early application of SFAS 145 is encouraged. Debt extinguishments reported as extraordinary items prior to scheduled or early adoption of this SFAS would be reclassified to other income in most cases following adoption.

The Company is currently evaluating the impact of the adoption of SFAS 145 would have on its consolidated results of operations subject to the evaluation in accordance with APB 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business and Extraordinary, Unusual and Infrequently Occurring Events and Transactions."

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"), which changes the accounting for costs such as lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operation, plant closing, or other exit or disposal activity initiated after December 31, 2002. The standard requires companies to recognize the fair value of costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan.

The Company anticipates that the adoption of SFAS 146 will not have a material effect on the Company's financial position or results of operations.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2002, we had working capital of $129.2 million, as compared to $116.5 million as of December 31, 2001. This increase was primarily attributable to the receipt of net proceeds from the sale of our common stock and from operating activities offset in part by disbursements relating to the acquisitions of Toymax and Trendmasters.

Operating activities provided net cash of $66.2 million including the sale of marketable securities of $37.1 million in the year ended December 31, 2002 as compared to $13.4 million, net of the purchase of marketable securities of $23.5 million, in 2001. Net cash was provided primarily by net income and non-cash charges, such as depreciation and amortization, the forgiveness of an officer note receivable and minority interest, as well as decreases in prepaid expenses and other current operating assets, the sale of marketable securities and increases in the reserve for sales returns and allowances, income taxes payable and deferred income taxes, which were offset in part by a non-cash benefit consisting of earned compensation from stock option grants, increases in the preferred return from THQ joint venture, accounts receivable, inventory, advanced royalty payments and decreases in accounts payable and accrued expenses. As of December 31, 2002, we had cash and cash equivalents of $68.4 million and no marketable securities.

Operating activities provided net cash of $13.4 million, net of the purchase of marketable securities of $23.5 million, in the year ended December 31, 2001 as compared to $30.0 million, including the sale of marketable securities of $25.7 million, in 2000. Net cash was provided primarily by net income and non-cash charges, such as depreciation and amortization and recognition of compensation expense from stock option grants, as well as the increases in accrued expenses and deferred income taxes and decrease in the preferred return due from the joint venture, which were offset in part by increases in accounts receivable and inventory and decreases in the reserve for sales returns and allowances and income taxes payable. As of December 31, 2001, we had cash and cash equivalents of $25.0 million and marketable securities of $37.1 million.

Our investing activities used cash of $87.8 million in the year ended December 31, 2002, as compared to $19.4 million in 2001, consisting primarily of the purchase of office furniture and equipment and molds and tooling used in the manufacture of our products, the goodwill acquired in the acquisitions of Toymax and Trendmasters, the $4.5 million in goodwill relating to the final earn-out for Flying Colors, and the increase in other assets, partially offset by the repayment of notes receivable from officers. In 2001, our investing activities consisted primarily of the purchase of molds and tooling used in the manufacture of our products, the goodwill acquired in the acquisitions of Kidz Biz Ltd. and Kidz Biz Far East, plus the $4.5 million in goodwill relating to the 2001 earn-out for Flying Colors, partially offset by the repayment of notes receivable from officers. As part of our strategy to develop and market new products, we have entered into various character and product licenses with royalties ranging from 1% to 12% payable on net sales of such products. As of December 31, 2002, these agreements required future aggregate minimum guarantees of $19.4 million, exclusive of $2.9 million in advances already paid.

Our investing activities used net cash of $19.4 million in the year ended December 31, 2001, as compared to $47.9 million in 2000, consisting primarily of the purchase of molds and tooling used in the manufacture of our products in 2001 and 2000, and goodwill acquired in the acquisitions of Kidz Biz Ltd. and Kidz Biz Far East in 2001 and Pentech in 2000. As part of our strategy to develop and market new products, we have entered into various character and product licenses with royalties ranging from 1% to 12% payable on net sales of such products. As of December 31, 2001, these agreements required future aggregate minimum guarantees of $11.5 million, exclusive of $2.0 million in advances already paid.

Our financing activities provided net cash of $64.9 million in the year ended December 31, 2002, as compared to $1.8 million in 2001. In 2002, cash was primarily provided from the sale of our common stock and from the exercise of stock options and warrants, partially offset by the repayment of long-term debt. In 2001, cash was primarily provided from the exercise of stock options and warrants, partially offset by the repayment of debt assumed in the acquisition of Pentech.

Our financing activities provided net cash of $1.8 million in the year ended December 31, 2001, compared to having used cash of $10.4 million in 2000. In 2000, we used cash primarily to repurchase 1,493,600 shares of our common stock for a total of $12.9 million, while cash was provided by the exercise of stock options and warrants and the assumption of debt related to the acquisition of Pentech. Net cash provided in 2001 consisted primarily of proceeds from the exercise of stock options and warrants, offset by the repayment of debt assumed in the acquisition of Pentech.

During 2002, we acquired all the outstanding common shares of Toymax for cash of approximately $41.0 million and 1,166,360 shares of our common stock and paid off approximately $12.3 million of indebtedness. In November 2002, we acquired certain assets of Trendmasters for approximately $19.0 million and paid off approximately $3.7 million of indebtedness in cash.

The following is a summary of our significant contractual cash obligations for the periods indicated that existed as of December 31, 2002 and is based on information appearing in the notes to the consolidated financial statements:

	2003	2004	2005	2006	2007	Thereafter	Total
Long-term debt	$ 17,805	$ 19,036	$ 20,350	$ 20,297	$ —	$ —	$ 77,488
Operating leases	4,707,091	4,601,158	3,967,662	3,905,415	3,490,756	1,292,900	21,964,982
Minimum guaranteed license/royalty payments	4,202,692	1,829,063	4,538,335	1,040,000	1,040,000	6,731,000	19,381,090
Employment contracts	4,887,867	4,114,997	3,201,000	2,855,000	2,930,000	4,410,000	22,398,864
Total contractual cash obligations	$13,815,455	$10,564,254	$11,727,347	$7,820,712	$7,460,756	$12,433,900	$63,822,424

In May and June 2002, we received an aggregate of $59.1 million in net proceeds from the sale of 3,525,000 shares of our common stock in an under-written public offering. These proceeds, which we invested temporarily in marketable securities and cash equivalents, were applied to our product acquisition, development, working capital and general corporate needs.

In December 2001, we acquired all of the outstanding capital stock of Kidz Biz Limited, a United Kingdom company, and an affiliated Hong Kong company, Kidz Biz Far East Limited, for an aggregate purchase price of approximately $12.4 million. Total consideration was paid on the closing of the transaction in cash in the amount of $6.4 million and the issuance of 308,992 shares of our common stock at a value of $6.0 million. In addition, we agreed to pay an earn-out for each of 2002, 2003, 2004 and 2005, based on the year-over-year increase in Kidz Biz sales, payable by delivery of up to 25,749 shares of our common stock. In 2002, nothing was earned.

In October 1999, we acquired Flying Colors Toys for approximately $34.7 million in cash for the stock and paid off approximately $17.6 million of indebtedness. In addition, we also paid an earn-out of up to $4.5 million in each of the three 12-month periods following the closing because the gross profit of Flying Colors products achieved certain targeted levels during these periods.

In October 2001, we secured a syndicated line of credit totaling $50.0 million with a consortium of banks led by Bank of America, N.A. ("Line of Credit"). The Line of Credit will be available for future acquisitions and working capital and is secured by a lien on substantially all of our assets and contains customary financial and non-financial covenants which require us to maintain a minimum net worth and limit our ability to incur additional indebtedness, pay cash dividends or make distributions, sell assets and enter into certain mergers or acquisitions. We are required to not have any outstanding borrowings in excess of $30.0 million for a period of at least 30 consecutive days during the first fiscal quarter of each year of the agreement. Amounts outstanding under this facility bear interest at 0.25% plus the greater of the Prime Rate or the Federal Funds Rate plus 0.5%, subject to adjustment based on certain financial ratios. As of December 31, 2002, we had no outstanding borrowings.

In February 2003, our Board of Directors approved a buyback of up to $20 million of our common stock. As of March 27, 2003, we repurchased 330,000 shares of our common stock for a total of approximately $3.4 million.

We believe that our cash flows from operations, cash and cash equivalents on hand and the availability under the Line of Credit will be sufficient to meet our working capital and capital expenditure requirements and provide us with adequate liquidity to meet our anticipated operating needs for at least the next 12 months. Although operating activities are expected to provide cash, to the extent we grow significantly in the future, our operating and investing activities may use cash and, consequently, this growth may require us to obtain additional sources of financing. There can be no assurance that any necessary additional financing will be available to us on commercially reasonable terms, if at all.

EXCHANGE RATES

Sales from our United States and Hong Kong operations are denominated in U.S. dollars and our manufacturing costs are denominated in either U.S. or Hong Kong dollars. Domestic sales from our United Kingdom operations and operating expenses of all of our operations are denominated in local currency, thereby creating exposure to changes in exchange rates. Changes in the Hong Kong dollar or British pound/U.S. dollar exchange rate may positively or negatively affect our gross margins, operating income and retained earnings. The exchange rate of the Hong Kong dollar to the U.S. dollar has been fixed by the Hong Kong government since 1983 at HK$7.80 to US$1.00 and, accordingly, has not represented a currency exchange risk to the U.S. dollar. We cannot assure you that the exchange rate between the United States and Hong Kong currencies will continue to be fixed or that exchange rate fluctuations between the United States and Hong Kong and United Kingdom currencies will not have a material adverse effect on our business, financial condition or results of operations.