CONTENTS

www.thecharacter.com
www.character-online.co.uk

DIRECTORS AND ADVISERS

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

Secretary
K P Shah FCCA

Company registration number
3033333

Registered office
5th 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

Nominated Advisers and Broker
Charles Stanley Securities
25 Luke Street
London EC2A 4AR

Bankers
National Westminster Bank plc
Standard Chartered Bank

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

CHAIRMAN'S STATEMENT

Introduction

I am delighted to report record pre-tax profits of £11.78 million for the financial year ended 31 August 2007, compared to £5.1 million for the previous year.

Since the disposal of our digital business in February 2006, we have been able to concentrate virtually all our efforts on developing our toys and games portfolio. This, together with our strategy of acquiring new product licences and designing and developing products in-house, has proven to be a major factor in the Group's growth.

This creditable performance not only reflects this focus but shows that our products continue to meet the market's needs and consumer demand.

Financials

The 2006/7 financial year is our first financial year where we have been able to focus fully on our continuing business following the sale of our digital business, although the comparative figures shown include revenue and contribution from the historical digital operation. (Note 2 compares the continuing business).

Turnover for Toys, Games and Gifts was £94.52 million against £69.55 million last year, an increase of approximately 36 per cent (2006: £95.53 million, including digital sales of £25.98 million).

Operating profit for the continuing business increased by approximately 74% to £12.06 million (2006: £6.91 million).

Profit before tax rose approximately 130% to £11.78 million (2006:£5.13 million).

Basic earnings per share in the period were 17.93 pence, up 115% from 8.36 pence achieved for the continuing business in the comparable period (2006: 5.80 pence).

Stocks at year end were £10.83 million (2006: £10.67 million, including digital stocks).

Cash at bank at the year end was £15.7 million, compared to £7.4 million at 31 August 2006.

Review of 2006/7

Through the team effort of our senior management, we entered the year with a determination to concentrate our efforts on developing the "brands" that we had in the business, whilst at the same time ensuring that our products got the distribution base they deserved.

Our growth to date in sales and profits reflects an outstanding performance for the Group, especially as we continue to operate in a difficult period for retailers, both in the UK and across Europe.

Our Doctor Who product line-up performed exceptionally well once again. As Master Toy licensee, we celebrated another phenomenal year, with over 3 million Doctor Who action figures projected to be sold through calendar year 2007 compared to 1.7 million for the previous year.

It is also satisfying to note that we experienced strong double digit growth in many of our other brands, including Scooby Doo, Disney Princess, Peppa Pig, Gr8 Art, Bindeez, Dragonfly (from our Robotic range) and Gloe Bears.

Overall, the growth that we have achieved has enabled us to increase our UK market share by approximately 30%.

During the year, we secured a number of new Master Toy licences, including:

- ***Primeval***

An Impossible Pictures production for ITV, ProSieben and M6, is a science fiction drama, which has been renewed for a second series and Character will be producing an extensive line of exciting products that will include a Dragonfly Rex and Carnivorous Pterosaur. These will be available from this month and will be followed by a number of other action figures and creatures from series one and two in January 2008.

- ***Dork Hunters From Outer Space***

The Pan-European licence covers all standard "master toy" products, such as basic plush; feature plush; action figures; toy vehicles and accessories; playsets; activity, arts & crafts; interactive toys; board-games; toy writing and school instruments and toy accessories, including lipstick and make-up. We envisage a full European roll-out in late summer 2008 and we see Dork Hunters from Outer Space as a strategic cornerstone for our extensive branding initiatives.

- ***Postman Pat***

The range of products for the UK and Eire market include toys, playsets, plush and collectables. Character will begin developing new product lines for Postman Pat, with new products to coincide with the brand new TV series which airs on CBeebies and BBC Two in 2009. Character plans to produce a comprehensive range at a new scale to that previously seen in the market, including characters from the classic and new series. The range will be available in early 2009.

Postman Pat is an iconic brand with an established heritage which has continually delighted pre-schoolers for over 25 years. We believe that this licence will become an important brand within our portfolio and a Top-5 pre-school property.

Revenues from these new licenses will commence making a contribution in the 2008/2009 financial years.

Product Quality

We have, since the outset, taken quality control and quality assurance as a high priority in our processes, whilst also continually improving our standards and procedures.

Following the recent problems which have been highlighted in the press, we have further reviewed these processes and have increased the testing of our products. We are pleased to confirm that none of our products have experienced the well publicised problems of one of our competitors.

The Group will continue to focus on delivering toys and related products that not only meet the demand of the consumer but also have been manufactured or sourced to the highest standards, thereby adhering to the Group's and UK and international bodies' strict guidelines.

Dividend

In-line with our progressive dividend policy and to further underpin the Board's confidence in the Group's portfolio of product which has already been reflected through this year's robust performance, the

Directors are recommending an increased final dividend of 2.4 pence per share, which together with the interim dividend of 2.0 pence makes a total dividend for the year of 4.4 pence per share, a 33% increase (2006: 3.30 pence).

Subject to approval by Shareholders at the Annual General Meeting to be held on 16 January 2008, the final dividend will be paid on 25 January 2008 to Shareholders on the Register as at 4 January 2008. The shares will go ex-dividend on 2 January 2008.

The total dividend is covered four times by earnings.

Share Buy-Backs

As we have clearly laid out to Shareholders, part of the Group's stated objectives is to continue its focus on ways to further enhance shareholder value, both through our on-going plans to implement a progressive dividend policy and monitoring the position in the market with a view to continuing to buy-back shares for Treasury and cancellation, when considered appropriate.

The Directors believe that the Group has used its current authority to buy-back shares in the market to great effect, and in the period under review, this alone has resulted in an increase of 17.3% to the earnings per share.

Over a two-year period, we have purchased approximately 9.15 million ordinary shares of 5p each in the Company ("Ordinary Shares") at an average price of 86 pence per share. The buy-back to date represents approximately 20.6% of the current issued share capital of the Company (excluding shares held in Treasury). Following the cancellation of these Ordinary Shares, the Company has 44,452,937 Ordinary Shares in issue (excluding 1,000,000 Ordinary Shares in the Company held in Treasury).

Share buy-backs have been used effectively to date and will continue to be considered as an effective tool for the future. In this regard, the Board has the ability to put in place a line of credit specifically for this purpose.

At the forthcoming AGM, Shareholders will be asked to approve a resolution to renew the Company's authority to repurchase Ordinary Shares in the Company, up to 25% of its issued share capital (excluding Ordinary Shares held in Treasury).

If this Resolution is once again approved by Shareholders, the Directors will continue to monitor the market position and will, if appropriate, make further purchases of the Company's own Ordinary Shares over the next financial year.

People

On behalf of the Board and all our Shareholders, I would like to welcome all new staff who joined the Group during the year.

It is also an appropriate time to recognise the hard work and dedication of everyone within the Group, without whom, we would not have been able to produce another successful set of results; on behalf of the Board and Shareholders I thank all our employees.

Current Trading

The Group is fortunate to have within its product portfolio a strong, innovative and appealing range of toys, gifts and games. We are greatly encouraged by the continued growth of our brands, the reaction by the consumer to our Christmas ranges, and the reception by the trade, to our new ranges for 2008.

We have established ourselves as a major supplier in the UK and we believe we are well positioned to capitalise further on this position, whilst continuing to develop our international sales.

Additionally, the Group has an all-time record three toys featured on the Toy Retailers Association (TRA) annual 'Dream Toys' list announced last month, an increase of 50% over last year.

The list is the only official prediction of Christmas 2007 best-sellers. In the 'Dream Dozen', Character has the following toys tipped for overall success:

- ***Doctor Who Dalek Sec Hybrid Voice Changer Mask***
- ***Flytech Dragonfly***
- ***Gr8 Art Bindeez Super Deluxe Studio Centre***

Out of five categories revealed by the TRA, twelve Character Options toys and games were featured, namely:

- ***Boys:*** ***Dr Who Dalek Sec Hybrid Voice Changer Mask***
Dr Who Figures Assortment
Stretch Power Ranger
- ***Pre-school:*** ***Peppa Pig Campervan Playset***
- ***Games:*** ***Splashy the Whale Game***
- ***Hip 'n Kool:*** ***Flytech Dragonfly***
- ***Creative:*** ***Gr8 Art Bindeez Super Deluxe Studio***
Gr8 Scrapheap Welder

This recognition gives us confidence that the increase in market share that we enjoyed last year and which we have continued to experience since the start of the new financial year is likely to be maintained through the important Christmas period.

Prospects

The new financial year has started well, with our Christmas 2007 offering already having achieved a wider distribution base than for the previous Christmas. With the addition of new brands to our portfolio and the continued growth we envisage to our existing brands, we are confident of achieving a further satisfactory financial year in 2008.

Richard King
Chairman
31 October 2007

DIRECTORS' BIOGRAPHIES

Richard King (aged 62), 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 to develop and implement Group strategies.

Kiran Shah (aged 53), Group Finance Director and Joint Managing 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.

Jon Diver (aged 43), Group Marketing Director and Joint Managing 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 product development and the development and implementation of the Group's marketing strategy.

Joe Kissane (aged 55), 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.

Ian Fenn (aged 64), 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 Blomfield Corporate Finance Limited, which is authorised and regulated by the Financial Services Authority.

Lord Birdwood (aged 69), 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. He is also retained by private equity firms to advise on future technologies.

David Harris (aged 57), 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, Osprey Small Companies Income Fund Ltd, Aseana Properties Ltd and COBRA Holdings Plc all of which are quoted companies.

Alan MacKay (aged 45), Non-Executive Director, is a partner at 3i Investments plc, one of the world's leading private equity companies. After founding, then selling, a marketing services business, he joined 3i in 1987 and was appointed to the Board of 3i plc in 1994. He currently leads 3i investment activity in the public equities arena. He is Chairman of 3TS Capital Partners, a member of the Strategic Advisory Board of SVG Investment Advisers, and a non-executive director of AIM listed company MDY Healthcare plc.

DIRECTORS' REPORT AND BUSINESS REVIEW

The directors present their report together with the accounts for the year ended 31 August 2007.

Directors

The following are the directors that served during the year:
Richard King (Executive Chairman)
Kirankumar Premchand Shah FCCA (Group Finance Director and Joint Managing Director)
Jonathan James Diver (Group Marketing Director and Joint Managing Director)
Joseph John Patrick Kissane (Managing Director, Character Options Limited)
Ian Stanley Fenn (Senior Independent Non-Executive Director)
Lord Birdwood (Independent Non-Executive Director)
David Harris (Independent Non-Executive Director)
Alan Browning Mackay (Non-Executive Director)

Biographies of the directors are set out on page 7.

Principal activity

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

Business review, results and dividend

A review of the business is contained in the Chairman's Statement on pages 2 to 5 and the results are detailed in the consolidated profit and loss account on page 20, the consolidated statement of total recognised gains and losses on page 21, the consolidated balance sheet on page 22 and the consolidated cash flow statement on page 24. There was a profit for the year, after taxation, amounting to £8,124,000 (2006: profit £2,992,000).

An interim dividend of 2.0 pence per share was paid on 25 May 2007. The directors recommend a final dividend of 2.4 pence per share making a total dividend of 4.4 pence per ordinary share (2006: 3.3 pence). If approved, the final dividend will be paid on 25 January 2008, to shareholders on the register on 4 January 2008.

International Financial Reporting Standards ("IFRS")

The consolidated accounts of the Group must comply with International Financial Reporting Standards (IFRS) for reporting periods beginning on or after 1 January 2007. The Group will therefore adopt IFRS from 1 September 2007.

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 31 August 2007 were as follows:

Directors	**Number of Ordinary Shares**	**31 August 2007 Ordinary Shares under option**	Number of Ordinary Shares	31 August 2006 Ordinary Shares under option
R King	**3,845,428**	**250,000**	5,345,428	250,000
K P Shah	**5,645,000**	**250,000**	5,645,000	250,000
J J P Kissane	**1,462,300**	**415,000**	1,462,300	415,000
J J Diver	**1,690,640**	**415,000**	1,690,640	415,000
I S Fenn	**9,000**	**–**	9,000	–
Lord Birdwood	**8,750**	**–**	8,750	–
D Harris	**14,097**	**–**	14,097	–
A B MacKay	**–**	**–**	–	–
TOPS Pension Scheme*	**450,000**	**–**	1,725,000	–

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

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 2007 and at 31 August 2006. 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 2007 and at 31 August 2006.

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 2007 and at 31 August 2006.

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 2007 and at 31 August 2006. 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.

A B MacKay is a partner of 3i Investments plc, adviser to 3i Quoted Private Equity Limited which has a beneficial interest in 11,525,898 ordinary shares at 31 August 2007.

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 2007, trade creditors of the Group represented an average of 74 (2006:75) days credit in relation to total purchases for the year.

Statement of directors' responsibilities

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and United Kingdom Generally Accepted Accounting Practice.

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and Group and of the profit or loss of the Group for that year. In preparing those financial statements the directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the accounts on a going concern basis unless it is inappropriate to presume that the Group will continue in business.

The directors are responsible for keeping accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Group's financial statements are published on the Group's website in accordance with legislation in the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the Group's website is the responsibility of the directors. The directors' responsibility also extends to the ongoing integrity of the financial statements.

Statement of Disclosure to Auditors

In so far as the Directors are aware:

- there is no relevant audit information of which the Group's auditors are unaware; and
- they have taken all steps they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the Group's auditors are aware of that information.

Substantial shareholders other than directors

At 31 October 2007 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 % (excluding shares held in Treasury)
3i Quoted Private Equity Limited	11,525,898	25.93%
Sweet Briar Investments Limited	1,675,000	3.77%

Changes in Share Capital

During the year, 491,750 ordinary shares of 5 pence each in the Company were issued to various employees on exercise of their share options. Details of such shares issued are given in note 16 to the accounts.

Also, during the year 4,087,722 ordinary shares were repurchased for cancellation, and 650,000 ordinary shares were repurchased and are held as treasury shares. Also, 775,000 ordinary shares from Treasury were sold. Details are given in note 16 to the accounts.

Share option schemes

Details of the Company's share option schemes are given in note 16 to the accounts.

Charitable and political donations

Payments of a charitable nature made during the year amounted to £93,726 (2006: £31,883). There were no political contributions in either year.

Annual General Meeting

Notice convening an annual general meeting of the Company is set out on page 41 of this document. Full details of the business to be transacted at that meeting are 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 £740,800 (14,816,000 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 2009 or the date falling 15 months following the passing of this resolution. The directors have no present intention to exercise this authority, which represents approximately 33.3% of the issued share capital of the Company at 31 August 2007, excluding shares held in treasury;

- authorise the directors to offer to allot new shares in the Company to shareholders who elect to accept the same in lieu of any cash dividend entitlement;

- authorise the Company to make purchases of issued ordinary shares in the Company 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 a maximum of 11,113,200 ordinary shares of 5 pence each in the capital of the Company (representing approximately 25% of the current issued share capital of the Company, excluding shares held in treasury). 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 price of an issued share in the Company in the five business days prior to purchase and a minimum of 5 pence, being the nominal value of an issued share in the Company. The directors intend to exercise this authority if and when to do so will, in the opinion of the directors, enhance shareholder value. If all options granted by the Company (pursuant to the Group's share option schemes and arrangements particularised in note 16 to the accounts) and subsisting as at 31 October 2007 were exercised a total of 2,812,500 new ordinary shares would be allotted, representing approximately 5.95% of the enlarged issue share capital of the Company following such exercise (excluding shares held in treasury). 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 approximately 7.78% of the issued share capital as enlarged by such allotments of shares (excluding shares held in treasury);

- allow the Company to send or supply documents and information to its shareholders by making them available on the Company's website. On 20 January 2007, new provisions within the Companies Act 2006 came into force concerning the ways in which a company is permitted to communicate with and supply information to its shareholders. Subject to this resolution being passed by shareholders, the Company may be able to use its website to publish documents and communications required or authorised to be sent or supplied by the Company to its shareholders (such as its interim reports, notices of general meetings and its annual report and accounts) as its default method of publication. The Company would like to be in a position to take advantage of these new provisions and so reduce the bulk in communications with shareholders that are currently required to be sent by post. This will potentially achieve cost savings and reduce the impact that unnecessary printing and distribution of some of these bulky documents has on the environment. Subject to this resolution being passed, the Companies Act 2006 entitles the Company to invite shareholders to agree that shareholder information may be supplied by means of a website. Shareholders who do not confirm that they wish to continue to receive hard copies of such communications within 28 days of any such invitation being made are deemed to have agreed to the Company communicating with them by means of the website. Where shareholders agree (or are deemed to have agreed) to communication by means of the website, they will be notified promptly by the Company, by post, of the availability of the relevant documents or information on the website. Shareholders will at all times continue to be entitled to request the Company to provide a paper copy of any documents which are provided by means of a website, if they so wish. There is no present intention to issue invitations in the manner required by the Companies Act 2006 and shareholders will receive notice of an intention to implement this regime by the Company, if and when any such decision is taken by the Board.

- approve a disapplication of shareholder pre-emption rights to enable the issue of equity securities in connection with any rights issues and/or an offer of issued shares held in treasury by way of rights 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 further limited disapplications of these pre-emption rights applying in relation to:

  (i) the allotment for cash of up to an aggregate nominal amount of £222,264 (4,445,280 ordinary shares of 5 pence each in the capital of the Company), representing approximately 10% of the nominal value of the issued ordinary share capital of the Company as at 31 August 2007 (excluding shares held in treasury);

  (ii) the sale of all or any of the 1,000,000 ordinary shares of 5 pence each in the capital of the Company held in treasury as at 31 October 2007.

Auditors

A resolution to reappoint HLB Vantis Audit plc as auditors to the Company will be proposed at the annual general meeting, convened by the notice set out on page 44 of this document.

CORPORATE GOVERNANCE STATEMENT

The directors continue to embrace the principles contained in the combined code of corporate governance issued in July 2003 as applicable to fully listed companies.

Directors

The Board of directors comprises four executive directors and four non-executive directors, as detailed on page 6. 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 at least four times a year and at other times as required to address requirements arising between these scheduled meetings.

During the year, five Board meetings were held. The directors attended as follows:

	Attendance
R King	4
K P Shah	5
J J P Kissane	5
J J Diver	4
I S Fenn	5
Lord Birdwood	4
D Harris	5
A B Mackay	5

The Board has a formal schedule of matters reserved for its decision. It determines the overall Group strategy; creation, acquisition or disposal of material corporate entities or assets; public announcements (including statutory accounts); significant changes in accounting policy, capital structure and dividend policy; group remuneration policy and Board structure, composition and succession.

The Board delegates to management, through the Executive Directors, the overall performance of the Group, which is conducted principally through the setting of clear objectives.

The Board has established an Audit Committee, a Remuneration Committee and a Nominations Committee, with duties and responsibilities formally delegated to them. The terms of reference set out each Committee's responsibilities. The terms of reference for the Audit Committee can be viewed at the Company's Registered Office.

Evaluation of the Board, Board Committees and Directors

The performance evaluation of the Board, its Committees and directors is undertaken by the Chairman and implemented in collaboration with the Committee Chairmen. The 2007 Board evaluation was conducted by way of a discussion between the Chairman and each of the directors. The independent non-executive directors met separately to review the Chairman's performance and provide feedback to him. Following formal performance evaluation, the Chairman confirms that the performance of non-executive directors continues to be effective and demonstrates their commitment to the role.

Audit Committee

I S Fenn (Chairman), Lord Birdwood and 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 auditors' 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. During the year, two meetings were held which were attended by all three members.

Remuneration Committee

Lord Birdwood (Chairman), I S Fenn and 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. During the year two meetings were held, which were attended by all three members.

Nominations Committee

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

The Nominations Committee is responsible for considering and recommending to the Board changes in the Board's composition and membership. No meetings were held during the year.

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 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 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
- 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 has 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.

During 2006, the Directors undertook to review the internal systems and procedures with the Group's internal and external business partners in order to attain the ISO 9001:2000 Quality Management Systems accreditation. As a result, the Company has appointed The British Standards Institute to act as external quality auditors.

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 invoice discounting. There was also continued use of short-term bank facilities during the period under review. As at 31 August 2007, the Group had committed bank facilities of £19.5 million, of which £3.4 million was undrawn.

Interest Rate Risk

The Group finances its operations through a mixture of invoice discounting, trade finance and bank borrowings. All such facilities are at variable rates of interest.

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.

Further information on the Group's use of financial instruments and exposure to risk are given in note 23 of the accounts.

Environmental

During 2007, further new EU Regulations concerning the control and registration of chemicals entering the EU came into force and will have an influence on the Group's controls in factories. The Regulations are as follows:

The R.E.A.C.H Regulations

The REACH Regulations (Registration, Evaluation and Authorisation of Chemicals) came into force in the EU on 1 June 2007. The Regulation introduces a new framework for legislation of chemicals in the EU, replacing a number of previous Directives and Regulations. The new scheme places the burden of responsibility for safe use of chemicals onto the suppliers of those substances, rather than on the authorities.

The process involves:

- Registration: Submission of a dossier of information on the substance to the European Chemicals Agency (ECHA), including a Chemical Safety Assessment where appropriate
- Evaluation: Review of the substance properties and identification of further testing needs
- Authorisation: Implementation of controls on substances where 'safe use' cannot be demonstrated.

One of the highest priorities of REACH is to identify so-called 'substances of very high concern' (sVHC), so that their manufacture and use can be controlled in order to protect the environment and human health. Substances of very high concern will be subject to authorisation. A list of candidate substances for authorisation will be published by the ECHA.

Substances that are included in the list will require authorisation for each use. Authorisation will only be granted if suitable alternatives are not available and provided risks can be adequately controlled.

Substances that are of very high concern include:

- Persistent, Bioaccumulative and Toxic substances (PBT)
- Substances which are very persistent and very bioaccumulative (vPvB)
- Substances classified as Carcinogenic, Mutagenic or toxic to Reproduction (CMR)
- Substances with endocrine disrupting properties, known as EDCs.

Timetable for implementation
(set up by the European Chemicals Agency)

1st June 2007	REACH regulations come into force
1st June 2007 – 1st December 2008	Entry into operation
30th November 2010	Registration of materials
31st May 2018	Review of new substances.

The Group continues to recognise that it can make a difference to the environment it works in and delivers to. With this in mind, the Group is still aiming to achieve, within its quality management system, accreditation to ISO 14001:2004.

The Group's key quality targets still continue to be:

- reduce packaging waste;
- recycle more product;
- reduce energy consumption in product design and increase its green office practices.

In 2006, the independent Pass Compliance Scheme® run by Product Assurance Limited was introduced to the Group's supplier base, which controls the management of hazardous materials within the Group's product ranges. The benefits of endorsing such a scheme will be borne out during 2007/8 as REACH will potentially become a complex administration process and will be administered by the PASS Compliance Scheme® group of experts.

A subsidiary is a stakeholder representing the toy industry in consultations concerning the EuP Directive (Energy Using Products) which concerns itself with the reduction of energy consumption associated with electronic products, such as toys that are supplied with or require the use of battery chargers and/or mains adaptors.

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 exception:

- Code provision A.7.1 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

31 October 2007

DIRECTORS' REMUNERATION REPORT

The Board presents the Remuneration Report for the year ended 31 August 2007.

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. Mr Diver is also entitled to a further bonus of 2% of pre-tax profits in the event that a specified target is met.

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 quoted 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. All executive directors are entitled to participate in the Company's unapproved executive Share Option Plan, details of which may also be found in note 16 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. Each of the non-executive directors is entitled to fees, currently at the rate of £20,000 per annum (2006: £20,000), plus expenses, without any right to compensation on early termination.

Audited Information

The following table shows a breakdown of the remuneration of the directors for the year ended 31 August 2007 and the year ended 31 August 2006.

Year ended 31 August 2007

	Salary/fees £	Performance bonus £	Benefits in kind £	Pension contribution £	Total £
R King	184,388	184,388	2,628	64,536	435,940
K P Shah	182,160	182,160	1,787	54,648	420,755
J J Diver	182,160	422,160	9,533	36,432	650,285
J J P Kissane	159,698	159,698	3,320	47,909	370,625
I S Fenn (non-executive)	20,000	–	–	–	20,000
Lord Birdwood (non-executive)	20,000	–	–	–	20,000
D Harris (non-executive)	20,000	–	–	–	20,000
A B MacKay (non-executive)	20,000	–	–	–	20,000
	788,406	948,406	17,268	203,525	1,957,605

Year ended 31 August 2006

	Salary/fees £	Performance bonus £	Benefits in kind £	Pension contribution £	Total £
R King	167,625	167,625	5,138	58,669	399,057
K P Shah	165,600	165,600	2,980	49,680	383,860
J J Diver	145,180	301,182	10,941	29,036	486,339
J J P Kissane	145,180	145,180	3,072	43,554	336,986
I S Fenn (non-executive)	20,000	–	–	–	20,000
Lord Birdwood (non-executive)	20,000	–	–	–	20,000
A G Horvat (non-executive)	15,000	–	–	–	15,000
D Harris (non-executive)	20,000	–	–	–	20,000
A B MacKay (non-executive)	–	–	–	–	–
	698,585	779,587	22,131	180,939	1,681,242

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 were granted pursuant to the Company's 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 years and not later than ten years from the date of grant, subject to the achievement of a predetermined profit related performance target, which has been achieved.

On 11 May 2006, options were granted over 960,000 new ordinary shares in the Company to the four executive directors as follows:

	Options granted
R King	250,000
K P Shah	250,000
J J Diver	230,000
J J P Kissane	230,000

These options were granted pursuant to the 2006 Share Option Plan, which was approved by shareholders on 29 November 2005 and adopted by the Company on 22 February 2006. The options are exercisable at a price of 63 pence per share normally no earlier than three years and not later than ten years from the date of grant, subject to the achievement of a predetermined profit related performance target, which has been achieved.

Audited Information Continued

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 2007 the mid-market price of an issued ordinary share in The Character Group plc was 171.5 pence, and during the year the price ranged from 72.5 pence to 208.5 pence.

On behalf of the Board

Lord Birdwood
Chairman, Remuneration Committee
31 October 2007

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE CHARACTER GROUP plc

We have audited the Group and Parent Company financial statements ("the financial statements") of The Character Group plc for the year ended 31 August 2007 which comprise the Consolidated Profit and Loss Account, the Consolidated Statement of Recognised Gains and Losses, the Consolidated Balance Sheet, the Parent Company Balance Sheet, the Consolidated Cash Flow Statement and the related notes. These financial statements have been prepared in accordance with the accounting policies set out therein. 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 any responsibility to anyone other than the Company and the Company's members as a body, for our 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 and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements. The information given in the Director's Report includes that specific information presented in the Chairman's Statement that is cross referenced from the Business Review section of the Directors' Report.

In addition we report to you if, in our opinion, 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 other transactions is not disclosed.

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

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the Group's and 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 financial statements and the part of the Directors' Remuneration Report 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 financial statements and the part of the Directors' Remuneration Report to be audited.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE CHARACTER GROUP plc CONTINUED

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Group's and the Parent Company's affairs as at 31 August 2007 and of the Group's profit for the year then ended;
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

HLB Vantis Audit plc
Registered Auditors
Chartered Accountants
82 St John Street
London
EC1M 4JN
17 December 2007

CONSOLIDATED PROFIT AND LOSS ACCOUNT

for the year ended 31 August 2007

	Note	Total 2007 £000's	Total 2006 (restated) £000's
Turnover — continuing		**94,523**	69,546
— discontinued		**–**	25,986
	2	**94,523**	95,532
Cost of sales		**(57,051)**	(66,543)
Gross profit		**37,472**	28,989
Net operating expenses			
Selling and distribution costs		**(10,098)**	(11,737)
Administration expenses		**(15,466)**	(13,894)
Other operating income		**151**	261
Operating profit/(loss) — continuing		**12,059**	6,912
— discontinued		**–**	(3,293)
Operating profit	3	**12,059**	3,619
Exceptional item — discontinued activity			
Gain before goodwill write-back		**–**	4,053
Goodwill charge		**–**	(1,897)
	3		2,156
Profit on ordinary activities before interest		**12,059**	5,775
Interest	5	**(282)**	(644)
Profit on ordinary activities before taxation		**11,777**	5,131
Taxation	6	**(3,653)**	(2,139)
Profit on ordinary activities after taxation		**8,124**	2,992
Earnings/(loss) per share	8		
— Basic — continuing		**17.93p**	8.36p
— discontinued		**–**	(2.56)p
		17.93p	5.80p
— Fully diluted — continuing		**17.39p**	8.32p
— discontinued		**–**	(2.55)p
		17.39p	5.77p
Dividend per share	7	**4.4p**	3.3p
Continuing business			
EBITDA (earnings before interest, tax, depreciation and amortisation)		**12,834**	7,456

There are no material recognised gains or losses other than the profit for the year disclosed above.

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

for the year ended 31 August 2007

	note	**12 months to 31 August 2007 £000's**	12 months to 31 August 2006 (restated) £000's
Profit for the financial period		**8,124**	2,992
Foreign exchange differences		**23**	18
Total recognised gains and losses relating to the financial period		**8,147**	3,010
Prior year adjustment	17	**(68)**	–
Total recognised gains and losses since last annual report		**8,079**	3.010

CONSOLIDATED BALANCE SHEET

as at 31 August 2007

	note	2007 £000's	2006 (restated) £000's
Fixed assets			
Intangible assets	9	**–**	400
Tangible assets	10	**1,494**	1,609
Investments	11	**–**	2
		1,494	2,011
Current assets			
Stocks	12	**10,831**	10,671
Trade debtors subject to finance arrangements		**18,249**	11,813
Finance advances		**(8,784)**	(6,275)
		9,465	5,538
Debtors — including non-financed trade debtors	13	**3,054**	9,474
Cash at bank and in hand		**15,658**	7,369
		39,008	33,052
Creditors: amounts falling due within one year	14	**(26,685)**	(23,324)
Net current assets		**12,323**	9,728
Total assets less current liabilities		**13,817**	11,739
Net assets		**13,817**	11,739
Capital and reserves			
Called up share capital	18	**2,273**	2,452
Shares held in treasury	18	**(676)**	(665)
Investment in own shares	24	**(908)**	(908)
Capital redemption reserve	18	**448**	243
Share based payment reserve	18	**315**	68
Share premium account	18	**12,568**	11,917
Merger reserve	18	**651**	651
Profit and loss account	18	**(854)**	(2,019)
Shareholders' funds	18	**13,817**	11,739

The accounts on pages 20 to 43 were approved by the Board of directors on 31 October 2007.

R King
Director

K P Shah
Director

PARENT COMPANY BALANCE SHEET

as at 31 August 2007

	Note	2007 £000's	2006 (restated) £000's
Fixed assets			
Tangible assets	10	**794**	835
Investments	11	**1,299**	3,195
		2,093	4,030
Current assets			
Debtors	13	**11,967**	11,618
Cash at bank and in hand		**2,685**	2,887
		14,652	14,505
Creditors: amounts falling due within one year	14	**(675)**	(1,657)
Net current assets		**13,977**	12,848
Total assets less current liabilities		**16,070**	16,878
Net Assets		**16,070**	16,878
Capital and reserves			
Called up share capital	16	**2,273**	2,452
Shares held in treasury	18	**(676)**	(665)
Investment in own shares	24	**(908)**	(908)
Capital redemption reserve	18	**448**	243
Share premium account	18	**12,568**	11,917
Share based payment reserve	18	**82**	17
Profit and loss account	18	**2,283**	3,822
Shareholders' funds	18	**16,070**	16,878

The accounts on pages 20 to 43 were approved by the Board of directors on 31 October 2007.

R King
Director

K P Shah
Director

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 August 2007

	note	2007 £000's	2006 £000's
Cash inflow from operating activities	20	**15,702**	5,995
Returns on investment and servicing of finance			
Interest received		**45**	76
Interest paid		**(327)**	(720)
Net cash outflow for returns on investment and servicing of finance		**(282)**	(644)
Taxation		**(1,043)**	(228)
Capital expenditure and financial investment			
Payments to acquire tangible fixed assets		**(288)**	(876)
Sale of investments		**3**	–
Sale of tangible fixed assets		**19**	397
Net cash outflow for capital expenditure and financial investment		**(266)**	(479)
Equity dividends paid		**(1,625)**	(1,258)
Acquisition and disposal			
Sale of business		**496**	3,178
Cash inflow before financing		**12,982**	6,564
Shares held in treasury (including expenses)		**434**	(672)
Issue of new shares		**225**	110
Repurchase of own shares for cancellation		**(5,352)**	(2,381)
Net cash (outflow) from financing		**(4,693)**	(2,943)
Increase in cash in the year		**8,289**	3,621
Increase in net funds in the year	21	**8,289**	3,621

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 comparative amounts have been restated to take account of the requirements of Financial Reporting Standard ("FRS") 20 "Share-based payment" in respect of dividends.

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

Basis of consolidation

The Group accounts for the year ended 31 August 2007 comprise the accounts of the Company and its subsidiaries, all of which are made up to the end of the Company's financial year.

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 18 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 and intangible assets", 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, or less if in the opinion of the directors estimated useful economic life is shorter. 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 "Goodwill and intangible assets".

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 stated at cost less provision for impairment. Provision is made against investments where 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.

Finance and invoice discounting arrangements

Certain group companies have agreements under which debts approved by the finance company are assigned to them without recourse. Non-refundable advances are made by the finance company. The Company has no obligation and the directors do not intend that the Company will support any losses from such 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 "Reporting the substance of transactions". The finance company has a debenture over the assets of the Company and certain group companies. The finance charges are charged to the profit and loss account as they accrue. The amount charged to the profit and loss in the year was £397,000 (2006: £458,000). Of this amount, £201,000 (2006: £197,000) has been charged as interest (see note 5), with the remainder being charges made by the finance company which have been included within administration expenses.

1 PRINCIPAL ACCOUNTING POLICIES CONTINUED

FRS 20: Share-based payment

During the year the Group has adopted FRS20 "Share-based payment", which applies to AIM listed companies for accounting periods commencing on or after 1 January 2006.

The Group has a number of employee share option schemes, detailed in note 16.

The fair value of employee share option plans is measured at the date of grant of the option using a binomial valuation model taking into account the terms and conditions under which the option was granted. Options vest subject to the employee remaining in service during the vesting period and that the relevant non market related performance conditions are met. The fair value determined is expensed on a straight line basis over the vesting period, based upon the Group's estimate of the number of shares that will vest. The estimate of vesting is reviewed annually with any impact on the cumulative charge being recognised immediately. The charge in respect of share-based payments is matched by an equal and opposite adjustment to profit and loss reserves, thereby having no net impact on the Group's closing reserves.

The Group has taken advantage of the transitional provisions of FRS 20 "Share-based payment" in respect of the fair value of equity settled awards so as to apply FRS 20 "Share-based payment" only to those equity settled awards granted after 7 November 2002 that had not vested before 1 September 2006.

The adoption of FRS 20 "Share-based payment" has resulted in a change in accounting policy for share-based payments. A prior year adjustment has been made to the financial information for the year ended 31st August 2006, details of which are given in note 17.

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. Debt instruments are initially stated at the amount of the net proceeds after deduction of issue costs. The carrying amount is increased by the finance cost and reduced by payments made in the year. 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 exemptions from disclosure in accordance with FRS 13 "Derivatives and other financial instruments: disclosures" 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.

1 PRINCIPAL ACCOUNTING POLICIES CONTINUED

Deferred tax assets in excess of liabilities are recognised to the extent that, in the directors' opinion, it is more likely than not that suitable taxable profits will arise from which the underlying timing differences can be deducted.

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.

2 TURNOVER

a) 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. An analysis of turnover by geographical market is given below:

	Continuing 31 August 2007 £000's	**Discontinued 31 August 2007 £000's**	**Total 31 August 2007 £000's**	Continuing 31 August 2006 (restated) £000's	Discontinued 31 August 2006 £000's	Total 31 August 2006 (restated) £000's
United Kingdom: Group	**85,796**	–	**85,796**	61,222	216	61,438
Rest of the world: Group	**8,727**	–	**8,727**	8,324	25,770	34,094
Total Group	**94,523**	–	**94,523**	69,546	25,986	95,532

b) Operating profit / (loss)

	Continuing 31 August 2007 £000's	**Discontinued 31 August 2007 £000's**	**Total 31 August 2007 £000's**	Continuing 31 August 2006 (restated) £000's	Discontinued 31 August 2006 £000's	Total 31 August 2006 (restated) £000's
Turnover	**94,523**	–	**94,523**	69,546	25,986	95,532
Cost of sales	**(57,051)**	–	**(57,051)**	(40,625)	(25,918)	(66,543)
Gross profit	**37,472**	–	**37,472**	28,921	68	28,989
Selling and distribution costs	**(10,098)**	–	**(10,098)**	(9,749)	(1,988)	(11,737)
Administrative expenses	**(15,466)**	–	**(15,466)**	(12,464)	(1,430)	(13,894)
Other operating income	**151**	–	**151**	204	57	261
Operating profit / (loss)	**12,059**	–	**12,059**	6,912	(3,293)	3,619

The Group's digital activities during the 12 months ended 31 August 2006 are classed as discontinued. 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 2007 £000's	12 months to 31 August 2006 £000's
Operating profit is stated after charging:			
Staff costs	4	**7,358**	7,231
Group Auditors' remuneration			
— Statutory audit services		**44**	48
— Financial reporting advisory services		**10**	10
— Tax compliance services		**–**	10
— Tax advisory services		**–**	5
— Further assurance services		**–**	35
Other Auditors' remuneration			
— Statutory audit services		**29**	25
— Tax compliance services		**6**	–
— Tax advisory services		**4**	5
Total fees payable to Auditors		**93**	138
Operating leases — land and buildings		**171**	180
Research and development costs		**–**	1,274
Depreciation of tangible fixed assets			
— owned assets		**375**	528
Goodwill amortisation		**400**	246

2006: Exceptional item

The exceptional gain of £2,156,000 relates to the disposal of the Group's digital activities. It is stated after charging goodwill previously written-off of £1,897,000 and associated costs on the disposal of the digital operation amounting to £4,384,000. 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 reserves.

4 DIRECTORS AND EMPLOYEES

	12 months to 31 August 2007 £000's	12 months to 31 August 2006 (restated) £000's
Staff costs including directors' emoluments		
Wages and salaries	**6,813**	6,501
Social security costs	**460**	431
Other pension costs	**332**	367
	7,605	7,299
The average number of employees during the year was:	**Number**	Number
Management and administration	**63**	65
Selling and distribution	**97**	142
	160	207

Of the total average number of employees, 105 were based in the UK and 55 in Hong Kong and mainland China.

The amount payable to pension schemes as at the balance sheet date was £156,000 (2006: £nil).

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 2007 £000's	12 months to 31 August 2006 £000's
Total interest receivable	**149**	76
Total interest payable:		
On bank overdraft and similar charges	**(174)**	(511)
Factor and invoice discounting advances	**(201)**	(197)
Other	**(56)**	(12)
	(282)	(644)

6 TAXATION

	12 months to 31 August 2007 £000's	12 months to 31 August 2006 (restated) £000's
UK Corporation Tax		
Tax on profit for the period	**2,969**	–
Adjustments to tax charge in respect of previous periods	**(19)**	–
Total UK corporation tax	**2,950**	–
Foreign Tax		
Tax on profit for the period	**870**	510
Adjustments to tax charge in respect of previous periods	**4**	(28)
Total foreign tax	**874**	482
Total current tax	**3,824**	482
Deferred Tax		
Tax losses utilised	**–**	1,731
Origination and reversal of timing differences	**(171)**	(74)
Total deferred tax	**(171)**	1,657
Tax on profit on ordinary activities	**3,653**	2,139
Factors affecting tax charge for the period		
Profit on ordinary activities before taxation	**11,777**	5,131
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2006: 30%)	**3,533**	1,539
Effects of:		
Expenses not deductible for tax purposes	**207**	251
Capital allowances (in excess of)/less than depreciation	**(11)**	54
Deduction for employee share options exercised	**(122)**	(68)
Other temporary differences between taxable and accounting profit	**248**	128
Overseas income not subject to tax	**–**	(1,345)
Goodwill charge not deductible	**120**	569
Lower tax rate on overseas earnings	**(581)**	(561)
Utilisation of tax losses	**(26)**	(1,667)
Tax losses not utilised	**37**	957
Adjustments to tax charge in respect of previous periods	**(15)**	(27)
Remitted earnings of overseas subsidiaries	**434**	652
Current tax charge for the year	**3,824**	482

7 DIVIDEND

	12 months to 31 August 2007 £000's	12 months to 31 August 2006 £000's
On equity shares:		
Final dividend paid for the year ended 31 August 2006		
— 1.65 pence (2005: 0.9 pence) per share	**733**	473
Interim dividend paid for the year ended 31 August 2007		
— 2.00 pence (2006: 1.65 pence) per share	**892**	785
	1,625	1,258
Proposed final dividend for the year ended 31 August 2007		
of 2.4 pence per share (2006: 1.65 pence)	**1,060**	791

8 EARNINGS / (LOSS) PER SHARE

	12 months to 31 August 2007			12 months to 31 August 2006 (Restated)		
	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	**8,124,000**	**45,298,688**	**17.93**	2,992,000	51,629,312	5.80
Impact of share options	**–**	**1,408,453**	**(0.54)**	–	221,975	(0.03)
Diluted earnings per share	**8,124,000**	**46,707,141**	**17.39p**	2,992,000	51,851,287	5.77

Earnings per share for year ended 31 August 2007 relate solely to continuing activities. The analysis of earnings per share between continuing and discontinued activities for year ended 31 August 2006 is as follows:

Year Ended 31 August 2006 (restated)

	CONTINUING			DISCONTINUED		
	Profit after taxation	Weighted average number of ordinary shares	Pence per share	Loss after taxation	Weighted average number of ordinary shares	Pence per share
Basic earnings/(loss) per share	4,314,000	51,629,312	8.36	(1,322,000)	51,629,312	(2.56)
Impact of share options	–	221,975	(0.04)	–	221,975	0.01
Diluted earnings per share	4,314,000	51,851,287	8.32	(1,322,000)	51,851,287	(2.55)

Comparatives for 2006 have been restated in accordance with FRS22 "Earnings per share".

9 INTANGIBLE FIXED ASSETS — GOODWILL

The Group

Cost	**£000's**
1 September 2006 and 31 August 2007	902
Amortisation	
1 September 2006	502
Charge for the year	400
31 August 2007	**902**
Net book value	
31 August 2007	–
31 August 2006	400

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 2006	1,182	118	26	1,912	371	3,609
Additions	–	4	–	232	52	288
Disposals	–	(28)	–	(248)	(59)	(335)
Differences on exchange	–	(5)	–	(14)	–	(19)
31 August 2007	1,182	89	26	1,882	364	3,543
Depreciation						
1 September 2006	353	85	26	1,379	157	2,000
Charge for the year	39	27	–	221	88	375
Disposals	–	(28)	–	(248)	(40)	(316)
Exchange rate movement	–	(3)	–	(7)	–	(10)
31 August 2007	392	81	26	1,345	205	2,049
Net book value						
31 August 2007	790	8	–	537	159	1,494
31 August 2006	829	33	–	533	214	1,609

The Company

Cost	Freehold land and buildings £000's	Fixtures, fittings and equipment £000's	Total £000's
1 September 2006	1,182	133	1,315
Additions	–	2	2
31 August 2007	**1,182**	**135**	**1,317**
Depreciation			
1 September 2006	353	127	480
Charge for the year	39	4	43
31 August 2007	**392**	**131**	**523**
Net book value			
31 August 2007	**790**	**4**	**794**
31 August 2006	829	6	835

11 FIXED ASSET INVESTMENTS

The Group

Cost	Shares listed in the UK £000's
1 September 2006	2
Disposals	(2)
31 August 2007	–
Amortisation and Provisions	
1 September 2006 and 31 August 2007	–
Net book value	
31 August 2007	–
31 August 2006	2

The listed investments were disposed during the year. The market value of the listed investments in 2006 was £1,330.

The Company

Cost	Shares in subsidiary undertakings £000's
1 September 2006 and 31 August 2007	3,195
Amortisation and Provisions	
1 September 2006	–
Charge for the year	1,896
31 August 2007	1,896
Net book value	
31 August 2007	**1,299**
31 August 2006	3,195

At 31 August 2007, 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 toys and games
Character Gifts Limited	United Kingdom	Ordinary	100%	Gift importer and distributor

World Wide Licenses Limited, WWL (Europe) Limited and Character Games (Far East) Limited are no longer principal undertakings. All of the subsidiary undertakings have been included in these consolidated accounts.

12 STOCKS

	The Group 2007 £000's	The Group 2006 £000's
Finished goods for resale	**10,831**	10,671

13 DEBTORS

	The Group 2007 £000's	The Group 2006 £000's	The Company 2007 £000's	The Company 2006 £000's
Due from subsidiary undertakings	**–**	–	**11,694**	10,846
Trade debtors (non-financed)	**968**	3,760	**–**	–
Other debtors	**843**	4,435	**62**	189
Prepayments and accrued income	**1,243**	1,279	**207**	231
Other taxation and social security	**–**	–	**4**	352
	3,054	9,474	**11,967**	11,618

During the year advances were made to R. King totaling £190,000. As at 31 August 2007 the amount due by R. King to the Group was £100,000. Included within creditors at that date is an amount of £110,000 due to R. King in respect of bonus entitlement.

14 CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	The Group 2007 £000's	The Group 2006 £000's	The Company 2007 £000's	The Company 2006 £000's
Trade creditors	**10,327**	13,809	**–**	–
Bills of exchange payable	**4,728**	3,687	**–**	–
Due to subsidiary undertakings	**–**	–	**15**	126
Corporation tax	**3,187**	578	**–**	7
Other taxation and social security	**1,052**	360	**–**	–
Accruals and deferred income	**7,391**	3,540	**660**	174
Loan	**–**	1,350	**–**	1,350
	26,685	23,324	**675**	1,657

A bank has a debenture over the assets and undertakings of the Company and certain group companies. Also, certain group companies pledge cash deposits with banks which provide mainly trade finance facilities, and such amounts are included in cash at bank and in hand. At 31 August 2007, the pledged deposits amounted to £759,000 (2006: £777,000). Further, a major trade creditor who offers trade finance is secured by a debenture over the assets and undertakings of a group company. As at 31 August 2007 the amount outstanding to the secured trade creditor amounted to £nil (2006: £763,000).

The movements in deferred tax are as follows:

	2007 £000's	2006 £000's
At 1 September 2006	**(171)**	1,486
Profit and loss account	**171**	(1,657)
At 31 August 2007	**–**	(171)

Deferred tax assets have not been recognised in respect of tax losses of £ 6,083,000 (2006: £6,932,000). At tax rates of either 17.5% or 30%, these losses represent a potential tax asset of £1,319,000 (2006: £1,541,810). These losses would be recoverable in the event of taxable profits arising in certain subsidiary companies.

15 RECONCILIATION OF EQUITY SHAREHOLDERS' FUNDS

	The Group 2007 £000's	The Group 2006 (restated) £000's	**The Company 2007 £000's**	The Company 2006 (restated) £000's
At 1 September 2006 restated	**11,739**	10,965	**16,878**	15,228
Profit for the financial period	**8,124**	2,992	**5,443**	5,834
Share based payment reserve	**247**	68	**65**	17
Write-back of goodwill previously written off	**–**	1,897	**–**	–
Exchange difference taken to reserves	**23**	18	**–**	–
Dividends paid	**(1,625)**	(1,258)	**(1,625)**	(1,258)
Shares issued	**225**	110	**225**	110
Repurchase of own shares for cancellation	**(5,351)**	(2,388)	**(5,351)**	(2,388)
Shares held in treasury	**435**	(665)	**435**	(665)
Net addition to/(subtraction from) shareholders' funds	**2,078**	774	**(808)**	1,650
Closing shareholders' funds	**13,817**	11,739	**16,070**	16,878

16 CALLED UP SHARE CAPITAL (EQUITY)

	2007 **£000's**	2006 £000's
Authorised		
110,000,000 (2006: 110,000,000) ordinary shares of 5 pence each	**5,500**	5,500
Allotted, called up and fully paid		
45,452,937* (2006: 49,048,909) ordinary shares of 5 pence each	**2,273**	2,452

* Including 1,000,000 ordinary shares held in treasury (2006: 1,125,000).

Share capital movements in the year

491,750 ordinary shares of 5 pence each (total nominal value £24,588) were issued during the year to employees and ex-employees exercising their share options as follows:

Date	**Number of ordinary shares at exercise price**			
	24.25p	54.00p	101.00p	136.50p
24 August 2006	46,500	74,750		
4 September 2006	1,000			
28 November 2006		8,500		
29 November 2006	1,500	6,500		
1 December 2006	1,000	32,500		
5 December 2006	2,500	1,000		
6 December 2006	7,000	2,250		
11 December 2006	10,000			
13 December 2006	7,500	10,000		
18 December 2006			4,000	
19 December 2006		1,500		
20 December 2006	13,000	19,000		
21 December 2006	4,000	2,250		
28 December 2006	5,000			
12 January 2007			4,000	
22 January 2007		1,000		
31 January 2007	1,000	1,000	2,000	
7 February 2007		5,000		
9 February 2007				3,000
12 February 2007	6,000	16,750		
15 February 2007	2,000	4,500		
20 February 2007		2,500		
26 February 2007			8,000	
6 March 2007	53,500	6,000		
7 March 2007		2,500		
4 April 2007		11,250		
26 April 2007	7,676			
30 April 2007	10,000	10,000		
3 May 2007		10,000		
8 May 2007		43,000		
9 May 2007	1,000	1,000		
19 July 2007		7,000		
20 July 2007	824	7,000		
27 July 2007				3,000

16 CALLED UP SHARE CAPITAL (EQUITY) CONTINUED

Share Capital movements in the year (continued)

During the year, the Company repurchased for cancellation 4,087,722 ordinary shares of 5 pence each as follows:

Date	Number of shares	Price	% of the issued share capital immediately prior to cancellation (excluding shares held in Treasury)
29-Nov-06	1,696,000	102.02 pence	3.58%
29-Nov-06	1,000,000	102.00 pence	2.19%
05-Dec-06	100,000	103.00 pence	0.22%
06-Dec-06	45,000	104.56 pence	0.10%
24-Apr-07	190,000	200.00 pence	0.42%
27-Apr-07	100,000	199.50 pence	0.22%
01-May-07	479,322	199.50 pence	1.06%
02-May-07	250,000	198.00 pence	0.56%
08-Jun-07	65,000	167.62pence	0.15%
11-Jun-07	100,000	167.45pence	0.22%
26-Jun-07	50,000	150.00pence	0.11%
28-Jun-07	12,400	160.00pence	0.03%

During the year, the Company repurchased 650,000 ordinary shares to be held as Treasury shares as follows:

Date	Number of shares	Price	% of the issued share capital immediately prior to cancellation (excluding shares held in Treasury)
27 September 2006	629,322	75 pence	1.31%
1 May 2007	20,678	199.5 pence	0.05%

On 31 January 2007, a total of 775,000 ordinary shares from Treasury were sold at a price of 123.5 pence per share.

Share options

The Company adopted the rules of an Inland Revenue approved executive share option scheme (the "1995 Scheme") on 3 May 1995. The 1995 Scheme terminated on 3 May 2005 but such termination has not affected the status of options granted under it prior to that date.

The Company adopted the rules of its unapproved executive share option scheme (the "1997 Scheme") on 2 June 1997. The directors resolved that no further options would be granted under the 1997 Scheme on or after 22 February 2006 but such resolution has not affected the status of options granted under it prior to that date.

The Company adopted the rules of an Inland Revenue qualifying Enterprise Management Incentive share option scheme (the "EMI 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 were granted to Group employees under the 1995 Scheme at an exercise price of 54 pence per share.

The Company adopted the rules of an Inland Revenue Share Option Plan (the "2006 Scheme") on 22 February 2006. On 11 May 2006, options over a total of 960,000 new ordinary shares of 5 pence each were granted under the 2006 Scheme to executive directors at an exercise price of 63 pence per share. On 15 May 2006, options over a total of 1,093,250 new ordinary shares of 5 pence each were granted under the 2006 Scheme to Group employees at an exercise price of 63 pence per share. On 18 August 2006, options over a total of 100,000 new ordinary shares of 5 pence each were granted under the 2006 Scheme to a Group employee at an exercise price of 66 pence per share.

On 11 July 2006, unapproved non-scheme options ("Non-Scheme Options") over a total of 165,000 new Ordinary Shares of 5 pence each were granted to Group employees at an exercise price of 63.25 pence per share. Such options are exercisable from 21 December 2007 until 19 December 2014.

16 CALLED UP SHARE CAPITAL (EQUITY) CONTINUED

At 31 August 2007 rights to options over 2,812,500 ordinary shares of the company were outstanding as follows:

	At 1 September 2006	Granted	Exercised/ lapsed	Cancelled	At 31 August 2007	Exercise Price	Exercise Period
1995 Scheme							
	20,000	–	(20,000)	–	–	101.0p	5 March 2000 to 4 March 2007
	13,500	–	(7,500)	–	6,000	136.5p	5 December 2000 to 4 December 2007
	196,000	–	(165,000)	–	31,000	24.25p	15 February 2005 to 14 February 2012
1997 Scheme							
	59,250	–	(53,500)	–	5,750	24.25p	15 February 2005 to 14 February 2009
	147,000	–	(115,250)	–	31,750	54.0p	6 February 2006 to 5 February 2010
EMI Scheme							
	622,250	–	(173,750)	–	448,500	54.0p	5 February 2006 to 4 February 2013
2006 Scheme							
	960,000	–	–	–	960,000	63.0p	11 May 2009 to 10 May 2016
	1,089,500	–	(25,000)	–	1,064,500	63.0p	15 May 2009 to 14 May 2016
	100,000	–	–	–	100,000	66.0p	18 August 2009 to 17 August 2016
	165,000	–	–	–	165,000	63.25p	21 December 2007 to 19 December 2014
	3,372,500		(560,000)	–	2,812,500		

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

17 SHARE-BASED PAYMENT

The Group has taken advantage of the transitional arrangements of FRS 20 "Share-based payment" in respect of the fair value of equity settled awards so as to apply FRS 20 "Share-based payment" only to those equity settled awards granted after 7 November 2002 and that had not vested before 1 September 2006.

A charge has been made for the year ended 31 August 2007 and a prior year adjustment has been made to the financial information for the year ended 31 August 2006 as detailed below:

	12 months ended 31 August 2007 £'000	12 months ended 31 August 2006 £'000
Charge for share based payment	247	68

17 SHARE-BASED PAYMENT CONTINUED

The fair value of equity settled awards has been estimated at the date of grant using a binomial valuation model for which the inputs are summarised below:

Grant Date	11 May 2006	15 May 2006	11 July 2006	18 August 2006
Options outstanding 1 September 2006	960,000	1,089,500	165,000	100,000
Lapsed	–	(25,000)	–	–
Options outstanding 31 August 2007	960,000	1,064,500	165,000	100,000
Contract term year(s)	10	10	8.5	10
Expected life of option	6	6	6	6
Exercise & share price at grant	63.0p	63.0p	63.25p	66.0p
Expected volatility	55% – 65%	55% – 65%	55% – 65%	55% – 65%
Annual risk free rate	4.425%	4.425%	4.690%	4.74%
Annual expected dividend	2% – 3%	2% – 3%	2% – 3%	2% – 3%
Fair value per share under option	32p	32p	32p	33p

Expected volatility was determined by calculating the historical volatility of the Group's share price over the previous 3 years. The expected life used in the model has been adjusted, based upon management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations. Option valuations are based upon the assumption that the dividend remains at this level in the future.

The share options, when exercised, shall have similar dividend and voting rights as the ordinary issued share capital.

18 SHARE CAPITAL AND RESERVES

	Called up share capital £000's	Treasury shares	Capital redemption reserve £000's	Share premium account £000's	Merger reserve £000's	Share Based Payment £000's	Profit and loss account £000's
The Group							
1 September 2006 as originally stated	2,452	(665)	243	11,917	651	–	(1,951)
Share-based payment	–	–	–	–	–	68	(68)
At 1 September 2006 restated	**2,452**	**(665)**	**243**	**11,917**	**651**	**68**	**(2,019)**
Share-based payment	–	–	–	–	–	247	–
Exchange differences	–	–	–	–	–	–	23
Profit after tax	–	–	–	–	–	–	8,124
Dividends	–	–	–	–	–	–	(1,625)
Shares issued	25	–	–	200	–	–	–
Sale of treasury shares	–	502	–	451	–	–	–
Shares cancelled and capitalised	(204)	(513)	205	–	–	–	(5,357)
31 August 2007	**2,273**	**(676)**	**448**	**12,568**	**651**	**315**	**(854)**
The Company							
1 September 2006 as originally stated	2,452	(665)	243	11,917	–	–	3,839
Share-based payment	–	–	–	–	–	17	(17)
At 1 September 2006 restated	**2,452**	**(665)**	**243**	**11,917**	**–**	**17**	**3,822**
Share-based payment	–	–	–	–	–	65	–
Profit after tax	–	–	–	–	–	–	5,443
Dividends	–	–	–	–	–	–	(1,625)
Shares issued	25	–	–	200	–	–	–
Sale of treasury shares	–	502	–	451	–	–	–
Shares cancelled and capitalised	(204)	(513)	205	–	–	–	(5,357)
31 August 2007	**2,273**	**(676)**	**448**	**12,568**	**–**	**82**	**2,283**

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 £3,748,000 (31 August 2006: £3,748,000). 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.

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 2007.

	2007 Land and buildings £000's	2006 Land and buildings £000's
Expiring within one year	**57**	95
Expiring between one and five years	**76**	99
	133	194

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:

	2007 £000's	2006 £000's
Within one year	**109**	298
Between one and two years	**385**	23
Between two and five years	**7**	45
	501	366

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

	12 months to 31 August 2007 £000's	12 months to 31 August 2006 (restated) £000's
Operating profit	**12,059**	3,619
Depreciation, impairment and amortisation	**775**	774
Profit on sale of investments	**(1)**	–
Loss on disposal of fixed assets	**–**	168
Share-based payment	**247**	68
(Increase) in stocks	**(160)**	(861)
Decrease in debtors	**1,997**	8,411
Increase/(decrease) in creditors	**753**	(6,225)
Exchange movement	**32**	41
Net cash inflow from operating activities	**15,702**	5,995

RECONCILIATION OF EXCEPTIONAL PROFIT TO NET CASH INFLOW FROM EXCEPTIONAL ACTIVITIES

	12 months to 31 August 2007 £000's	12 months to 31 August 2006 £000's
Exceptional profit	–	2,156
Write-back of goodwill previously written off	–	1,897
Decrease/(increase) in debtor	496	(948)
Increase in creditors	–	73
Net cash inflow from exceptional activities	496	3,178

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

21 RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	12 months to 31 August 2007 £000's	12 months to 31 August 2006 £000's
Increase in cash in the period	8,289	3,621
Movement in net funds resulting from cash flows	8,289	3,621
Net funds at 1 September 2006	7,369	3,748
Net funds at 31 August 2007	**15,658**	7,369

22 ANALYSIS OF NET FUNDS

	Cash at bank and in hand £000's	Total £000's
1 September 2005	3,748	3,748
Cash flow	3,621	3,621
31 August 2006	7,369	7,369
Cash flow	8,289	8,289
31 August 2007	15,658	15,658

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 13. As permitted by FRS 13 "Derivatives and other financial instruments: disclosures", 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:

	At 31 August 2007 Functional currency of Group operation			At 31 August 2006 Functional currency of Group operation		
Net foreign currency monetary assets	Sterling £000's	HK$ £000's	Total £000's	Sterling £000's	HK$ £000's	Total £000's
Sterling	–	–	–	–	6	6
US$	**262**	**326**	**588**	202	1,916	2,118
Euro	**21**	–	**21**	13	–	13
Chinese renminbi	–	**5**	**5**	–	18	18
Total	**283**	**331**	**614**	215	1,940	2,155

b. Fair values

The fair values of all financial instruments at 31 August 2007 and 31 August 2006 were not materially different from their book values.

23 FINANCIAL INSTRUMENTS CONTINUED

c. Borrowing facilities

The Group has available various borrowing facilities. The undrawn committed facilities available in respect of which all conditions had been met at 31 August 2007, were as follows:

	2007 £000's	2006 £000's
Expiring within one year	3,368	5,642
Total	3,368	5,642

d. Interest rate risk profile of financial assets and financial liabilities

Financial assets

Financial assets comprise cash at bank.

	At 31 August 2007				At 31 August 2006			
Currency	Floating rate financial assets £000's	Fixed rate financial assets £000's	Financial assets on which no interest received £000's	Total £000's	Floating rate financial assets £000's	Fixed rate financial assets £000's	Financial assets on which no interest received £000's	Total £000's
Sterling	14,171	–	–	14,171	4,493	–	–	4,493
US$	588	–	–	588	2,117	–	–	2,117
Euro	21	–	–	21	13	–	–	13
HK$	873	–	–	873	728	–	–	728
Chinese renminbi	5	–	–	5	18	–	–	18
Total	15,658	–	–	15,658	7,369	–	–	7,369

Financial liabilities

	At 31 August 2007				At 31 August 2006			
Currency	Floating rate financial liabilities £000's	Fixed rate financial liabilities £000's	Financial liabilities on which no interest is paid £000's	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	Total £000's
Sterling	–	–	–	–	–	1,350	–	–
Euro	–	–	–	–	–	–	–	–
HK$	–	–	–	–	–	–	–	–
Total	–	–	–	–	–	1,350	–	–

The fixed rate financial liability comprised a loan. Interest was payable at the rate of 5% per annum.

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 2007, the Trust held 285,000 ordinary shares (2006: 285,000), which had a market value of £489,000 (2006: £219,450), and has waived its right to dividend income thereon. The cost of these shares was £908,000. At 31 August 2007, no options had been granted by the Trust.

25 CONTINGENT LIABILITIES

The Company has guaranteed the obligations of certain subsidiary companies to their finance companies, trade finance companies, certain banks and others in the normal course of business. The finance 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.

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the thirteenth Annual General Meeting of The Character Group plc ("Company") will be held at the offices of Citigate Dewe Rogerson, 3 London Wall Buildings, London Wall, London EC2M 5SY on16 January 2008 at 11 a.m. to transact the following business:

ORDINARY BUSINESS

1. To approve the Directors' Remuneration Report for the year ended 31 August 2007.
2. To receive and adopt the Directors' Report and the Accounts of the Company for the year ended 31 August 2007 and the report of the Auditors thereon.
3. To declare a final dividend on the ordinary shares in the capital of the Company (other than ordinary shares held by the Company in treasury) for the year ended 31 August 2007 of 2.4p per share.
4. To consider an ordinary resolution of the Company that Lord Birdwood, who retires in accordance with the terms of his letter of appointment, be and is hereby re-elected as a director of the Company.
5. To consider an ordinary resolution of the Company that Mr. I.S. Fenn, who retires in accordance with the terms of his letter of appointment, be and is hereby re-elected as a director of the Company.
6. To consider an ordinary resolution of the Company that Mr. D. Harris, who retires in accordance with the terms of his letter of appointment, be and is hereby re-elected as a director of the Company.
7. To consider an ordinary resolution of the Company that Mr. A. B. MacKay, who retires in accordance with the terms of his letter of appointment, be and is hereby re-elected as a director of the Company.
8. To reappoint HLB Vantis Audit plc as auditors of the Company and to authorise the directors to fix their remuneration.

SPECIAL BUSINESS

To consider and, if thought fit, to pass the following resolutions of the Company:

Ordinary Resolutions

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 £740,800, 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 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 of 5p each in the capital of the Company hereby authorised to be acquired is 11,113,200;
    (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;
    (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 pursuant of any such contract.

Special Resolutions

12. That:

(A) the Company may send or supply any document or information that is required or authorised to be sent or supplied by the Company:

(i) under the Companies Acts (as defined in section 2 of the Companies Act 2006 (the "2006 Act")); or

(ii) pursuant to the Company's Articles of Association; or

(iii) pursuant to any other rules or regulations to which the Company may be subject; by making it available on a website;

(B) the relevant provisions of the 2006 Act, which apply when documents sent under the Companies Acts are made available on a website, shall also apply, with any necessary changes, when any document or information is sent or supplied under the Company's Articles of Association or other rules or regulations to which the Company may be subject;

(C) this Resolution shall supersede any provision of the Company's Articles of Association to the extent that it is inconsistent with this resolution; and

(D) any communication with a shareholder by making it available on the Company's website rather than through the supply of a hard copy of that communication to that shareholder's address (as set out in the register of members) shall be subject to that shareholder having agreed or been deemed to have agreed to such method of communication.

13. 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 and/or to sell equity securities held as treasury shares (within the meaning of section 162A of the Act) for cash in each case as if Section 89(1) of the Act did not apply to any such allotment or sale, provided that this power shall be limited:

(i) to the allotment and/or sale of equity securities in connection with any offer by way of rights to holders of ordinary shares in the capital of the Company (other than to the holder(s) of treasury shares) 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 paragraph (i) above) of equity securities up to an aggregate nominal value of £222,264;

(iii) the sale of (otherwise than pursuant to paragraph (i) above) of equity securities held as treasury shares up to an aggregate nominal value of £50,000 (equivalent to 1,000,000 ordinary shares of 5p each in the Company);

(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 and/or sale after such power expires and the directors may allot and/or sell 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 and/or sell 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.

By order of the Board,

K.P. Shah

Secretary

21 December 2007

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

NOTES:

1. The register of directors' interests and copies of the directors' service agreements or (as appropriate) their letters of appointment and the Articles of Association of the Company 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 10.00 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 or proxies to attend, speak and vote in his/her place. A member may only appoint more than one proxy if each proxy is appointed to exercise the voting rights attached to different shares. A member may not appoint more than one proxy to exercise rights attached to the same shares.
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 47.
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. For the purposes of Regulation 41 of the Uncertificated Securities Regulations 2001, the members entitled to attend, speak and/or vote at the Annual General Meeting shall be those entered on the Company's register of members at 11.00 a.m. on 14 January 2008. Changes to entries on the register of members after that time will be disregarded in determining the rights of any person to attend, speak and/or vote at the meeting.

FORM OF PROXY

THE CHARACTER GROUP plc

For use at the Annual General Meeting of the Company to be held on 16 January 2008 at 11 a.m.

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, 3 London Wall Buildings, London Wall, London EC2M 5SY on 16 January 2008 at 11 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 for the year ended 31 August 2007		
2. Ordinary resolution — adoption of accounts for year ended 31 August 2007		
3. Ordinary resolution — declaration of final dividend		
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 of Mr D. Harris as a director		
7. Ordinary resolution — re-election of Mr A. B. MacKay as a director		
8. Ordinary resolution — reappointment of HLB Vantis Audit plc as auditors to the Company		
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 — to enable the Company to send or supply documents or information to shareholders via a website		
13. Special resolution — disapplication of pre-emption rights		

Dated ______________________ Signature ______________________

NOTES:

1. 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.
2. A member may only appoint more than one proxy if each proxy is appointed to exercise the voting rights attached to different shares. A member may not appoint more than one proxy to exercise rights attached to the same shares.
3. If no indication is given as to how you wish your proxy/ies to vote, your proxy/ies will vote or abstain as he/she/they think(s) fit. On any other business arising at the meeting (including any motion to adjourn the meeting) the proxy/ies will act at his/her/their discretion.
4. 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.
5. 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 or other person duly authorised on its behalf.
6. 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.
7. To be effective, 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 the meeting. Completion of this form of proxy will not prevent the holder from attending, speaking and voting at the meeting in person should he so wish.
8. As permitted by Regulation 41 of the Uncertificated Securities Regulations 2001, members must be entered on the Company's register of members at 11.00 a.m. on 14 January 2008 in order to be entitled to attend, speak 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, speak and/or vote at the meeting 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

1

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

First fold

Third fold, then tuck in flap
and tape along edge