Digital Bros S.p.A.

Quarterly Report as at March 31, 2002

Notes to the consolidated information of Digital Bros S.p.A. for the quarter ended March 31, 2002

Methods used to prepare the consolidated quarterly accounts

The consolidated accounts for the quarter ended March 31, 2002 were prepared using the same criteria as were used for the consolidated financial statements for the year ended December 31, 2001 and for the consolidated accounts for the quarter ended March 31, 2001.

The consolidation area changed during the quarter following the merger of companies Game Channel S.p.A., Evolution Entertainment S.r.l. and Communications & Promotions S.r.l. into Digital Bros S.p.A.; the mergers took place on February 26, 2002 with effect for balance sheet and income statement purposes from January 1, 2002. The acquisition of 33% of Game Channel S.p.A. was effected by means of a share capital increase of Digital Bros S.p.A. involving the issue of 400,000 shares with a nominal value of Euro 0.13 each – a total of Euro 52,000 – in favour of minority shareholder Sem Moioli. As a result of the merger, the Game Network trademark, like all other trademarks owned by the Group, became directly owned by Digital Bros.

As a result of the above, the consolidation area at March 31, 2002 was as follows:

Company Name	Head Office	Currency	Share Capital	% interest held	Consolidation method
Digital Bros S.p.A.	Milan	Euro	1,677,000	Parent company	Line-by-line
Twine Holdings Ltd.	London	GBP	999	66.75	Line-by-line
Eon Digital Entertainment Ltd. (1)	London	GBP	999	66.75	Line-by-line
Game Network On line S.r.l.	Milan	Euro	500,000	100	Line-by-line
Game Network S.p.A.	Milan	Euro	1,149,900	100	Line-by-line
Game Network Ltd.	London	GBP	1	100	Line-by-line
AD1 S.r.l. (2)	Milan	Euro	10,000	100	Line-by-line

(1) Indirectly owned through subsidiary Twine Holdings Ltd.

(2) Indirectly owned through subsidiary Game Network S.p.A.

The balance sheet and financial information as at March 31, 2002 is compared with the corresponding amounts in the financial statements at December 31, 2001. Income statement figures for the quarter ended March 31, 2002 are compared with the period ended March 31, 2001.

Income statement figures are reported before taxation.

Accounting estimates made

When preparing the quarterly accounts, several accounting estimates – unnecessary at year end – had to be made.

Digital Bros has entered into contracts with several clients whereby it pays them a percentage bonus based on the volume of business generated. The percentages payable increase as targets are reached over the year. For the cost estimate, it was assumed, prudently, that the maximum target would be reached by all clients. At year end, no such estimate has to be made as the costs can be calculated on an actual basis.

Activities during the quarter

Distribution and co-publishing of video games in Italy

The Digital Bros Group is the leading distributor and co-publisher of video games on the Italian market. This activity is performed directly by Digital Bros S.p.A. It consists of localising video games and distributing them within Italy. Using the Halifax brand name, Digital Bros S.p.A. distributes the products of the international video games publishers which it has exclusive rights to represent in Italy.

Localisation or co-publishing involves making language and cultural changes to video games to adapt them to the Italian market as well as the translation into Italian of the original game manuals and the dubbing of any voices used in the game. For licensed products, it also includes the production of supporting materials and the design of packaging. The localisation process is carried out by Digital Bros and the video game publishers using dedicated staff.

Video game publishing

Video game publishing involves the purchase of licensed rights to video games from developers and their subsequent launch on the market using the Group's international distribution network. The length of the contracts with the developers and the geographical areas covered vary from contract to contract.

The poor performance of the international market together with the losses recorded by the UK subsidiaries which carried out this activity in 2001 led to the decision to bring the business back to Italy within the internal structure of Digital Bros S.p.A. which was already responsible for video game licenses acquired in respect of Italy only. It is expected that the sector will begin to pick up again in the second half of the year and, to a greater extent, over the winter period.

Digital Them TV

Through its subsidiaries Game Network S.p.A. and Game Network Ltd, the Digital Bros Group manages the Game Network satellite TV channel which broadcasts programmes produced in-house and dedicated to the video games world 24 hours a day. The signal is broadcast to continental Europe by the Eutelsat satellite and by the Astra Satellite in the United Kingdom. The programmes can be seen unscrambled by anyone with suitable reception equipment and a satellite dish pointed towards the correct satellite. Last year, in order to have an organisation dedicated to the sale of advertising space on the satellite TV channel, the Group set up AD1 S.r.l. which sells advertising space on behalf of Game Network S.p.A., Game Network on line S.r.l. and some third party publications including well known Internet web sites.

On-line gaming

The on-line gaming business enables PC owning gamers to play on-line via Internet and challenge other players connected to the same server. This is a subscription service and Digital Bros has developed the in house the system which handles payments by players together with billing and the technology used to integrate the data with the gaming servers and enable on-line services to be used.

Current technology - narrow-band internet connection and games consoles with no Internet access – does not exploit the potential of on-line gaming. However, the games the Group has exclusive rights to in Europe - “Legend of Mir” and “Myth of Soma” – can be played using current technology. The Internet access possible using the new generation of games consoles (Playstation2, Nintendo Gamecube and Microsoft Xbox) and the expanding range of broad band Internet connections will offer games the chance to use the available services to a greater extent in the near future and will lead to significant growth in the sector.

During the first quarter of 2002, the Group performed its on-line gaming activities through subsidiary Game Network on Line S.r.l. “Legend of Mir” was the first game launched on the market in June 2001. It became a subscription only game in September 2001 and has continued to grow in terms of the number of registered players. The second game, “Myth of Soma”, only entered its commercial phase in April 2002 with the result that related services were offered free of charge during the first quarter in order to publicise the game and build up the user base.

During the second half of 2002, in order to expand further the user base and increase revenues significantly, the Group plans to launch the game on a Europe wide level involving the use of traditional distribution channels (Large scale retail, specialist and small retail) by offering it on CD-ROM together with a prepaid subscription.

Analysis of the results for the quarter and of the outlook for the business

In the first quarter of 2002, the Group recorded revenues from sales and services totalling Euro '000 11,667, an 39% increase over the Euro '000 8,411 recorded in the first quarter of 2001.

Revenues may be analysed by business activity as follows:

Euro '000s	**March 31 2001**	**March 31 2002**	**Change**
Distribution and localisation Italy	6,593	11,251	71%
On-line gaming	20	135	n.s.
Digital TV and advertising revenues	1,071	281	-73%
International Publishing	727	0	n.s.
TOTAL REVENUES	**8,411**	**11,667**	**39%**

The increase in revenues from the distribution and localisation of video games in Italy is in line with the strength shown by the market even before the launch of two new generation consoles - the Microsoft Xbox (March 2002) and the Nintendo Gamecube (Mayo 2002). This is thanks to the expansion of the base of Sony Playstation 2 users. The following analysis provides further evidence of the situation:

Euro '000s	**March 31, 2001**		**March 31, 2002**		**Change**	
	Units	Revenues	Units	Revenues	Units	Revenues
Sega Dreamcast	4,154	109	524	3	-87%	-97%
Nintendo Gameboy	25,377	401	15,347	280	-39%	-30%
Nintendo Gameboy Advance	0	0	10,496	377		
Sony Playstation	179,404	3,456	72,644	1,107	-59%	-68%
Sony Playstation 2	50,747	1,623	202,184	8,429	+298%	+419%
Microsoft XBox	0	0	2,615	121		
Sub-Total Distribution Consoles	**259,682**	**5,589**	**303,810**	**10,317**	**17%**	**85%**
PC CD-ROM	57,025	970	71,205	883	+25%	-9%
Hardware and Accessories	3,330	34	1,188	51	-64%	+50%
Total Revenues – Distribution Italy	**320,037**	**6,593**	**376,203**	**11,251**	**+18%**	**+71%**

As the figures show, the market growth due to the combined effect of increases in sales volumes (+18% but +17% in the consoles segment) and in average prices (+45% but +58% in the consoles segment). Average selling prices rose from Euro 20.6 Euro in the first quarter of 2001 to Euro 29.9 in the first quarter of 2002. Higher prices per game sold are typical of the period following the launch of any new hardware platform. Software products are launched at high prices which gradually fall over the life cycle of the hardware.

Looking ahead to the second quarter of the year and to the subsequent autumn period – traditionally the time of peak sales levels – further growth is expected thanks to the hardware manufacturers' commercial decision to reposition their consoles in terms of pricing and to the launch of the last of the new generation consoles, the Nintendo Gamecube, on May 3, 2002. The repositioning of the price of the Microsoft Xbox and Nintendo Gamecube consoles practically upon their launch should lead to the expansion of the user base with a knock on effect on software sales. The lower console prices should also mean that more cash will be available for the purchase of software.

In February 2002, the Group signed a non-exclusive distribution agreement with Nintendo for the Italian market. The contract regards the distribution of Nintendo software products and hardware including Gameboy, Gameboy Advance and, from May 5, 2002, Nintendo Gamecube. This will enable the group to record an increase in sales revenues of at least Euro 2 million in May which is historically a month of low activity.

As described previously, revenues from on-line gaming activities consist entirely of revenues from subscriptions by gamers to the fits on-line game launched by the Digital Bros in Europe, "Legend of Mir". The revenue base is expected to increase considerably in the second half of the year as a result of the introduction of a subscription requirement for the second game "Myth of Soma". A further boost to revenues will result from the physical distribution of these products, especially Myth of Soma, in CD-ROM format together with a prepaid subscription. The Group believes that this will make the game more visible without undertaking any costly marketing campaigns and, in particular, that it will be able to penetrate potentially the most receptive markets where there has not been great success to date in terms of number of paying players (e.g. the German market).

The analysis of revenues from TV activities set out below explains better the decrease of Euro 709,000 in the first quarter of 2002 compared to the same period in 2001:

Euro '000s	**March 31 2002**	**March 31 2001**
Advertising revenues from exchange of goods	0	1,032
Advertising revenues	87	38
Revenues from prize competitions	195	0
Total Digital TV and advertising revenues	**282**	**1,071**

Until such time as the advertising market recovers or the Digital TV channel establishes itself as a reference media, the Group has begun to look for alternative sources of revenue such as the prize competitions run during the quarter in the UK market only under and agreement with a UK telephone company. In the second quarter of the year, prize competitions will be extended to other countries – France, Germany and Italy – together with another alternative source of revenue called "SMS premium". This new source of revenue will make an important contribution as the related contract will provide a guaranteed minimum of Euro 45,000 per month once it is fully operational. It involves a level of interaction as the service enables viewers to play by means of SMS messages seen on television.

Profitability varies directly in relation to revenues. The positive revenue trend, together with cost containment measures introduced with effect from the final quarter of 2001, has enabled the profit indicators set out below to improve significantly:

Euro ‘000s	**Group**			**Digital Bros S.p.A.**		
	March 31 2001	**March 31 2002**	**Delta**	**March 31 2001**	**March 31 2002**	**Delta**
EBITDA	(1,710)	333	2,043	(851)	909	1,760
EBIT	(2,369)	(86)	2,455	(1,190)	536	1,726
EBT	(2,335)	(597)	2,932	(1,056)	26	1,082

The improved profitability means that EBITDA is positive and EBIT is close to zero at consolidated level in the first quarter of the year. In the past, the first two quarters of the year have always resulted in a loss as a result of the seasonal pattern of sales which are largely concentrated towards the Christmas period.

Even more noteworthy is the performance of the parent company, Digital Bros S.p.A. Notwithstanding the seasonal factors mentioned above, it as ended the first quarter of the year close to break-even at profit before taxation level.

This positive result is due to several factors:

- the higher margin on each video game sold partly thanks to the success of “Metal Gear Solid 2” a game distributed as from March 2002;
- the containment of Digital Bros S.p.A.’s fixed costs, especially cost of services (down by Euro 130,000 compared to prior year from Euro ‘000 1,547 in the first quarter of 2001 to Euro ‘000 1,417 in the first quarter of this year) which fell from 23% of sales revenues in the first quarter of 2001 to just 13% in the first quarter of 2002;
- personnel cost savings – these were reduced by Euro 522,000 from Euro 1,544,000 in the first quarter of 2001 to Euro 1,022,000 in the first quarter of 2002 in line with the lower number of employees at Group level following the termination of the UK businesses. In percentage terms, these costs have fallen from 18% of consolidated sales revenues in the first quarter of 2001 to 9% in 2002;

these savings were countered in part by:

- an Euro 200,000 increase in fixed costs regarding the broadcasting of the Game Network satellite TV channel in the UK;
- a total deterioration of Euro 438,000 in net financial income and charges due to increased financial exposure and a Euro 108,000 deterioration in financial income and charges.

Investments made during the quarter

The level of investments made during the first quarter following the refocusing and reorganisation of the publishing activities was fairly limited and much lower than in the prior year. At Group level, total investments made during the first quarter of 2002 amounted to Euro 289,000 compared to Euro 3,208,000 in the first quarter of 2001. Investments in intangible assets may be analysed as follows:

Euro '000s	**March 31 2002**
Software licences – Italy	137
Investments in progress	54
Other intangible assets	12
Total investments in intangible assets	**203**

Investments in progress relate to costs incurred to date on the development of a new management information system based on ERP technology. It is expected to come into use as from July 1, 2002.

The costs incurred in relation to the launch of the Group's second on-line game during the "beta testing" phase i.e. the initial three month period when games can use the services free of charge were expensed in full during the period.

During the period, investments in tangible fixed assets amounted to Euro 86,000 and entirely related to industrial and commercial equipment (servers for on-line gaming activities and personal computers).

There were no investments in financial fixed assets.

Net financial position

The Group's net financial position has changed little from net indebtedness of Euro '000 10,928 at March 31, 2001 to net indebtedness of Euro '000 11,091 at March 31, 2002. A Euro '000 1,103 decrease in short-term financial assets has been offset by a Euro'000 940 decrease in amounts due to banks.

The working capital cycle i.e. average debtor days less average creditor days plus average days inventory on hand amounts to around 90 days. The concentration of revenues during the intense period of commercial activity between October and April leads to an increased financial exposure which tends to decrease during the middle part of the year.

The leverage ratio i.e. net financial position divided by shareholders' equity is fairly low at 0.5.

Significant events subsequent to the end of the quarter

On April 19, 2002, an extraordinary general meeting of Digital Bros approved the issue of 4,000 three year bonds with a nominal value of Euro 1,000, each of them convertible into ordinary shares in Digital Bros S.p.A. The issue of the bond loan – option rights excluded – will be subscribed in full by Societè Generale. The conversion ration will be reviewed every three months in relation to the market share price in order to enable Digital Bros to benefit from share price increases.

On April 19, 2002, an extraordinary general meeting of Digital Bros also approved a share capital increase through the use of reserves of Euro 3,843,000 whereby the nominal value of shares was increased from Euro 0.13 to Euro 0.40 per share.

The same general meeting also resolved to change the accounting year end to June 30. This means that the accounting period in progress will last just six months.

Digital Bros Group
Consolidated Balance Sheet at March 31, 2002
(Amounts in Euro '000s)

December 31, 2001		March 31, 2001	March 31, 2002
	Assets		
10,582	Non-current assets	10,675	10,452
42,392	Current assets	67,938	44,534
6,446	*including cash at bank and on hand and short-term financial assets*	19,333	5,483
347	Prepaid expenses and accrued income	1,298	427
53,321	*Total assets*	**79,911**	**55,413**
	Liabilities and shareholders' equity		
40,364	Share capital and reserves	40,385	22,577
(17,767)	Loss for the period	(2,087)	(597)
22,597	**Total shareholders' equity**	**38,297**	**21,980**
0	Provisions for risks	178	0
334	Employee severance indemnity reserve	258	369
30,133	Payables	40,710	32,688
30,041	*due after less than a year*	40,602	32,596
92	*due after more than a year*	107	92
257	Accrued expenses and deferred income	468	376
30,724	**Total liabilities**	**41,614**	**33,433**
53,321	**Total liabilities and shareholders' equity**	**79,911**	**55,413**
2,559	Cash at bank and on hand	19,333	2,113
3,887	Short-term financial assets	0	3,230
17,282	Short term financial liabilities	24,541	16,342
92	Financial liabilities due after more than a year	107	92
(10,928)	**Net financial position**	**(5,315)**	**(11,091)**

Digital Bros Group

Consolidated Income Statement at March 31, 2002
(amounts in Euro '000s)

December 31, 2001		**March 31, 2001**	**March 31, 2002**
42,037	Sales revenues	8,411	11,667
3,306	Change in inventory	3,576	1,500
927	Other revenues	274	8
46,270	**Value of production**	**12,262**	**13,175**
47,170	Production costs	13,972	12,842
(900)	**Gross operating margin**	**(1,710)**	**333**
4,694	Amortisation and depreciation	583	419
0	Provisions	76	0
(5,594)	**Operating loss**	**(2,369)**	**(86)**
(1,504)	Net financial income (charges)	38	(400)
(10,626)	Extraordinary income (charges)	(3)	(111)
(17,724)	**Loss before taxation a minority interests**	**(2,335)**	**(597)**
(43)	Taxes	0	0
0	Minority interests	248	0
(17,767)	**Loss before taxation**	**(2,087)**	**(597)**

Digital Bros S.p.A.
Balance Sheet at March 31, 2002
(amounts in Euro '000s)

December 31, 2001		**March 31, 2001**	**March 31, 2002**
	Assets		
7,895	Non-current assets	7,619	8,749
45,077	Current assets	69,468	47,478
5,980	*including cash at bank and on hand and short-term financial assets*	18,539	11,470
222	Prepaid expenses and accrued income	524	248
53,194	**Total assets**	**77,612**	**56,475**
	Liabilities and shareholders' equity		
40,515	Share capital and reserves	40,516	26,936
(13,631)	Profit (Loss) for the period	(1,056)	27
26,884	**Total shareholders' equity**	**39,460**	**26,963**
0	Provisions for risks	0	0
268	Employee severance indemnity reserve	216	313
25,784	Payables	37,467	28,888
25,692	*due after less than a year*	37,360	28,796
92	*due after more than a year*	107	92
257	Accrued expenses and deferred income	468	311
26,310	**Total liabilities**	**38,152**	**29,512**
53,194	**Total liabilities and shareholders' equity**	**77,612**	**56,475**
13,337	Cash at bank and on hand Short-term financial assets	18,539	11,470
17,046	Short term financial liabilities	24,021	16,341
92	Financial liabilities due after more than a year	107	92
(3,801)	**Net financial position**	**(5,590)**	**(4,963)**

Digital Bros S.p.A.
Income Statement at March 31, 2002
(amounts in Euro '000s)

December 31, 2001		March 31, 2001	March 31, 2002
33,903	Sales revenues	6,692	11,256
4,094	Change in inventory	3,628	1,481
1,345	Other revenues	148	177
39,342	**Value of production**	**10,467**	**12,914**
35,493	Production costs	11,319	12,005
3,849	**Gross operating margin**	**(852)**	**909**
1,608	Amortisation and depreciation	338	373
0	Provisions	0	0
2,241	**Operating profit (loss)**	**(1,190)**	**536**
(1,398)	Net financial income (charges)	143	(397)
(14,434)	Extraordinary income (charges)	(8)	(113)
(13,591)	**Profit (Loss) before taxation**	**(1,056)**	**26**