ACTIVISION®

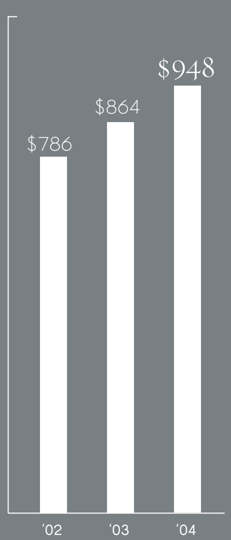
25th Anniversary

2004 Annual Report

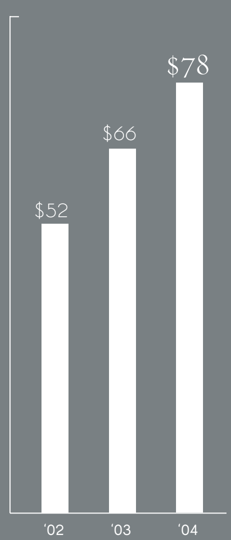
Financial Highlights

In thousands of dollars, except per share data	2004	2003	2002
Net revenues	$947,656	$864,116	$786,434
Operating income	109,817	94,847	80,574
Net earnings	77,715	66,180	52,238
Diluted earnings per share	0.54	0.43	0.39

Net Revenues
in millions of dollars



Net Earnings
in millions of dollars



Diluted Earnings
per common share

Robert A. Kotick Brian G. Kelly Ronald Doornink

To our shareholders:

Two thousand and four marks a milestone in Activision's history—25 years of delivering quality interactive entertainment experiences to consumers worldwide. Few companies have created a business model that laid the foundation for a multi-billion dollar industry. Activision can rightfully make this claim and we are proud to be at the helm of such a tradition-rich enterprise.

Throughout Activision's evolution, our goal has been to create a company that is well integrated and capable of delivering long-term value to our shareholders. We have worked diligently to build a company that has the flexibility to seize opportunities, yet maintains the foresight to anticipate challenges and plan for its future. In fiscal 2004, our vision translated into the most successful year in our history.

We delivered our 12th consecutive year of revenue growth, posted record earnings and increased our operating margin. Our results represent a five-year compound annual revenue growth rate of 17% and compound annual earnings growth rate of 39%. We further enhanced our balance sheet ending the year with $588 million in cash and short-term investments, low days sales outstanding, a solid inventory position and $833 million in shareholder equity.

We successfully created two wholly owned game properties—***Call of Duty***™ and ***True Crime***™***: Streets of L.A.***™—and introduced a new direction for the Tony Hawk brand, resulting in three franchises from which we can develop a variety of games for multiple platforms. According to NPD, Chart Track, GfK and Media Control, each of these games has sold more than one million units with life to date revenues from the Tony Hawk franchise exceeding $800 million worldwide.

During the fiscal year, we substantially strengthened our business and remained focused on three key initiatives—developing and expanding our intellectual property portfolio, building our development capabilities and strengthening our market presence. In addition to creating three original game properties, we expanded our relationships with DreamWorks, LucasArts Entertainment Company and Columbia Pictures/Marvel Enterprises, Inc. These activities will not only increase our range of product offerings but should also enhance the consistency and predictability of our future financial results. Under our agreement with DreamWorks, we acquired the rights to publish games based on the blockbuster film "Shrek 2" as well as DreamWorks' next three animated feature films, "Shark Tale," "Madagascar" and "Over the Hedge." We expanded our role with LucasArts Entertainment Company to publish and distribute LucasArts' video game console and PC products in more than 60 countries in Europe and Africa. Additionally, we recently expanded our agreement with Columbia Pictures/Marvel Enterprises, Inc. to publish games based on the upcoming feature film "Spider-Man 3," which is set for release in May 2007.

We added resources to our internal development studios through the acquisition of Infinity Ward which created ***Call of Duty,*** the #1 best-selling PC game in the U.S. during the holiday season. Additionally, we expanded our relationships with retailers and increased our shelf space around the world.

Earlier this year, we announced a strategic alliance with Nielsen Entertainment to work together to create a reliable measurement of the effectiveness of in-game advertising. We believe that there will be exciting opportunities in the future to leverage the billions of hours that consumers spend playing games annually into advertising revenues. The first step in this initiative is a Nielsen research study to better understand the demographic makeup of U.S. households with a video game console and/or PC gaming system; an analysis of the relationship between video gaming and television viewing; and an investigation into how the video game playing community perceives in-game advertising.

Nielsen will be developing a standardized methodology to measure advertising metrics in video games, in the same manner that they have created standardized measurement metrics for other forms of media including television and in-theater advertising. Nielsen will be able to provide advertisers with the tools to gauge effectively everything from in-game ad exposure, reach and frequency, to audience recall. They will develop these metrics in a language that makes it possible for media buyers to evaluate in-game advertising the same way they evaluate other media opportunities.

We also announced our support for two new hand-held platforms—the Nintendo DS and Sony's PlayStation® Portable (PSP™). We expect to have games available at the launch of these systems. Hand-held gaming has been a popular form of entertainment since the introduction of the Game Boy® in 1989 and we expect that these new devices will continue to broaden its appeal.

While our primary focus is increasing the sales of our titles, there are new and exciting opportunities for growth in the future. We are especially enthusiastic about three developments—online interaction, broadband penetration and increased production values.

Online interaction will create more personal interest and engagement. Today, the majority of console game playing takes place alone. The second most popular way to play is in the same room with a sibling or friend. Playing with others over the Internet through Xbox™ ***Live*** or the PlayStation®2 is a relatively new concept, but it is a big part of the future.

The maturity of broadband will make this interaction possible. The telecom industry continues to provide substantial incentives for investment in broadband meaning critical infrastructure growth is on the way. We believe the tipping point for industry-changing player interaction could occur when broadband reaches 50 to 60 percent of households. Penetration today is about 45 percent, so we are getting closer.

And as the presence of broadband increases, especially wireless broadband, we will deliver games to more platforms and more devices including cell phones, tablet computers and even PDAs.

Production values, the way games look and sound, continue to increase as console technology advances and we expect that the production values of the next generation of console systems will approximate those of movies and TV. In 1981, "ER" and "Jurassic Park" creator Michael Crichton made a movie called "Looker," about a scheme to replace actors with computer-generated images indistinguishable from real people. It seemed fantasy then, but today's computer-made imagery does look real enough to fool the casual observer.

The technology that makes possible these visual advances (and audio advances, too, which already approximate reality) also allows us to move beyond linear storytelling to player-controlled development of characters and plots. Players will transcend the standard video game quest experience to affect the plot of the story, character behavior, settings and background, and even the nature and degree of interaction itself.

We think of it as a shift from re-creating a part in an action movie, to actually taking on the role in a virtual arena, defining and experiencing it through players' own choices.

For the past 25 years, Activision has been at the forefront of the video game industry. Today, our business, the business of creating quality interactive entertainment experiences and distributing them worldwide, spans the most dynamic part of the digital economy with high prospects of continued expansion.

Activision's strength and purpose reside in the shared values that bring so many extraordinarily talented employees here and cause them to invest their abilities, artistry and time in our company. We believe that by seeking a broad diversity of talent and ambition, we make ourselves stronger. We carry out this belief inside the company through the way that we hire, promote and compensate our employees and outside the company in our commitment to community building initiatives. This year, our support for community involvement has never been stronger. We forged an alliance with the Tomorrow's Leaders program which provides more than 4,000 youths with a strong foundation for academic, social and technological success. Many of our employees are involved with the program's volunteer activities that aim to help participants learn about positive peer interaction, complete their homework and teach them computer skills.

As we look ahead, we are determined that Activision will remain focused on innovation, imagination and finding new ways to better serve our customers and reward our employees and shareholders. We will always seek to stand for quality entertainment, and we are more confident than ever that we will meet this responsibility and be tomorrow what we have been for the past 25 years, one of the world's leading interactive entertainment companies.

Sincerely,

Robert A. Kotick Chairman and CEO	Brian G. Kelly Co-Chairman	Ronald Doornink President

Activision, Inc. — 2004 Annual Report

Capitalizing on 25 Years of Achievement

Twenty-five

years of delivering quality & choice

Can fun be serious business? At Activision we think so. Every day, millions of people around the world are entertained by our games. Over the past quarter century, we have built one of the largest portfolios of recognized brands and in fiscal 2005 expect to release our strongest game slate ever. The company's lineup is comprised of high-profile entertainment properties and titles created by some of the industry's premier development talent.

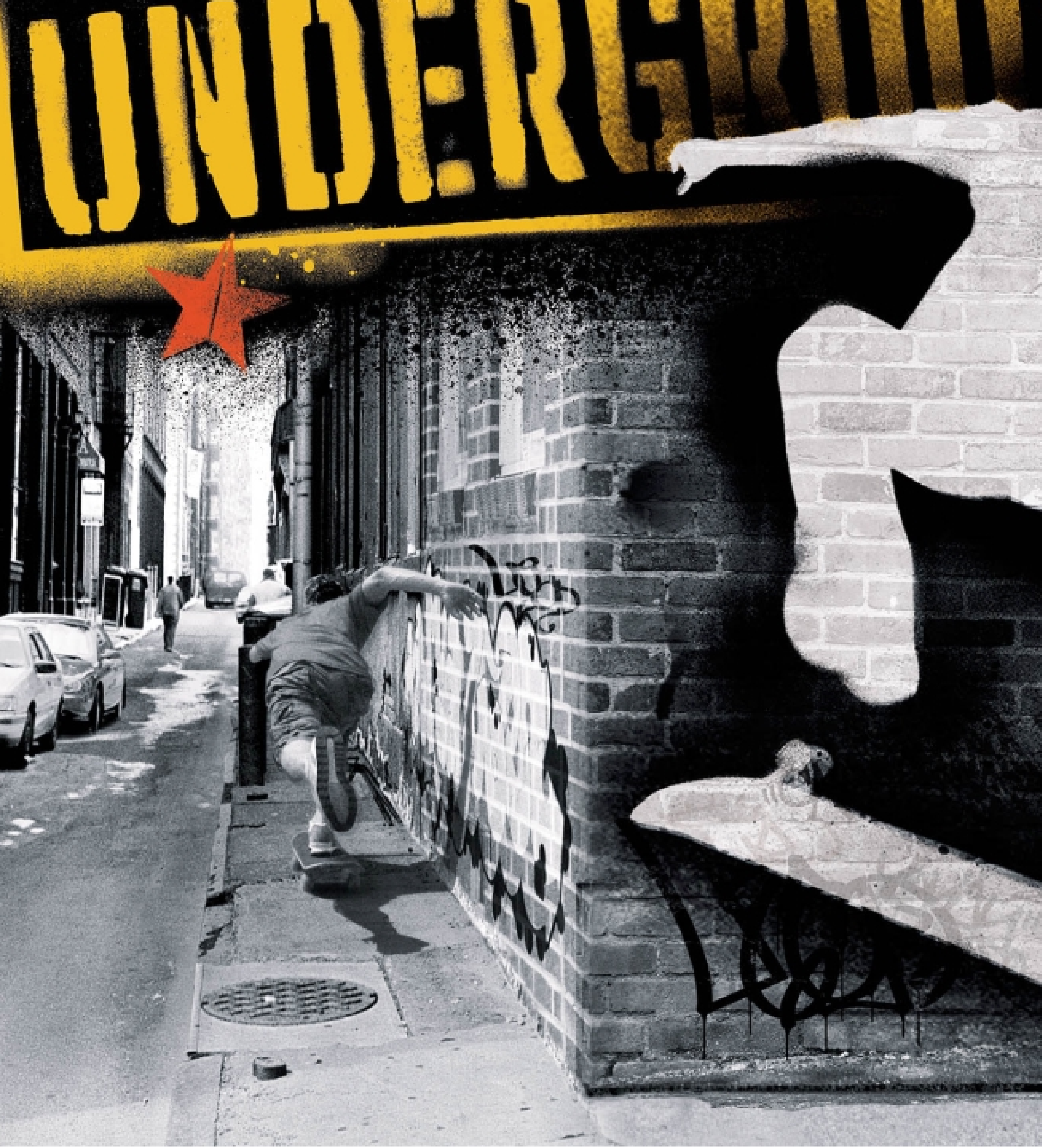
Our release schedule includes games based on such highly anticipated movies as "Shrek 2™"; "Spider-Man 2™"; "DreamWorks' Shark Tale™"; and "Lemony Snicket's A Series of Unfortunate Events™"; as well as id Software's™ gripping 3D action game ***DOOM 3***™; ***Tony Hawk's Underground 2***™, the sequel to the best-selling action sports game; ***X-Men Legends***™, the first 3D action role-playing game based on the renowned Marvel X-Men characters; The Creative Assembly's award-winning real-time strategy game *Rome: Total War*™; the newest installment in the award-winning ***Call of Duty***™ series, ***Call of Duty: Finest Hour***; and ***Vampire: the Masquerade Bloodlines***™, an action role-playing game based on the popular White Wolf book series.

Innovative

marketing programs that drive sales

Aggressive marketing is not a new concept at Activision. In support of our fiscal year 2004 holiday titles, we increased our trade and consumer marketing programs and raised awareness for our products through in-store merchandising, as well as in-theater, print, online and television advertising. This strategy drove sales of our key titles at launch and for several months post launch.

In fiscal year 2005, the company will continue to focus on initiatives that will broaden consumer awareness of our games. We are partnering with our retailers on new programs that mark a series of firsts for our company and the industry. This year we introduced pre-order programs at several key accounts and were successful in having our products removed from glass cases and showcased in floor displays at our top retail accounts.



Developing

the games that audiences crave

In video games, great gameplay rules. The foundation for Activision's success has been our ability to develop franchises from which we can produce high-quality entertainment products year after year. Innovation, technical achievements and compelling gameplay experiences have made us a leading developer for the PC and console platforms. At the core of our success is our proprietary "Greenlight Process," a disciplined methodology for the selection, development, production and quality assurance of our titles.

With our recent acquisition of Infinity Ward, we now have eight wholly owned studios and employ more than 700 of the best artists, programmers, designers and storytellers in the industry. In addition to our own studio operations, we have forged long-term partnerships with some of the premier independent developers including id Software, Peter Molyneaux's Lionhead Studios and The Creative Assembly. Each of these extraordinarily talented development teams continues to revolutionize the game development process through their technical mastery and originality.

Financial Review

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Selected Consolidated Financial Data

The following table summarizes certain selected consolidated financial data, which should be read in conjunction with our Consolidated Financial Statements and Notes thereto and with Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere herein. The selected consolidated financial data presented below as of and for each of the fiscal years in the five-year period ended March 31, 2004 are derived from our audited consolidated financial statements. The Consolidated Balance Sheets as of March 31, 2004 and 2003 and the Consolidated Statements of Operations and Consolidated Statements of Cash Flows for each of the fiscal years in the three-year period ended March 31, 2004, and the reports thereon, are included elsewhere in this Annual Report.

(In thousands, except per share data)		Restated[1]			
Year ended March 31,	**2004[2]**	**2003[2]**	**2002[2]**	**2001**	**2000**
Statement of Operations Data:					
Net revenues	$947,656	$ 864,116	$786,434	$620,183	$572,205
Cost of sales—product costs	475,541	440,977	435,725	324,907	319,422
Cost of sales—intellectual property licenses and software royalties and amortization	91,606	124,196	99,006	89,702	91,238
Income (loss) from operations	109,817	94,847	80,574	39,807	(30,325)
Income (loss) before income tax provision (benefit)	115,992	103,407	83,120	32,544	(38,736)
Net income (loss)	77,715	66,180	52,238	20,507	(34,088)
Basic earnings (loss) per share	0.58	0.46	0.46	0.24	(0.41)
Diluted earnings (loss) per share	0.54	0.43	0.39	0.22	(0.41)
Basic weighted average common shares outstanding	133,249	144,359	113,966	83,921	83,334
Diluted weighted average common shares outstanding	144,893	155,483	133,775	92,475	83,334
Cash Provided by (Used in):					
Operating activities	67,403	90,975	111,792	81,565	2,883
Investing activities	(15,169)	(155,101)	(8,701)	(8,631)	(25,041)
Financing activities	117,569	64,090	50,402	2,547	42,028

As of March 31,	**2004[2]**	**2003[2]**	**2002[2]**	**2001**	**2000**
Balance Sheet Data:					
Working capital	$675,796	$ 422,500	$333,199	$182,980	$158,225
Cash, cash equivalents and short-term investments	587,649	406,954	279,007	125,550	49,985
Capitalized software development and intellectual property licenses	135,201	107,921	56,742	42,205	40,808
Goodwill	76,493	68,019	35,992	10,316	12,347
Total assets	968,817	704,816	556,887	359,957	309,737
Long-term debt	—	2,671	3,122	63,401	73,778
Shareholders' equity	832,738	597,740	430,091	181,306	132,009

(1) Consolidated financial information for fiscal years 2003–2000 has been restated for the effect of our three-for-two stock split effected in the form of a 50% stock dividend to shareholders of record as of February 23, 2004, paid March 15, 2004.

(2) Effective April 1, 2001, we adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangibles." SFAS No. 142 addresses financial accounting and reporting requirements for acquired goodwill and other intangible assets. Under SFAS No. 142, goodwill is deemed to have an indefinite useful life and should not be amortized but rather tested at least annually for impairment. In accordance with SFAS No. 142, we have not amortized goodwill during the years ended March 31, 2004, 2003 and 2002.

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

Overview

Our Business

We are a leading international publisher of interactive entertainment software products. We have built a company with a diverse portfolio of products that spans a wide range of categories and target markets and that is used on a variety of game hardware platforms and operating systems. We have created, licensed and acquired a group of highly recognizable brands, which we market to a variety of consumer demographics.

Our products cover game categories such as action/adventure, action sports, racing, role-playing, simulation, first-person action and strategy. Our target customer base ranges from game enthusiasts and children to mass-market consumers and "value" buyers. We currently offer our products primarily in versions that operate on the Sony PlayStation 2 ("PS2"), Nintendo GameCube ("GameCube") and Microsoft Xbox ("Xbox") console systems, Nintendo Game Boy Advance ("GBA") hand-held device and the personal computer ("PC"). The installed base for this current generation of hardware platforms is significant and growing. We believe recent price cuts in calendar 2004 on the Xbox and PS2 hardware should continue to drive the growth of the installed base of these two platforms. We also expect the installed base of the other current-generation platforms to continue to grow. In addition, Sony announced that it would be entering the hand-held hardware market with the introduction of its hand-held gaming device, PlayStation Portable ("PSP"). PSP is currently expected to be released in the United States toward the end of the first quarter of calendar 2005. Nintendo has also announced that it plans to launch a new dual-screened, portable game system, Nintendo Dual Screen ("NDS"), before the end of calendar 2004. We are currently developing titles for the PSP and the NDS with the objective of having one or more titles at launch for each of these platforms. We are also planning to develop titles for the next-generation console systems expected to be developed by Sony, Microsoft and Nintendo for release in the next two to three years. Though there are still many unknowns relating to these new platforms, our aim is to have a significant presence at the launch of each new platform while being careful not to move away too quickly from the current generation platforms given their large and growing installed base.

Our publishing business involves the development, marketing and sale of products directly, by license or through our affiliate label program with certain third-party publishers. In the United States, we primarily sell our products on a direct basis to mass-market retailers, consumer electronics stores, discount warehouses and game specialty stores. We conduct our international publishing activities through offices in the United Kingdom ("UK"), Germany, France, Italy, Australia, Sweden, Canada and Japan. Our products are sold internationally on a direct-to-retail basis, through third-party distribution and licensing arrangements and through our wholly-owned European distribution subsidiaries. Our distribution business consists of operations located in the UK, the Netherlands and Germany that provide logistical and sales services to third-party publishers of interactive entertainment software, our own publishing operations and manufacturers of interactive entertainment hardware.

Our profitability is directly affected by the mix of revenues from our publishing and distribution businesses. Operating margins realized from our publishing business are substantially higher than margins realized from our distribution business. Operating margins in our publishing business are affected by our ability to release highly successful or "hit" titles. Though many of these titles have substantial production or acquisition costs and marketing budgets, once a title recoups these costs, incremental net revenues directly and positively impact our operating margin. Operating margins in our distribution business are affected by the mix of hardware and software sales, with software producing higher margins than hardware.

Our Focus

With respect to future game development, we will continue to focus on our "big propositions," products that are backed by strong brands and high quality development, for which we will provide significant marketing support.

A number of our fiscal 2005 "big propositions" will include well-established brands, which are backed by high profile intellectual property and/or highly anticipated motion picture releases. Examples of these brands are our superheroes and skateboarding brands. We have a long-term relationship with Marvel Enterprises through an exclusive licensing agreement that expires in 2009. This agreement grants us the exclusive rights to develop and publish video games based on Marvel's comic book franchises Spider-Man, X-MEN, Fantastic Four and Iron Man. Through our long-term relationship with Spider-Man Merchandising, LLP, we have completed the development of the video game *Spider-Man 2: The Movie*, the sequel to the highly successful *Spider-Man: The Movie*, a key fiscal 2003 title release that has continued to perform strongly into fiscal 2004. The video game release of *Spider-Man 2: The Movie* is scheduled to coincide with the "Spider-Man 2" theatrical release in June 2004. We also recently announced that through our licensing agreement with Spider-Man Merchandising, LLP, we will be developing and publishing video games based on Columbia Pictures/Marvel Enterprises, Inc.'s upcoming feature film "Spider-Man 3," which is expected to be released in May 2007. In addition, we have an exclusive licensing agreement with professional skateboarder Tony Hawk that continues until 2015. The agreement grants us exclusive rights to develop and publish video games using Tony Hawk's name and his likeness. Through fiscal 2004, we have released five successful titles in the Tony Hawk franchise with cumulative net revenues of over $800.0 million, including the most recent, *Tony Hawk's Underground*, which was released in the third quarter of fiscal 2004. We will continue to promote our skateboarding franchise with the release in fiscal 2005 of the sequel to the very successful *Tony Hawk's Underground*.

We will also continue to develop new intellectual properties such as *True Crime: Streets of L.A.* and *Call of Duty*, which were originally released in the third quarter of fiscal 2004. These highly successful titles were both ranked by third-party sales tracking agencies as among the top-five selling games for the holiday season. We expect to develop a variety of games on multiple platforms based on these two new original properties and hope to establish them as a source of recurring revenues. For example, in fiscal 2005, we are scheduled to release *Call of Duty: Finest Hour* which will be released on multiple console platforms.

We will also continue to evaluate emerging brands that we believe have potential to become successful game franchises. For example, we have a multi-year, multi-property publishing agreement with DreamWorks SKG that grants us the exclusive rights to publish video games based on DreamWorks SKG's theatrical release "Shrek 2," as well as upcoming computer-animated films, "Shark Tale," "Madagascar" and "Over the Hedge," and their sequels. We also have an exclusive licensing agreement to develop and publish video games for the best-selling children's book series, Lemony Snicket's A Series of Unfortunate Events, which is being developed for a feature film by Paramount Pictures, Nickelodeon Movies and DreamWorks SKG.

In addition to acquiring or creating high profile intellectual property, we have also continued our focus on establishing and maintaining relationships with talented and experienced software development teams. We have strengthened our internal development capabilities through the acquisition in prior fiscal years of a number of talented and experienced development companies. Most recently, in October 2003, we exercised our option to acquire the remaining 70% of the outstanding capital of Infinity Ward, the developer of our PC title, *Call of Duty*. We had acquired the initial 30% of Infinity Ward's outstanding capital stock in May 2002. We also have development agreements with other top-level, third-party developers such as id Software, Valve Corporation, Spark Unlimited, Lionhead Studios and The Creative Assembly.

We are utilizing these developer relationships, new intellectual property acquisitions, new original intellectual property creations and our existing library of intellectual property to further focus our game development on product lines that will deliver significant, lasting and recurring revenues and operating profits.

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

Critical Accounting Policies

We have identified the policies below as critical to our business operations and the understanding of our financial results. The impact and any associated risks related to these policies on our business operations is discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations where such policies affect our reported and expected financial results. For a detailed discussion on the application of these and other accounting policies, see Note 1 to the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition. We recognize revenue from the sale of our products upon the transfer of title and risk of loss to our customers. Revenue from product sales is recognized after deducting the estimated allowance for returns and price protection. With respect to license agreements that provide customers the right to make multiple copies in exchange for guaranteed amounts, revenue is recognized upon delivery of such copies. Per copy royalties on sales that exceed the guarantee are recognized as earned. In addition, in order to recognize revenue for both product sales and licensing transactions, persuasive evidence of an arrangement must exist and collection of the related receivable must be probable. Revenue recognition also determines the timing of certain expenses, including cost of sales—intellectual property licenses and cost of sales—software royalties and amortization.

Allowances for Returns, Price Protection, Doubtful Accounts and Inventory Obsolescence. In determining the appropriate unit shipments to our customers, we benchmark our titles using historical and industry data. We closely monitor and analyze the historical performance of our various titles, the performance of products released by other publishers and the anticipated timing of other releases in order to assess future demands of current and upcoming titles. Initial volumes shipped upon title launch and subsequent reorders are evaluated to ensure that quantities are sufficient to meet the demands from the retail markets but at the same time, are controlled to prevent excess inventory in the channel.

We may permit product returns from, or grant price protection to, our customers under certain conditions. In general, price protection refers to the circumstances when we elect to decrease the wholesale price of a product by a certain amount and, when granted and applicable, allows customers a credit against amounts owed by such customers to Activision with respect to open and/or future invoices. The conditions our customers must meet to be granted the right to return products or price protection are, among other things, compliance with applicable payment terms, delivery to us of weekly inventory and sell-through reports, and consistent participation in the launches of our premium title releases. We may also consider other factors, including the facilitation of slow-moving inventory and other market factors. Management must make estimates of potential future product returns and price protection related to current period product revenue. We estimate the amount of future returns and price protection for current period product revenue utilizing historical experience and information regarding inventory levels and the demand and acceptance of our products by the end consumer. The following factors are used to estimate the amount of future returns and price protection for a particular title: historical performance of titles in similar genres, historical performance of the hardware platform, historical performance of the brand, console hardware lifecycle, Activision sales force and retail customer feedback, industry pricing, weeks of on-hand retail channel inventory, absolute quantity of on-hand retail channel inventory, Activision warehouse on-hand inventory levels, the title's recent sell-through history (if available), marketing trade programs and competing titles. The relative importance of these factors varies among titles depending upon, among other items, genre, platform, seasonality and sales strategy. Significant management judgments and estimates must be made and used in connection with establishing the allowance for returns and price protection in any accounting period. Historically, total actual returns and price protection have not exceeded our allowance estimates. However, actual returns and price protection could vary materially from our allowance estimates due to a number of reasons including, among others, a lack of consumer acceptance of a title, the release in the same period of a similarly themed title by a competitor, or technological obsolescence due to the emergence of new hardware platforms. Material differences may result in the amount and timing of our revenue for any period if management makes different judgments or utilizes different estimates in determining the allowances for returns and price protection.

Similarly, management must make estimates of the uncollectibility of our accounts receivable. In estimating the allowance for doubtful accounts, we analyze the age of current outstanding account balances, historical bad debts, customer concentrations, customer creditworthiness, current economic trends and changes in our customers' payment terms and their economic condition, as well as whether we can obtain sufficient credit insurance. Any significant changes in any of these criteria would impact management's estimates in establishing our allowance for doubtful accounts.

We value inventory at the lower of cost or market. We regularly review inventory quantities on hand and in the retail channel and record a provision for excess or obsolete inventory based on the future expected demand for our products. Significant changes in demand for our products would impact management's estimates in establishing our inventory provision.

Software Development Costs. Software development costs include payments made to independent software developers under development agreements, as well as direct costs incurred for internally developed products.

We account for software development costs in accordance with Statement of Financial Accounting Standard ("SFAS") No. 86, "Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed." Software development costs are capitalized once technological feasibility of a product is established and such costs are determined to be recoverable. Technological feasibility of a product encompasses both technical design documentation and game design documentation. For products where proven technology exists, this may occur early in the development cycle. Technological feasibility is evaluated on a product-by-product basis. Prior to a product's release, we expense, as part of cost of sales—software royalties and amortization, capitalized costs when we believe such amounts are not recoverable. Capitalized costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation. Amounts related to software development which are not capitalized are charged immediately to product development expense. We evaluate the future recoverability of capitalized amounts on a quarterly basis. The recoverability of capitalized software development costs is evaluated based on the expected performance of the specific products for which the costs relate. Criteria used to evaluate expected product performance include: historical performance of comparable products using comparable technology; orders for the product prior to its release; and estimated performance of a sequel product based on the performance of the product on which the sequel is based.

Commencing upon product release, capitalized software development costs are amortized to cost of sales—software royalties and amortization based on the ratio of current revenues to total projected revenues, generally resulting in an amortization period of six months or less. For products that have been released in prior periods, we evaluate the future recoverability of capitalized amounts on a quarterly basis. The primary evaluation criterion is actual title performance.

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

Significant management judgments and estimates are utilized in the assessment of when technological feasibility is established, as well as in the ongoing assessment of the recoverability of capitalized costs. In evaluating the recoverability of capitalized costs, the assessment of expected product performance utilizes forecasted sales amounts and estimates of additional development costs to be incurred. If revised forecasted or actual product sales are less than and/or revised forecasted or actual costs are greater than the original forecasted amounts utilized in the initial recoverability analysis, the actual impairment charge may be larger than originally estimated in any given quarter.

Intellectual Property Licenses. Intellectual property license costs represent license fees paid to intellectual property rights holders for use of their trademarks, copyrights, software, technology or other intellectual property or proprietary rights in the development of our products. Depending upon the agreement with the rights holder, we may obtain the rights to use acquired intellectual property in multiple products over multiple years, or alternatively, for a single product.

We evaluate the future recoverability of capitalized intellectual property licenses on a quarterly basis. The recoverability of capitalized intellectual property license costs is evaluated based on the expected performance of the specific products in which the licensed trademark or copyright is to be used. As many of our intellectual property licenses extend for multiple products over multiple years, we also assess the recoverability of capitalized intellectual property license costs based on certain qualitative factors such as the success of other products and/or entertainment vehicles utilizing the intellectual property, whether there are any future planned theatrical releases or television series based on the intellectual property and the rights holder's continued promotion and exploitation of the intellectual property. Prior to the related product's release, we expense, as part of cost of sales—intellectual property licenses, capitalized intellectual property costs when we believe such amounts are not recoverable. Capitalized intellectual property costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation. Criteria used to evaluate expected product performance include: historical performance of comparable products using comparable technology; orders for the product prior to its release; and estimated performance of a sequel product based on the performance of the product on which the sequel is based.

Commencing upon the related product's release, capitalized intellectual property license costs are amortized to cost of sales—intellectual property licenses based on the ratio of current revenues for the specific product to total projected revenues for all products in which the licensed property will be utilized. As intellectual property license contracts may extend for multiple years, the amortization of capitalized intellectual property license costs relating to such contracts may extend beyond one year. For intellectual property included in products that have been released, we evaluate the future recoverability of capitalized amounts on a quarterly basis. The primary evaluation criterion is actual title performance.

Significant management judgments and estimates are utilized in the assessment of the recoverability of capitalized costs. In evaluating the recoverability of capitalized costs, the assessment of expected product performance utilizes forecasted sales amounts and estimates of additional development costs to be incurred. If revised forecasted or actual product sales are less than and/or revised forecasted or actual costs are greater than the original forecasted amounts utilized in the initial recoverability analysis, the actual impairment charge may be larger than originally estimated in any given quarter. Additionally, as noted above, as many of our intellectual property licenses extend for multiple products over multiple years, we also assess the recoverability of capitalized intellectual property license costs based on certain qualitative factors such as the success of other products and/or entertainment vehicles utilizing the intellectual property, whether there are any future planned theatrical releases or television series based on the intellectual property and the rights holder's continued promotion and exploitation of the intellectual property. Material differences may result in the amount and timing of charges for any period if management makes different judgments or utilizes different estimates in evaluating these qualitative factors.

Selected Consolidated Statements of Operations Data

The following table sets forth certain consolidated statements of operations data for the periods indicated as a percentage of consolidated net revenues and also breaks down net revenues by territory and platform, as well as operating income by business segment:

(In thousands)

Year ended March 31,	2004		2003		2002	
Net revenues	$947,656	100%	$864,116	100%	$786,434	100%
Costs and expenses:						
Cost of sales—product costs	475,541	50	440,977	51	435,725	56
Cost of sales—software royalties and amortization	59,744	6	79,194	9	58,892	7
Cost of sales—intellectual property licenses	31,862	3	45,002	5	40,114	5
Product development	97,859	10	56,971	7	40,960	5
Sales and marketing	128,221	14	100,646	12	86,161	11
General and administrative	44,612	5	46,479	5	44,008	6
Total costs and expenses	837,839	88	769,269	89	705,860	90
Income from operations	109,817	12	94,847	11	80,574	10
Investment income, net	6,175	—	8,560	1	2,546	1
Income before income tax provision	115,992	12	103,407	12	83,120	11
Income tax provision	38,277	4	37,227	4	30,882	4
Net income	$ 77,715	8%	$ 66,180	8%	$ 52,238	7%
Net Revenues by Territory:						
United States	$446,812	47%	$432,261	50%	$404,905	51%
Europe	479,224	51	413,125	48	368,799	47
Other	21,620	2	18,730	2	12,730	2
Total net revenues	$947,656	100%	$864,116	100%	$786,434	100%
Net Revenues by Segment/Platform Mix:						
Publishing:						
Console	$508,418	76%	$466,116	76%	$312,986	57%
Hand-held	24,945	4	49,966	8	119,177	22
PC	132,369	20	99,893	16	117,345	21
Total publishing net revenues	665,732	70	615,975	71	549,508	70
Distribution:						
Console	223,802	79	208,505	84	167,709	71
Hand-held	18,361	7	14,103	6	39,865	17
PC	39,761	14	25,533	10	29,352	12
Total distribution net revenues	281,924	30	248,141	29	236,926	30
Total net revenues	$947,656	100%	$864,116	100%	$786,434	100%
Operating Income by Segment:						
Publishing	$ 93,223	10%	$ 79,139	9%	$ 68,675	9%
Distribution	16,594	2	15,708	2	11,899	1
Total operating income	$109,817	12%	$ 94,847	11%	$ 80,574	10%

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

Results of Operations—Fiscal Years Ended March 31, 2004 and 2003

Net income for the year ended March 31, 2004 was $77.7 million or $0.54 per diluted share, as compared to $66.2 million or $0.43 per diluted share for the year ended March 31, 2003.

Net Revenues

We primarily derive revenue from sales of packaged interactive software games designed for play on video game consoles (such as the PS2, Xbox and GameCube), PCs and hand-held game devices (such as the GBA). We also derive revenue from our distribution business in Europe that provides logistical and sales services to third-party publishers of interactive entertainment software, our own publishing operations and third-party manufacturers of interactive entertainment hardware.

The following table details our consolidated net revenues by business segment and our publishing net revenues by territory for the years ended March 31, 2004 and 2003 (in thousands):

Year ended March 31,	2004	2003	Increase/ (Decrease)	Percent Change
Publishing Net Revenues				
North America	$446,812	$432,261	$14,551	3%
Europe	197,300	164,984	32,316	20%
Other	21,620	18,730	2,890	15%
Total International	218,920	183,714	35,206	19%
Total Publishing Net Revenues	665,732	615,975	49,757	8%
Distribution Net Revenues	281,924	248,141	33,783	14%
Consolidated Net Revenues	$947,656	$864,116	$83,540	10%

Consolidated net revenues increased 10% from $864.1 million for the year ended March 31, 2003 to $947.7 million for the year ended March 31, 2004. This increase was generated by both our publishing and distribution businesses. The increase in consolidated net revenue was driven by the following:

- Strong performance of our fiscal 2004 third quarter releases of *True Crime: Streets of L.A.* and *Tony Hawk's Underground* for the PS2, Xbox and GameCube and *Call of Duty* for the PC. We continued to see strong sales of these titles through March 2004. In addition, we had strong results from several other titles released during fiscal 2004 including *Return to Castle Wolfenstein, X2: Wolverine's Revenge, Cabela's Dangerous Hunts, Cabela's Deer Hunt 2004 Season,* and in select European markets, *Jedi Knight: Jedi Academy*. We also had strong catalog sales from a number of our franchises, including Spider-Man. Catalog sales are sales of titles released prior to the current fiscal year.
- Publishing console net revenues increased by 9% from $466.1 million for the year ended March 31, 2003 to $508.4 million for the year ended March 31, 2004. As expected, within the mix of specific consoles, net revenues from the sale of software for the prior generation console hardware systems, such as PS1, continued to decline while the net revenues from the sale of software for the current generation of console hardware systems continued to grow.

- Net revenues were positively impacted from titles selling at higher average retail prices throughout fiscal 2004 as compared to fiscal 2003. As a result of the strong performance of our key fiscal 2004 releases, we were able to maintain the original price points for those titles for an extended period of time.
- International net revenues benefited from the strong year-over-year strengthening of the Euro ("EUR") and Great British Pound ("GBP") in relation to the U.S. dollar. We estimate that foreign exchange rates increased reported net revenue by approximately $52.1 million. Excluding the impact of changing foreign currency rates, our international net revenue increased 4% year-over-year.
- The increase in publishing net revenues was offset by fewer titles released in fiscal 2004 as compared to fiscal 2003.

North America Publishing Net Revenue

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$446,812	47%	$432,261	50%	$14,551	3%

Domestic publishing net revenues increased 3% from $432.3 million for the year ended March 31, 2003 to $446.8 million for the year ended March 31, 2004. The increase reflects the strong performance of our fiscal 2004 third quarter releases of *True Crime: Streets of L.A.* and *Tony Hawk's Underground* for the PS2, Xbox and GameCube and *Call of Duty* for the PC. We continued to see strong sales of these titles through March 2004. The increase in net revenues was offset by fewer titles released in fiscal 2004 as compared to fiscal 2003.

International Publishing Net Revenue

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$218,920	23%	$183,714	21%	$35,206	19%

International publishing net revenues increased by 19% from $183.7 million for the year ended March 31, 2003 to $218.9 million for the year ended March 31, 2004. International publishing also saw strong results from our 2004 releases of *True Crime: Streets of L.A.* and *Tony Hawk's Underground* for the PS2, Xbox and GameCube and *Call of Duty* for the PC. We also had strong results from several other titles released during fiscal 2004 including *Return to Castle Wolfenstein*, *X2: Wolverine's Revenge* and *Jedi Knight: Jedi Academy*. In addition, we had strong catalog sales from a number of our franchises, including Spider-Man. There also was a positive strengthening of the EUR and the GBP in relation to the U.S. dollar of approximately $22.2 million. Excluding the impact of changing foreign currency rates, our international publishing net revenue increased 7% year-over-year. The increase in net revenues was offset by fewer titles released in fiscal 2004 as compared to fiscal 2003.

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Publishing Net Revenue by Product Line

Publishing net revenues increased 8% from $616.0 million for the year ended March 31, 2003 to $665.7 million for the year ended March 31, 2004. The following table details our publishing net revenues by platform and as a percentage of total publishing net revenues for the years ended March 31, 2004 and 2003 (in thousands):

	Year Ended March 31, 2004	% of Publishing Net Revenues	Year Ended March 31, 2003	% of Publishing Net Revenues	Increase/ (Decrease)	Percent Change
Publishing Net Revenues						
PC	$132,369	20%	$ 99,893	16%	$ 32,476	33%
Console						
PlayStation 2	289,048	43%	260,307	42%	28,741	11%
Microsoft Xbox	145,111	22%	75,329	12%	69,782	93%
Nintendo						
GameCube	52,909	8%	74,694	12%	(21,785)	(29%)
PlayStation	20,843	3%	52,722	9%	(31,879)	(60%)
Other	507	—%	3,064	1%	(2,557)	(83%)
Total Console	508,418	76%	466,116	76%	42,302	9%
Hand-held						
Game Boy Advance	24,621	4%	44,060	7%	(19,439)	(44%)
Game Boy Color	324	—%	5,906	1%	(5,582)	(95%)
Total Hand-held	24,945	4%	49,966	8%	(25,021)	(50%)
Total Publishing Net Revenues	$665,732	100%	$615,975	100%	$ 49,757	8%

Personal Computer Net Revenue

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$132,369	20%	$99,893	16%	$32,476	33%

Net revenue from sales of titles for the PC increased 33% from $99.9 million for the year ended March 31, 2003 to $132.4 million for the year ended March 31, 2004. Though the number of premium PC titles released in fiscal 2004 remained relatively consistent with fiscal 2003, certain of our fiscal 2004 releases, *Call of Duty*, *Empires: Dawn of the Modern World* and, in select European markets, *Jedi Knight: Jedi Academy*, performed very well in both the domestic and international markets. According to NPD Group, a third-party sales tracking agency, *Call of Duty* was the number one selling PC title in North America during the quarter of its release, our third quarter of fiscal 2004. We expect fiscal 2005 PC publishing net revenues to increase as a percentage of total publishing net revenues over fiscal 2004 reflecting the release of more PC titles in fiscal 2005, including the highly anticipated *Doom 3*.

PlayStation 2 Net Revenue

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$289,048	43%	$260,307	42%	$28,741	11%

Net revenue from sales of titles for the PS2 increased 11% from $260.3 million for the year ended March 31, 2003 to $289.0 million for the year ended March 31, 2004. Though the number of new PS2 titles reduced in fiscal 2004 to 10 from 13 in fiscal 2003, we were able to increase our PS2 sales in both the domestic and international markets. The increase is primarily due to strong worldwide sales of several of our PS2 titles including *True Crime: Streets of L.A., Tony Hawk's Underground, X2: Wolverine's Revenge, Return to Castle Wolfenstein, Cabela's Dangerous Hunts* and *Cabela's Deer Hunt 2004 Season*. We expect the growth of the installed base of PS2 hardware to be driven by the recent price cut announced by Sony in May 2004.

Microsoft Xbox Net Revenue

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$145,111	22%	$75,329	12%	$69,782	93%

Net revenue from sales of titles for the Xbox increased 93% from $75.3 million for the year ended March 31, 2003 to $145.1 million for the year ended March 31, 2004. Though the number of new Xbox titles remained relatively consistent from fiscal 2003 to fiscal 2004, we were able to increase our Xbox sales in both the domestic and international markets. The increase is primarily due to strong worldwide sales of several of our Xbox titles including *True Crime: Streets of L.A., Tony Hawk's Underground, Return to Castle Wolfenstein, Soldier of Fortune 2, X2: Wolverine's Revenge, Tenchu: Return from Darkness* and, in select European markets, *Jedi Knight: Jedi Academy*. The increase was also due to an increased installed base of the Xbox. We expect the growth of the installed base of Xbox hardware to be driven by the recent price cut announced by Microsoft in March 2004.

Nintendo GameCube Net Revenue

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$52,909	8%	$74,694	12%	$(21,785)	(29%)

Net revenue from sales of titles for the Nintendo GameCube decreased 29% from $74.7 million for the year ended March 31, 2003 to $52.9 million for the year ended March 31, 2004. The decrease is primarily due to a reduction in the number of GameCube new title releases from 9 in fiscal 2003 to 5 in fiscal 2004. The titles that were released for GameCube performed strongly, including *Tony Hawk's Underground* and *True Crime: Streets of L.A.* We expect the installed base of GameCube hardware to continue to grow at its current low price point.

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PlayStation Net Revenue

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$20,843	3%	$52,722	9%	$(31,879)	(60%)

Net revenue from sales of titles for the Sony PlayStation console system ("PS1") for the year ended March 31, 2004 decreased 60% from the prior fiscal year, from $52.7 million to $20.8 million. The decrease was expected due to the market transition away from the prior generation of hardware platforms, such as PS1, to the current generation console systems. We expect sales of PS1 products to continue to decline in fiscal 2005.

Game Boy Advance Net Revenue

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$24,621	4%	$44,060	7%	$(19,439)	(44%)

Net revenue from sales of titles for the GBA for the year ended March 31, 2004 decreased 44% from the prior fiscal year, from $44.1 million to $24.6 million. This is due to a decrease in the number of GBA games released year-over-year. In fiscal 2003, we released 11 GBA titles, whereas in fiscal 2004 we released 4 GBA titles. We expect the hand-held installed base to grow with the release of the NDS and PSP which are expected to launch in late calendar year 2004 and early calendar year 2005, respectively. In addition, in fiscal 2005, as the GBA hardware approaches the peak of its life cycle, we expect to increase our focus on developing GBA games for mass-market consumers.

The platform mix of our future publishing net revenues will likely be impacted by a number of factors, including the ability of hardware manufacturers to continue to increase their installed hardware base, the introduction of new hardware platforms, as well as the timing of key product releases from our product release schedule. We expect that net revenues from console titles will continue to represent the largest component of our publishing net revenues with PS2 having the largest percentage of that business due to its larger installed hardware base. We expect net revenues from hand-held titles to remain the smallest component of our publishing net revenues. However, if the PSP and/or the NDS hand-held devices are introduced in fiscal 2005, we may see an increase in our hand-held business in comparison to prior periods. Our net revenues from PC titles will be primarily driven by our product release schedule.

A significant portion of our revenues and profits are derived from a relatively small number of popular titles and brands each year as revenues and profits are significantly affected by our ability to release highly successful or "hit" titles. For example, for the year ended March 31, 2004, 28% of our consolidated net revenues and 40% of worldwide publishing net revenues were derived from net revenues from our *Tony Hawk's Underground* and *True Crime: Streets of L.A.* titles. Though many of these titles have substantial production or acquisition costs and marketing budgets, once a title recoups these costs, incremental net revenues directly and positively impact operating profits resulting in a disproportionate amount of operating income being derived from these select titles. We expect that a limited number of titles and brands will continue to produce a disproportionately large amount of our net revenues and profits.

Two factors that could affect future publishing and distribution net revenue performance are console hardware pricing and software pricing. As console hardware moves through its life cycle, hardware manufacturers typically enact price reductions. Reductions in the price of console hardware typically result in an increase in the installed base of hardware owned by consumers. Price cuts on Xbox and PS2 hardware were announced in March and May 2004, respectively. Historically, we have also seen that lower console hardware prices put downward pressure on software pricing. While we expect console software launch pricing for most genres to hold at $49.99 through the calendar 2004 holidays, we believe we could see additional software price declines thereafter.

Distribution Net Revenue

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$281,924	30%	$248,141	29%	$33,783	14%

Distribution net revenues for the year ended March 31, 2004 increased 14% from the prior fiscal year, from $248.1 million to $281.9 million. The increase was primarily due to the positive impact of the year-over-year strengthening of the EUR and the GBP in relation to the U.S. dollar. Excluding the impact of the changing foreign currency rates, our distribution net revenue was in line with our prior fiscal year, with a slight increase of 2% year-over-year. The mix of distribution net revenues between hardware and software sales varied year-over-year with approximately 28% hardware in the year ended March 31, 2004 as compared to 38% hardware in the prior fiscal year. This is mainly attributed to an increase in business with large, mass-market customers that generate a higher percentage of sales from software. In both fiscal years, hardware sales were principally comprised of sales of console hardware. The mix of future distribution net revenues will be driven by a number of factors including the occurrence of further hardware price reductions instituted by hardware manufacturers, the introduction of new hardware platforms and our ability to establish and maintain distribution agreements with hardware manufacturers and third-party software publishers. We are expecting our fiscal 2005 distribution results to be in line with fiscal 2004.

Costs and Expenses

Cost of Sales—Product Costs

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$475,541	50%	$440,977	51%	$34,564	8%

Cost of sales—product costs represented 50% and 51% of consolidated net revenues for the years ended March 31, 2004 and 2003, respectively. In absolute dollars, cost of sales—product costs increased due to higher sales volume in fiscal 2004 as compared to fiscal 2003. There were two primary factors that affected cost of sales—product costs as a percentage of consolidated net revenues:

- The product mix of our publishing business for the year ended March 31, 2004 reflects a lower proportion of net revenues from titles for hand-held devices, as compared to the year ended March 31, 2003. Titles for hand-held devices generally have the highest manufacturing per unit cost of all platforms.
- Due to the lower manufacturing costs for PC titles, we were able to benefit from the strong sales of *Call of Duty* for the year ended March 31, 2004.

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We expect cost of sales—product costs as a percentage of net revenue to decrease primarily due to a lower percentage of revenue generated from our distribution business in fiscal 2005, which is a lower margin business. We may also receive a benefit from changes in product mix in fiscal 2005 due to an increase in PC publishing net revenues as a percentage of total publishing net revenues and the focus on "big proposition" titles, for which we could benefit from volume discounts.

Cost of Sales—Software Royalties and Amortization

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$59,744	9%	$79,194	13%	$(19,450)	(25%)

Cost of sales—software royalties and amortization for the year ended March 31, 2004 decreased as a percentage of publishing net revenues from the prior fiscal year, from 13% to 9%. In absolute dollars, cost of sales—software royalties and amortization for the year ended March 31, 2004 also decreased from the prior fiscal year, from $79.2 million to $59.7 million. The decrease in absolute dollars reflects that there were approximately fifteen major titles released in fiscal 2004 as compared to over twenty in fiscal 2003. The decrease in the percentage reflects the strong performance of our internally developed key fiscal 2004 third quarter releases.

Cost of Sales—Intellectual Property Licenses

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$31,862	5%	$45,002	7%	$(13,140)	(29%)

Cost of sales—intellectual property licenses for the year ended March 31, 2004 decreased in absolute dollars and as a percentage of publishing net revenues over the same period last year, from 7% to 5%. The decreases reflect the fact that two of our top performing titles in fiscal 2004, *True Crime: Streets of L.A.* and *Call of Duty*, were based on our wholly-owned original intellectual property. Additionally, during fiscal 2003, we recorded an approximate $7.0 million charge related to an assessment of the recoverability of certain of our investments in long-term licensing agreements. We expect cost of sales—intellectual property licenses to increase in fiscal 2005 as compared to fiscal 2004, as we expect to have more titles releasing with licensed intellectual property.

Product Development

(In thousands)

March 31, 2004	% of Publishing Net Revenue	March 31, 2003	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$97,859	15%	$56,971	9%	$40,888	72%

Product development expenses for the year ended March 31, 2004 increased as a percentage of publishing net revenues from the prior fiscal year, from 9% to 15%. In absolute dollars, product development expenses for the year ended March 31, 2004 also increased from the prior fiscal year, from $57.0 million to $97.9 million. The increase in product development as a percentage of publishing net revenues and in absolute dollars resulted from:

- A $21 million game cancellation charge recorded in the fiscal 2004 third quarter. We executed a realignment of our product portfolio driven by the evolution of the video game market, which is increasingly dominated by high quality products that are based on recognizable franchises and supported with big marketing programs. We completed a comprehensive review of our product portfolio in which we evaluated each product based on a number of criteria, including: the strength of the franchise, the projected product quality, the potential responsiveness of the product to aggressive marketing support and the financial risk in the event of product failure. As a result of this review, we believe that we have an extensive slate of high potential properties in development. However, we found that certain projects had a lower likelihood of achieving acceptable levels of operating performance and that continued pursuit of these projects would create a substantial opportunity cost as it related to our slate of high potential projects. Accordingly, in the three months ended December 31, 2003, we cancelled the development of ten products that we believed were unlikely to produce an acceptable level of return on our investment. In connection with the cancellation of these products, we recorded a pre-tax charge of approximately $21 million.
- Our increased emphasis on product quality and the lengthening of product development schedules. To maintain the competitiveness of our products and to take advantage of increasingly sophisticated technology associated with new hardware platforms, we have increased the amount of time spent play-testing new products, conducted more extensive product quality evaluations and lengthened product development schedules to allow time to make the improvements indicated by our testing and evaluations. We are focused on improved game quality, and in many cases, this has resulted in an increase in product development costs.
- The increase in absolute dollars is also due to an increase in studio employee incentive compensation as a result of the strong performances of key fiscal 2004 title releases.

Sales and Marketing

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$128,221	14%	$100,646	12%	$27,575	27%

Sales and marketing expenses of $128.2 million and $100.6 million represented 14% and 12% of consolidated net revenues for the years ended March 31, 2004 and 2003, respectively. The increase in sales and marketing expense dollars and as a percentage of net revenues for the year ended March 31, 2004 from the prior fiscal year was primarily generated by our publishing business as a result of significant marketing programs, including television and in-theatre ad campaigns and in-store promotions, run in support of our three key fiscal 2004 third quarter title releases, *Tony Hawk's Underground*, and our two new original properties, *True Crime: Streets of L.A.* and *Call of Duty*. We expect to continue to provide significant marketing support for our future "big proposition" titles. Accordingly, we expect fiscal 2005 sales and marketing costs to exceed fiscal 2004 spending levels.

General and Administrative

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$44,612	5%	$46,479	5%	$(1,867)	(4%)

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General and administrative expenses for the year ended March 31, 2004 decreased $1.9 million over the same period last year, from $46.5 million to $44.6 million. As a percentage of consolidated net revenues, general and administrative expenses remained constant at 5%. The decrease in absolute dollars was primarily due to:

- Lower bad debt expense of approximately $3.9 million.
- The incurrence in the first quarter of fiscal 2003 of $1.0 million of merger related expenses by our publishing business.
- An approximate $2.0 million charge incurred in fiscal 2003 by our distribution business for the relocation of our UK distribution facility.

Partially offset by:

- A $5.2 million year-over-year increase in general and administrative employee related costs in both our publishing and distribution businesses.

Operating Income

(In thousands)	March 31, 2004	% of Segment Net Revs	March 31, 2003	% of Segment Net Revs	Increase/ (Decrease)	Percent Change
Publishing	$ 93,223	14%	$79,139	13%	$14,084	18%
Distribution	16,594	6	15,708	6	886	6
Consolidated	$109,817	12%	$94,847	11%	$14,970	16%

Publishing operating income for the year ended March 31, 2004 increased $14.1 million from the same period last year, from $79.1 million to $93.2 million. International publishing operating income for the year ended March 31, 2004 benefited from the positive impact of the year-over-year strengthening of the EUR and the GBP in relation to the U.S. dollar. Excluding the impact of changes in foreign currency rates, publishing operating income for the year ended March 31, 2004 increased approximately $7.8 million from the same period last year. This increase is primarily due to:

- Strong performance in both the domestic and international markets of our fiscal 2004 third quarter title releases.

Partially offset by:

- Increased sales and marketing spending.
- The product development charge recorded in the fiscal 2004 third quarter in connection with the cancellation of ten products.

Distribution operating income for the year ended March 31, 2004 increased slightly over the same period last year, from $15.7 million to $16.6 million. Distribution operating income for the year ended March 31, 2004 benefited from the positive impact of the year-over-year strengthening of the EUR and the GBP in relation to the U.S. dollar. Excluding the impact of changes in foreign currency rates, distribution operating income for the year ended March 31, 2004 was down slightly by approximately $0.9 million from the same period last year. This decrease is primarily due to an increase in general and administrative employee related costs.

Investment Income, Net

(In thousands)

March 31, 2004	% of Consolidated Net Revenue	March 31, 2003	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$6,175	—%	$8,560	1%	$(2,385)	(28%)

Investment income, net for the year ended March 31, 2004 was $6.2 million as compared to $8.6 million for the year ended March 31, 2003. The decrease was primarily due to interest rate reductions and the utilization of excess cash to enter into structured stock repurchase transactions and to purchase treasury stock during the year ended March 31, 2004. Premiums earned on structured stock repurchase transactions are recorded in additional paid-in capital.

Provision for Income Taxes

(In thousands)

March 31, 2004	% of Pre-Tax Income	March 31, 2003	% of Pre-Tax Income	Increase/ (Decrease)	Percent Change
$38,277	33%	$37,227	36%	$1,050	3%

The income tax provision of $38.3 million for the year ended March 31, 2004 reflects our effective income tax rate of 33%. The significant items that generated the variance between our effective rate and our statutory rate of 35% were research and development tax credits and the impact of foreign tax rate differentials, partially offset by an increase in our deferred tax asset valuation allowance and state taxes. The realization of deferred tax assets depends primarily on the generation of future taxable income. We believe that it is more likely than not that we will generate taxable income sufficient to realize the benefit of net deferred tax assets recognized.

Results of Operations—Fiscal Years Ended March 31, 2003 and 2002

Net income for the year ended March 31, 2003 was $66.2 million or $0.43 per diluted share, as compared to $52.2 million or $0.39 per diluted share for the year ended March 31, 2002.

Net Revenues

Net revenues for the year ended March 31, 2003 increased 10% from the prior fiscal year, from $786.4 million to $864.1 million. This increase was generated by our publishing business and, to a lesser degree, our distribution business.

The following table details our consolidated net revenues by business segment and our publishing net revenues by territory for the years ended March 31, 2003 and 2002 (in thousands):

Year ended March 31,	2003	2002	Increase/ (Decrease)	Percent Change
Publishing Net Revenues				
North America	$432,261	$404,905	$27,356	7%
Europe	164,984	131,873	33,111	25%
Other	18,730	12,730	6,000	47%
Total International	183,714	144,603	39,111	27%
Total Publishing Net Revenues	615,975	549,508	66,467	12%
Distribution Net Revenues	248,141	236,926	11,215	5%
Consolidated Net Revenues	$864,116	$786,434	$77,682	10%

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Publishing net revenues for the year ended March 31, 2003 increased 12% from the prior fiscal year, from $549.5 million to $616.0 million. The following table details our publishing net revenues by platform as a percentage of total publishing net revenues for the years ended March 31, 2003 and 2002 (in thousands):

	Year Ended March 31, 2003	% of Publishing Net Revenues	Year Ended March 31, 2002	% of Publishing Net Revenues	Increase/ (Decrease)	Percent Change
Publishing Net Revenues						
PC	$ 99,893	16%	$117,345	21%	$ (17,452)	(15%)
Console						
PlayStation 2	260,307	42%	110,120	20%	150,187	136%
Microsoft Xbox	75,329	12%	32,921	6%	42,408	129%
Nintendo GameCube	74,694	12%	16,773	3%	57,921	345%
PlayStation	52,722	9%	113,655	21%	(60,933)	(54%)
Other	3,064	1%	39,517	7%	(36,453)	(92%)
Total Console	466,116	76%	312,986	57%	153,130	49%
Hand-held						
Game Boy Advance	44,060	7%	79,168	15%	(35,108)	(44%)
Game Boy Color	5,906	1%	40,009	7%	(34,103)	(85%)
Total Hand-held	49,966	8%	119,177	22%	(69,211)	(58%)
Total Publishing Net Revenues	$615,975	100%	$549,508	100%	$ 66,467	12%

There were several factors that affected the fiscal 2003 net revenue performance of our publishing business. First, positively impacting our performance, was an improvement in console sales. Our publishing console net revenues for the year ended March 31, 2003 increased 49% from the prior fiscal year, from $313.0 million to $466.1 million. Fiscal 2003 publishing console net revenues reflect the simultaneous cross-platform, multi-national releases of *Spider-Man: The Movie* in the first quarter and *Tony Hawk's Pro Skater 4* in the third quarter. In addition, publishing console net revenue performance was also driven by the following releases: *Tenchu: Wrath of Heaven*, *Street Hoops* and *Cabela's Big Game Hunter* for PS2. Second, publishing hand-held net revenues for the year ended March 31, 2003 decreased by 58% from the prior fiscal year, from $119.2 million to $50.0 million. This decrease reflects the fact that the GBA hardware was launched in June 2001. Our GBA software sales for the year ended March 31, 2002 benefited from the related hardware launch. We also released fewer titles for the hand-held platforms in fiscal 2003—11 titles, in comparison to 19 titles in fiscal 2002. Additionally, the average retail price of titles for hand-held devices was lower in fiscal 2003 than in fiscal 2002. Third, PC net revenues for the year ended March 31, 2003 decreased 15% from the prior fiscal year, from $117.3 million to $99.9 million. Though the number of PC titles released in fiscal 2003 was relatively consistent with fiscal 2002, during fiscal 2002, we released *Return to Castle Wolfenstein* for the PC, which was one of our top performing titles of fiscal 2002. PC net revenues for the year ended March 31, 2002 reflect that title's worldwide strong performance. Lastly, net revenues from our international publishing business for the year ended March 31, 2003 benefited by approximately $14.1 million from a year-over-year strengthening of the EUR and the GBP in relation to the U.S. dollar. Excluding the impact of foreign currency fluctuations, our domestic publishing business and our international publishing business experienced similar year-over-year improvements for the reasons detailed above.

A significant portion of our revenues and profits are derived from a relatively small number of popular titles and brands each year as revenues and profits are significantly affected by our ability to release highly successful or "hit" titles. For example, for the year ended March 31, 2003, 30% of our consolidated net revenues and 43% of worldwide publishing net revenues were derived from net revenues from our *Spider-Man: The Movie* and *Tony Hawk's Pro Skater 4* titles. Though many of these titles have substantial production or acquisition costs and marketing budgets, once a title recoups these costs, incremental net revenues directly and positively impacts operating profits resulting in a disproportionate amount of operating income being derived from these select titles. We expect that a limited number of titles and brands will continue to produce a disproportionately large amount of our net revenues and profits.

Distribution net revenues for the year ended March 31, 2003 increased 5% from the prior fiscal year, from $236.9 million to $248.1 million. The increase was due to the positive impact of the year-over-year strengthening of the EUR and the GBP in relation to the U.S. dollar. Distribution console net revenues for the year ended March 31, 2003 also benefited from the international hardware launches of Xbox and GameCube in March 2002 and May 2002, respectively. It additionally benefited from the price reduction on PS2 hardware that was effective September 2001, as this resulted in both an increase in sales of PS2 hardware, as well as an increase in sales of PS2 software due to the corresponding larger installed hardware base. This increase was partially offset by declines in distribution hand-held and PC net revenues for the reasons detailed in the discussion of publishing net revenues. The mix of distribution net revenues between hardware and software sales remained relatively constant year-over-year at approximately 38% hardware and 62% software.

Domestic net revenues increased 7% from $404.9 million for the year ended March 31, 2002 to $432.3 million for the year ended March 31, 2003 for the reasons detailed above in the discussion of our publishing business net revenues. International net revenues increased by 13% from $381.5 million for the year ended March 31, 2002 to $431.9 million for the year ended March 31, 2003 for the reasons detailed above in the discussion of our publishing business, as well as the result of the year-over-year strengthening of the EUR and the GBP in relation to the U.S. dollar.

Costs and Expenses

Cost of Sales—Product Costs

(In thousands)

March 31, 2003	% of Consolidated Net Revenue	March 31, 2002	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$440,977	51%	$435,725	56%	$5,252	1%

Cost of sales—product costs represented 51% and 56% of consolidated net revenues for the years ended March 31, 2003 and 2002, respectively. There were two primary factors that affected cost of sales—product costs as a percentage of consolidated net revenues. First, the product mix of our publishing business for the year ended March 31, 2003 reflects a lower proportion of net revenues from titles for hand-held devices, as compared to the year ended March 31, 2002. Titles for hand-held devices generally have the highest manufacturing per unit cost of all platforms. Second, our manufacturing costs for console titles for the year ended March 31, 2003 benefited from the economies of scale due to the high volume of *Spider-Man: The Movie* units manufactured.

Cost of Sales—Software Royalties and Amortization

(In thousands)

March 31, 2003	% of Publishing Net Revenue	March 31, 2002	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$79,194	13%	$58,892	11%	$20,302	34%

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Cost of sales—software royalties and amortization for the year ended March 31, 2003 increased as a percentage of publishing net revenues from the prior fiscal year, from 11% to 13%. In absolute dollars, cost of sales—software royalties and amortization for the year ended March 31, 2003 also increased from the prior fiscal year, from $58.9 million to $79.2 million. The increases reflect the change in the product mix of our publishing business. Though titles for hand-held devices generally have the highest per unit manufacturing cost of all platforms, they have the lowest product development cost structure. In the year ended March 31, 2002 in which titles for hand-held devices accounted for a higher proportion of publishing net revenues, the related cost of sales—software royalties and amortization was correspondingly low. This is in comparison to the year ended March 31, 2003 in which console titles accounted for a higher proportion of publishing net revenues. Console titles such as PS2, Xbox and GameCube have high product development cost structures, and the release of titles on these platforms will result in a correspondingly high cost of sales—software royalties and amortization. In addition, we recorded during the fourth quarter of fiscal 2003 approximately $8.0 million related to an assessment of the recoverability of capitalized development costs pertaining to certain products.

Cost of Sales—Intellectual Property Licenses

(In thousands)

March 31, 2003	% of Publishing Net Revenue	March 31, 2002	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$45,002	7%	$40,114	7%	$4,888	12%

Cost of sales—intellectual property licenses for the year ended March 31, 2003 remained constant as a percentage of publishing net revenues with the prior fiscal year at 7%. In absolute dollars, cost of sales—intellectual property licenses for the year ended March 31, 2003 increased from the prior fiscal year, from $40.1 million to $45.0 million. During the fourth quarter of fiscal 2003, we recorded an approximate $7.0 million related to an assessment of the recoverability of certain of our investments in long-term licensing agreements. We recorded additional costs relating to common stock warrants issued in connection with those licensing agreements. The impact of these costs was partially offset by the fact that one of our top performing titles released in fiscal 2002 had a higher intellectual property royalty rate structure than the majority of the top performing titles released in fiscal 2003.

Product Development

(In thousands)

March 31, 2003	% of Publishing Net Revenue	March 31, 2002	% of Publishing Net Revenue	Increase/ (Decrease)	Percent Change
$56,971	9%	$40,960	7%	$16,011	39%

Product development expenses for the year ended March 31, 2003 increased as a percentage of publishing net revenues from the prior fiscal year, from 7% to 9%. In absolute dollars, product development expense for the year ended March 31, 2003 also increased from the prior fiscal year, from $41.0 million to $57.0 million. These increases reflect the change in the product mix of titles in development—more console and less hand-held—during fiscal 2003. The cost to develop titles for current console systems, such as PS2, Xbox and GameCube, is higher than the cost to develop titles for the legacy console systems and hand-held devices. Additionally, we had more titles in development during fiscal 2003 than fiscal 2002. Lastly, in the fourth quarter of fiscal 2003, we decided to eliminate certain smaller and non-core projects from our future development plan. The cost relating to the cancellation of those titles was approximately $2.6 million.

Sales and Marketing

(In thousands) March 31, 2003	% of Consolidated Net Revenue	March 31, 2002	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$100,646	12%	$86,161	11%	$14,485	17%

Sales and marketing expenses of $100.6 million and $86.2 million represented 12% and 11% of consolidated net revenues for the years ended March 31, 2003 and 2002, respectively. The increase in sales and marketing expense dollars for the year ended March 31, 2003 from the prior fiscal year was the result of increased costs in both our publishing and distribution businesses. The increase in sales and marketing expense dollars in our publishing business was the result of a significant marketing program in support of the simultaneous cross-platform, multinational release of *Spider-Man: The Movie* during the first quarter of fiscal 2003, as well as increased TV and print ads in support of second, third and fourth quarter releases such as *Street Hoops, Tony Hawk's Pro Skater 4* and *Tenchu: Wrath of Heaven*. Additionally, in the year ended March 31, 2003, we provided sponsorship for select action sports tours/tournaments in support of our Activision action sports brands. The increase in sales and marketing expense dollars in our distribution business was due to an increasing percentage of our distribution business being generated from large national accounts. Such large national accounts generally result in increased sales costs.

General and Administrative

(In thousands) March 31, 2003	% of Consolidated Net Revenue	March 31, 2002	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$46,479	5%	$44,008	6%	$2,471	6%

General and administrative expenses for the year ended March 31, 2003 increased $2.5 million from the prior fiscal year, from $44.0 million to $46.5 million. As a percentage of consolidated net revenues, general and administrative expenses remained relatively constant year-over-year at approximately 5% to 6% as a result of our continued focus on building operating efficiencies and controlling costs. The increase in absolute dollars was primarily due to the incurrence in the first quarter of fiscal 2003 of an approximate $2.0 million charge for the relocation of our UK distribution facility due to the increased growth of our UK distribution and UK publishing businesses.

Operating Income

(In thousands)	March 31, 2003	% of Segment Net Revenues	March 31, 2002	% of Segment Net Revenues	Increase/ (Decrease)	Percent Change
Publishing	$79,139	13%	$68,675	12%	$10,464	15%
Distribution	15,708	6	11,899	5	3,809	32
Consolidated	$94,847	11%	$80,574	10%	$14,273	18%

Operating income for the year ended March 31, 2003 was $94.8 million, compared to $80.6 million in the prior fiscal year. The increase reflects improvements in both our publishing and distribution businesses. Publishing operating income improvement reflects, as previously discussed, the benefits generated by the release of hit titles, the decrease in cost of sales—product costs due to changes in product mix and our continued focus on building operating efficiencies and controlling costs. Distribution operating income improvement includes the distribution of a very successful third-party publisher's title in several countries and reductions in headcount related expenses.

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Investment Income, Net

(In thousands)

March 31, 2003	% of Consolidated Net Revenue	March 31, 2002	% of Consolidated Net Revenue	Increase/ (Decrease)	Percent Change
$8,560	1%	$2,546	1%	$6,014	236%

Investment income, net for the year ended March 31, 2003 was $8.6 million as compared to $2.5 million for the year ended March 31, 2002. The increase is primarily due to higher average cash and short-term investment balances during fiscal 2003, partially offset by lower market rates.

Provision for Income Taxes

(In thousands)

March 31, 2003	% of Pre-Tax Income	March 31, 2002	% of Pre-Tax Income	Increase/ (Decrease)	Percent Change
$37,227	36%	$30,882	37%	$6,345	21%

The income tax provision of $37.2 million for the year ended March 31, 2003 reflects our effective income tax rate of 36%. The significant items that generated the variance between our effective rate and our statutory rate of 35% were state taxes and an increase in our deferred tax asset valuation allowance, partially offset by research and development tax credits and the impact of foreign tax rate differentials. The realization of deferred tax assets depends primarily on the generation of future taxable income. We believe that it is more likely than not that we will generate taxable income sufficient to realize the benefit of net deferred tax assets recognized.

Quarterly Operating Results

Our quarterly operating results have in the past varied significantly and will likely vary significantly in the future, depending on numerous factors, several of which are not under our control. For a detailed description of these factors see our Form 10-K filed with the Securities and Exchange Commission. Our business also has experienced and is expected to continue to experience significant seasonality, largely due to consumer buying patterns and our product release schedule focusing on those patterns. Net revenues typically are significantly higher during the fourth calendar quarter, primarily due to the increased demand for consumer software during the year-end holiday buying season. Accordingly, we believe that period-to-period comparisons of our operating results are not necessarily meaningful and should not be relied upon as indications of future performance.

The following table is a comparative breakdown of our quarterly results for the immediately preceding eight quarters (amounts in thousands, except per share data):

	Restated(1)							
Quarter ended	March 31, 2004	Dec. 31, 2003(2)	Sept. 30, 2003	June 30, 2003	March 31, 2003(2)	Dec. 31, 2002	Sept. 30, 2002	June 30, 2002
Net revenues	$162,897	$508,511	$117,523	$158,725	$125,001	$378,685	$169,172	$191,258
Operating income (loss)	4,643	116,961	(16,933)	5,146	(14,444)	66,761	11,334	31,196
Net income (loss)	6,664	76,981	(10,093)	4,163	(7,957)	44,347	9,086	20,704
Basic earnings (loss) per share	0.05	0.58	(0.08)	0.03	(0.06)	0.30	0.06	0.15
Diluted earnings (loss) per share	0.04	0.53	(0.08)	0.03	(0.06)	0.28	0.06	0.14

(1) Consolidated financial information has been restated for the effect of our three-for-two stock split effected in the form of a 50% stock dividend to shareholders of record as of February 23, 2004, paid March 15, 2004.

(2) See Note 5, "Software Development Costs and Intellectual Property Licenses" of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

Liquidity and Capital Resources

Sources of Liquidity

(In thousands) As of and for the year ended March 31,	2004	2003	Increase/ (Decrease)
Cash and cash equivalents	$466,552	$ 285,554	$180,998
Short-term investments	121,097	121,400	(303)
	$587,649	$ 406,954	$180,695
Percentage of total assets	61%	58%	
Cash flows provided by operating activities	$ 67,403	$ 90,975	$ (23,572)
Cash flows used in investing activities	(15,169)	(155,101)	139,932
Cash flows provided by financing activities	117,569	64,090	53,479

As of March 31, 2004, our primary source of liquidity is comprised of $466.6 million of cash and cash equivalents and $121.1 million of short-term investments. Over the last three years, our primary sources of liquidity have included cash on hand at the beginning of the year and cash flows generated from continuing operations. We have also generated significant cash flows from the issuance of our common stock to employees through the exercise of options and to the public through an underwritten public offering in fiscal 2003, as well as from the utilization of structured stock repurchase transactions, which are described in more detail below in "Cash Flows from Financing Activities." In recent years, we have not utilized debt financing as a significant source of cash flows. However, we do have available at certain of our international locations, credit facilities, which are described below in "Credit Facilities," that can be utilized if needed.

In August 2003, we filed with the Securities and Exchange Commission two amended shelf registration statements, including the base prospectuses therein. The first shelf registration statement, on Form S-3, allows us, at any time, to offer any combination of securities described in the base prospectus in one or more offerings with an aggregate initial offering price of up to $500.0 million. Unless we state otherwise in the applicable prospectus supplement, we expect to use the net proceeds from the sale of the securities for general corporate purposes, including capital expenditures, working capital, repayment or reduction of long-term and short-term debt and the financing of acquisitions and other business combinations. We may invest funds that we do not immediately require in marketable securities.

The second shelf registration statement, on Form S-4, allows us, at any time, to offer any combination of securities described in the base prospectus in one or more offerings with an aggregate initial offering price of up to $250.0 million in connection with our acquisition of the assets, business or securities of other companies whether by purchase, merger, or any other form of business combination.

We believe that we have sufficient working capital ($675.8 million at March 31, 2004), as well as proceeds available from our international credit facilities, to finance our operational requirements for at least the next twelve months, including purchases of inventory and equipment, the funding of the development, production, marketing and sale of new products and the acquisition of intellectual property rights for future products from third parties.

Cash Flows from Operating Activities

In recent years, the primary drivers of cash flows from operating activities typically have included the collection of customer receivables generated by the sale of our products, offset by payments to vendors for the manufacture, distribution and marketing of our products, third-party developers and intellectual property holders and our own employees. A significant operating use of our cash relates to our continued investment in software development and intellectual property licenses. We spent approximately $115.2 million and $151.6 million in the years ended March 31, 2004 and 2003, respectively, in connection with the acquisition of publishing or distribution rights for products being developed by third parties, the execution of new license agreements granting us long-term rights to intellectual property of

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third parties, as well as the capitalization of product development costs relating to internally developed products. We expect that we will continue to make significant expenditures relating to our investment in software development and intellectual property licenses. Our future cash commitments relating to these investments are detailed below in "Commitments." Cash flows from operations are affected by our ability to release highly successful or "hit" titles. Though many of these titles have substantial production or acquisition costs and marketing budgets, once a title recoups these costs, incremental net revenues typically will directly and positively impact cash flows.

The principal components comprising cash flows from operating activities for the year ended March 31, 2004 included favorable operating results and increases in accounts payable, partially offset by increases in accounts receivable and our continued investment in software development and intellectual property licenses. See an analysis of the change in key balance sheet accounts below in "Key Balance Sheet Accounts." We expect that a primary source of future liquidity, both short-term and long-term, will be the result of cash flows from continuing operations.

Cash Flows from Investing Activities

In recent years, the primary drivers of cash used in investing activities typically have included capital expenditures, acquisitions of privately held interactive software development companies and the net effect of purchases and sales/maturities of short-term investment vehicles. The goal of our short-term investments is to maximize return while minimizing risk, maintaining liquidity, coordinating with anticipated working capital needs and providing for prudent investment diversification.

For the year ended March 31, 2004, cash flows used in investing activities were primarily the result of capital expenditures and the utilization of approximately $3.5 million of cash to acquire the privately held interactive software development company, Infinity Ward. We have historically financed our acquisitions through the issuance of shares of common stock or a combination of common stock and cash. We will continue to evaluate potential acquisition candidates as to the benefit they bring to us.

Cash Flows from Financing Activities

In recent years, the primary drivers of cash provided by financing activities have related to transactions involving our common stock, including the issuance of shares of common stock to employees and the public, the purchase of treasury shares, as well as the use of structured stock repurchase transactions. In recent years, we have not utilized debt financing as a significant source of cash flows. However, we do have available at certain of our international locations, credit facilities, which are described below in "Credit Facilities," that can be utilized if needed.

The cash provided by financing activities for the year ended March 31, 2004 primarily is the result of the maturity of structured stock repurchase transactions, partially offset by cash used to purchase treasury stock and enter into additional structured stock repurchase transactions. During fiscal 2003, our Board of Directors authorized a buyback program under which we can repurchase up to $350.0 million of our common stock. Under the program, shares may be purchased as determined by management and within certain guidelines, from time to time, in the open market or in privately negotiated transactions, including privately negotiated structured stock repurchase transactions and through transactions in the options markets. Depending on market conditions and other factors, these purchases may be commenced or suspended at any time or from time to time without prior notice. In the past, we have entered into structured stock repurchase transactions that were settled in cash or stock based on the market price of our common stock on the date of the settlement. Upon settlement, we either had our capital investment returned with a premium or received shares of our common stock, depending, respectively, on whether the market price of our common stock was above or below a pre-determined price agreed in connection with each such transaction. As of March 31, 2004, we had approximately $226.2 million available for utilization under the buyback program and no outstanding structured stock repurchase transactions. We actively manage our capital structure and balance sheet as a component of our overall business strategy. Accordingly, in the future, when we determine that market conditions are appropriate, we may seek to achieve long-term value for the shareholders through, among other things, new debt or equity financings or refinancings, share repurchases and other transactions involving our equity or debt securities.

Key Balance Sheet Accounts

Accounts Receivable *(Amounts in thousands)*	March 31, 2004	March 31, 2003	Increase/ (Decrease)
Gross accounts receivable	$109,605	$73,178	$36,427
Net accounts receivable	62,577	15,822	46,755

The increase in gross accounts receivable was primarily the result of:

- Higher sales in the fourth quarter of fiscal 2004 over the prior year quarter due to the continued strong sales of our key third quarter fiscal 2004 releases, *True Crime: Streets of L.A.*, *Tony Hawk's Underground* and *Call of Duty*, and an increase in the number of titles released in the fourth quarter of fiscal 2004 (*Tenchu: Return from Darkness* on Xbox and *Pitfall: The Lost Expedition* and *MTX: Mototrax* on multiple platforms) over the prior year quarter (*Tenchu: Wrath of Heaven* on PS2).
- A significant increase in business of our UK distribution facility with large, mass-market customers. Large, mass-market customers typically have longer trading terms than smaller, independent accounts.

Reserves for returns, price protection and bad debt decreased from $57.4 million at March 31, 2003 to $47.0 million at March 31, 2004, primarily due to the strong sell through to end consumers of our key third quarter fiscal 2004 releases.

Inventories *(Amounts in thousands)*	March 31, 2004	March 31, 2003	Increase/ (Decrease)
Inventories	$26,427	$19,577	$6,850

The increase in inventories was driven by our distribution business, primarily the result of:

- Higher PS2 hardware on hand at March 31, 2004 at our UK distribution facility.

Software Development and Intellectual Property Licenses *(Amounts in thousands)*	March 31, 2004	March 31, 2003	Increase/ (Decrease)
Software development and intellectual property licenses	$135,201	$107,921	$27,280

The increase in software development and intellectual property licenses was primarily the result of:

- Continued investment in software development and intellectual property licenses. We spent approximately $115.2 million in the year ended March 31, 2004 in connection with the acquisition of publishing or distribution rights for products being developed by third parties, the execution of new license agreements granting us long-term rights to intellectual property of third parties, as well as the capitalization of product development costs relating to internally developed products.

Offset by:

- $87.9 million of amortization and write-offs of capitalized software development costs and intellectual property licenses.

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Accounts Payable *(Amounts in thousands)*	March 31, 2004	March 31, 2003	Increase/ (Decrease)
Accounts payable	$72,874	$45,602	$27,272

The increase in accounts payable was primarily the result of:

- Increased inventory purchases by our publishing business as a result of the increased sales in the fourth quarter of fiscal 2004 over the prior year quarter due to the continued strong sales of our key third quarter fiscal 2004 releases, *True Crime: Streets of L.A.*, *Tony Hawk's Underground* and *Call of Duty,* and an increase in the number of titles released in the fourth quarter of fiscal 2004 (*Tenchu: Return from Darkness* on Xbox and *Pitfall: The Lost Expedition* and *MTX: Mototrax* on multiple platforms) over the prior year quarter (*Tenchu: Wrath of Heaven* on PS2).

Accrued Expenses *(Amounts in thousands)*	March 31, 2004	March 31, 2003	Increase/ (Decrease)
Accrued expenses	$63,205	$58,656	$4,549

The increase in accrued expenses was primarily driven by:

- Marketing support for our key title releases.
- Increased foreign income taxes payable.
- Increased annual bonuses as a result of company performance.

Partially offset by:

- A $7.5 million accrual at March 31, 2003 for the settlement of treasury stock purchases.

Credit Facilities

We have revolving credit facilities with our Centresoft subsidiary located in the UK (the "UK Facility") and our NBG subsidiary located in Germany (the "German Facility"). The UK Facility provided Centresoft with the ability to borrow up to GBP 8.0 million ($14.6 million), including issuing letters of credit, on a revolving basis as of March 31, 2004. Furthermore, under the UK Facility, Centresoft provided a GBP 0.3 million ($0.5 million) guarantee for the benefit of our CD Contact subsidiary as of March 31, 2004. The UK Facility bore interest at LIBOR plus 2.0% as of March 31, 2004, is collateralized by substantially all of the assets of the subsidiary and expires in November 2004. The UK Facility also contains various covenants that require the subsidiary to maintain specified financial ratios related to, among others, fixed charges. As of March 31, 2004, we were in compliance with these covenants. No borrowings were outstanding against the UK Facility as of March 31, 2004. The German Facility provided for revolving loans up to EUR 0.5 million ($0.6 million) as of March 31, 2004, bore interest at a Eurocurrency rate plus 2.5%, is collateralized by certain of the subsidiary's property and equipment and has no expiration date. No borrowings were outstanding against the German Facility as of March 31, 2004.

Commitments

In the normal course of business, we enter into contractual arrangements with third parties for the development of products, as well as for the rights to intellectual property. Under these agreements, we commit to provide specified payments to a developer or intellectual property holder, based upon contractual arrangements. Typically, the payments to third-party developers are conditioned upon the achievement by the developers of contractually specified development milestones. These payments to third-party developers and intellectual property holders typically are deemed to be advances and are recoupable against future royalties earned by the developer or intellectual property holder based on the sale of the related game. Additionally, in connection with certain intellectual property right acquisitions and development agreements, we will commit to spend specified amounts for marketing support for the related game(s) which is to be developed or in which the intellectual property will be utilized. Assuming all contractual provisions are met, the total future minimum commitments for these and other contractual arrangements in place as of March 31, 2004 are scheduled to be paid as follows (amounts in thousands):

	Contractual Obligations			
Fiscal year ending March 31,	Facility Leases	Developer and IP	Marketing	Total
2005	$ 8,936	$62,529	$39,919	$111,384
2006	7,520	17,328	11,500	36,348
2007	6,870	4,545	15,000	26,415
2008	4,033	1,895	—	5,928
2009	2,993	3,020	—	6,013
Thereafter	16,222	—	—	16,222
Total	$46,574	$89,317	$66,419	$202,310

The developer and intellectual property commitments above exclude approximately $9.3 million of commitments originally scheduled to be paid between fiscal 2004 through fiscal 2007 relating to an intellectual property rights agreement with a third party. Effective June 30, 2003, we terminated the agreement and filed a breach of contract suit against the third party.

Financial Disclosure

We maintain internal controls over financial reporting, which generally include those controls relating to the preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America. We also are focused on our "disclosure controls and procedures," which, as defined by the Securities and Exchange Commission, are generally those controls and procedures designed to ensure that financial and non-financial information required to be disclosed in our reports filed with the Securities and Exchange Commission is reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is communicated to management, including our chief executive officer and our chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Our Disclosure Committee, which operates under the Board-approved Disclosure Committee Charter and Disclosure Controls & Procedures Policy, includes senior management representatives and assists executive management in its oversight of the accuracy and timeliness of our disclosures, as well as in implementing and evaluating our overall disclosure process. As part of our disclosure process, senior finance and operational representatives from all of our corporate divisions and business units prepare quarterly reports regarding their current quarter operational performance, future trends, subsequent events, internal controls, changes in internal controls and other accounting and disclosure-relevant information. These quarterly reports are reviewed by certain key corporate finance representatives. These corporate finance representatives also conduct quarterly interviews on a rotating basis with the preparers of selected quarterly reports. The results of the quarterly reports and related interviews are reviewed by the Disclosure Committee. Finance representatives also conduct reviews with our senior management team, our external counsel and other appropriate personnel involved in the disclosure process, as appropriate. Additionally, senior finance and operational representatives provide internal certifications regarding the accuracy of information they provide that is utilized in the preparation of our periodic public reports filed with the Securities and Exchange Commission. Financial results and other financial information also are reviewed with the Audit Committee of the board of directors on a quarterly basis. As required by applicable regulatory requirements, the Chief Executive Officer and the Chief Financial Officer review and make various certifications regarding the accuracy of our periodic public reports filed with the Securities and Exchange Commission, our disclosure controls and procedures, and our internal control over financial reporting. With the assistance of the Disclosure Committee, we will continue to assess and monitor our disclosure controls and procedures, and our internal controls over financial reporting, and will make refinements as necessary.

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Inflation

Our management currently believes that inflation has not had a material impact on continuing operations.

Quantitative and Qualitative Disclosures about Market Risk

Market risk is the potential loss arising from fluctuations in market rates and prices. Our market risk exposures primarily include fluctuations in interest rates, foreign currency exchange rates and market prices. Our market risk sensitive instruments are classified as "other than trading." Our views on market risk are not necessarily indicative of actual results that may occur and do not represent the maximum possible gains and losses that may occur, since actual gains and losses will differ from those estimated, based upon actual fluctuations in interest rates, foreign currency exchange rates and market prices and the timing of transactions.

Interest Rate Risk

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio. We do not use derivative financial instruments in our investment portfolio. We manage our interest rate risk by maintaining an investment portfolio consisting primarily of debt instruments with high credit quality and relatively short average maturities. We also manage our interest rate risk by maintaining sufficient cash and cash equivalent balances such that we are typically able to hold our investments to maturity. As of March 31, 2004, our cash equivalents and short-term investments included debt securities of $426.2 million.

The following table presents the amounts and related weighted average interest rates of our investment portfolio as of March 31, 2004 (amounts in thousands):

	Average Interest Rate	Amortized Cost	Fair Value
Cash equivalents:			
Fixed rate	1.12%	$305,132	$305,132
Variable rate	0.95	60,006	60,006
Short-term investments:			
Fixed rate	1.81%	$121,000	$121,097

Our short-term investments generally mature between three months and two years.

Foreign Currency Exchange Rate Risk

We transact business in many different foreign currencies and may be exposed to financial market risk resulting from fluctuations in foreign currency exchange rates, particularly GBP and EUR. The volatility of GBP and EUR (and all other applicable currencies) will be monitored frequently throughout the coming year. When appropriate, we enter into hedging transactions in order to mitigate our risk from foreign currency fluctuations. We will continue to use hedging programs in the future and may use currency forward contracts, currency options and/or other derivative financial instruments commonly utilized to reduce financial market risks if it is determined that such hedging activities are appropriate to reduce risk. We do not hold or purchase any foreign currency contracts for trading purposes. As of March 31, 2004, we had no outstanding hedging contracts.

Market Price Risk

With regard to the structured stock repurchase transactions described in Note 16 in the Notes to the Consolidated Financial Statements, at those times when we have structured stock repurchase transactions outstanding, it is possible that at settlement we could take delivery of shares at an effective repurchase price higher than the then market price. As of March 31, 2004, we had no structured stock repurchase transactions outstanding.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
of Activision, Inc.:

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Activision, Inc. and its subsidiaries at March 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2004 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Los Angeles, California
June 8, 2004

Consolidated Balance Sheets

(In thousands, except share data)

March 31,	2004	2003
Assets		
Current assets:		
Cash and cash equivalents	$ 466,552	$ 285,554
Short-term investments	121,097	121,400
Accounts receivable, net of allowances of $47,028 and $57,356 at March 31, 2004 and 2003, respectively	62,577	15,822
Inventories	26,427	19,577
Software development	58,320	26,791
Intellectual property licenses	32,115	8,906
Deferred income taxes	26,127	38,290
Other current assets	18,660	10,565
Total current assets	811,875	526,905
Software development	28,386	35,281
Intellectual property licenses	16,380	36,943
Property and equipment, net	25,539	22,265
Deferred income taxes	9,064	10,322
Other assets	1,080	5,081
Goodwill	76,493	68,019
Total assets	$ 968,817	$ 704,816
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt	$ —	$ 147
Accounts payable	72,874	45,602
Accrued expenses	63,205	58,656
Total current liabilities	136,079	104,405
Long-term debt, less current portion	—	2,671
Total liabilities	136,079	107,076
Commitments and contingencies (Note 14)		
Shareholders' equity:		
Preferred stock, $.000001 par value, 3,750,000 shares authorized, no shares issued at March 31, 2004 and 2003	—	—
Series A Junior Preferred stock, $.000001 par value, 1,250,000 shares authorized, no shares issued at March 31, 2004 and 2003	—	—
Common stock, $.000001 par value, 225,000,000 and 125,000,000 shares authorized, 166,876,567 and 161,059,091 shares issued and 137,331,242 and 135,126,368 shares outstanding at March 31, 2004 and 2003, respectively	—	—
Additional paid-in capital	758,626	592,295
Retained earnings	208,279	130,564
Less: Treasury stock, at cost, 29,545,325 and 25,932,723 shares as of March 31, 2004 and 2003, respectively	(144,128)	(121,685)
Accumulated other comprehensive income (loss)	9,961	(3,434)
Total shareholders' equity	832,738	597,740
Total liabilities and shareholders' equity	$ 968,817	$ 704,816

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Operations

(In thousands, except per share data)

For the years ended March 31,	2004	2003	2002
Net revenues	$947,656	$864,116	$786,434
Costs and expenses:			
Cost of sales—product costs	475,541	440,977	435,725
Cost of sales—software royalties and amortization	59,744	79,194	58,892
Cost of sales—intellectual property licenses	31,862	45,002	40,114
Product development	97,859	56,971	40,960
Sales and marketing	128,221	100,646	86,161
General and administrative	44,612	46,479	44,008
Total costs and expenses	837,839	769,269	705,860
Income from operations	109,817	94,847	80,574
Investment income, net	6,175	8,560	2,546
Income before income tax provision	115,992	103,407	83,120
Income tax provision	38,277	37,227	30,882
Net income	$ 77,715	$ 66,180	$ 52,238
Basic earnings per share	$ 0.58	$ 0.46	$ 0.46
Weighted average common shares outstanding	133,249	144,359	113,966
Diluted earnings per share	$ 0.54	$ 0.43	$ 0.39
Weighted average common shares outstanding—assuming dilution	144,893	155,483	133,775

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity

(In thousands) For the years ended March 31, 2004, 2003 and 2002	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Treasury Stock Shares	Treasury Stock Amount	Accumulated Other Comprehensive Income (Loss)	Shareholders' Equity
Balance, March 31, 2001	101,813	$—	$ 200,786	$ 12,146	(9,734)	$ (20,249)	$(11,377)	$ 181,306
Components of comprehensive income:								
Net income for the year	—	—	—	52,238	—	—	—	52,238
Foreign currency translation adjustment	—	—	—	—	—	—	(121)	(121)
Total comprehensive income								52,117
Issuance of common stock pursuant to warrants and common stock warrants	2,332	—	1,044	—	—	—	—	1,044
Issuance of common stock and common stock options to employees	19,740	—	63,053	—	—	—	—	63,053
Tax benefit attributable to employee stock options and common stock warrants	—	—	48,513	—	—	—	—	48,513
Issuance of common stock pursuant to conversion of convertible subordinated notes	10,716	—	58,651	—	—	—	—	58,651
Issuance of common stock to effect business combinations	2,726	—	25,481	—	—	—	—	25,481
Purchase of treasury shares	—	—	—	—	(6)	(74)	—	(74)
Balance, March 31, 2002	137,327	—	397,528	64,384	(9,740)	(20,323)	(11,498)	430,091
Components of comprehensive income:								
Net income for the year	—	—	—	66,180	—	—	—	66,180
Unrealized appreciation on short-term investments	—	—	—	—	—	—	134	134
Foreign currency translation adjustment	—	—	—	—	—	—	7,930	7,930
Total comprehensive income								74,244
Issuance of common stock pursuant to underwritten public offering	16,875	—	247,291	—	—	—	—	247,291
Issuance of common stock to employees	5,999	—	20,547	—	—	—	—	20,547
Issuance of common stock pursuant to warrants and common stock warrants	69	—	2,184	—	—	—	—	2,184
Tax benefit attributable to employee stock options and common stock warrants	—	—	23,884	—	—	—	—	23,884
Purchase of structured stock repurchase transactions	—	—	(110,000)	—	—	—	—	(110,000)
Issuance of common stock to effect business combinations	790	—	10,861	—	—	—	—	10,861
Purchase of treasury shares	—	—	—	—	(16,192)	(101,362)	—	(101,362)
Balance, March 31, 2003	161,060	—	592,295	130,564	(25,932)	(121,685)	(3,434)	597,740
Components of comprehensive income:								
Net income for the year	—	—	—	77,715	—	—	—	77,715
Unrealized depreciation on short-term investments	—	—	—	—	—	—	(37)	(37)
Foreign currency translation adjustment	—	—	—	—	—	—	13,432	13,432
Total comprehensive income								91,110
Issuance of common stock to employees	5,140	—	25,730	—	—	—	—	25,730
Issuance of common stock pursuant to warrants and common stock warrants	419	—	1,038	—	—	—	—	1,038
Tax benefit attributable to employee stock options and common stock warrants	—	—	12,417	—	—	—	—	12,417
Structured stock repurchase transactions	—	—	(52,621)	—	—	—	—	(52,621)
Settlement of structured stock repurchase transactions	—	—	176,521	—	(1,716)	(10,000)	—	166,521
Issuance of common stock to effect business combinations	258	—	3,246	—	—	—	—	3,246
Purchase of treasury shares	—	—	—	—	(1,898)	(12,443)	—	(12,443)
Balance, March 31, 2004	166,877	$—	$ 758,626	$208,279	(29,546)	$(144,128)	$ 9,961	$ 832,738

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Cash Flows

(In thousands)

For the years ended March 31,	2004	2003	2002
Cash flows from operating activities:			
Net income	$ 77,715	$ 66,180	$ 52,238
Adjustments to reconcile net income to net cash provided by operating activities:			
Deferred income taxes	15,147	3,355	(23,352)
Depreciation and amortization	10,774	11,880	7,350
Amortization and write-offs of capitalized software development costs and intellectual property licenses	87,922	100,415	62,456
Tax benefit of stock options and warrants exercised	12,417	23,884	48,513
Change in operating assets and liabilities (net of effects of acquisitions):			
Accounts receivable	(42,497)	61,922	(2,010)
Inventories	(6,850)	1,159	23,152
Software development and intellectual property licenses	(115,202)	(151,594)	(76,993)
Other assets	(5,232)	1,836	(1,753)
Accounts payable	23,005	(19,072)	3,357
Accrued expenses and other liabilities	10,204	(8,990)	18,834
Net cash provided by operating activities	67,403	90,975	111,792
Cash flows from investing activities:			
Cash used in business acquisitions (net of cash acquired)	(3,480)	(21,199)	—
Capital expenditures	(11,976)	(11,877)	(9,150)
Purchase of short-term investments	(195,587)	(408,175)	—
Proceeds from sales and maturities of short-term investments	195,874	287,145	—
Other	—	(995)	449
Net cash used in investing activities	(15,169)	(155,101)	(8,701)
Cash flows from financing activities:			
Proceeds from issuance of common stock to employees	26,483	20,547	59,836
Proceeds from issuance of common stock pursuant to warrants	—	—	1,044
Payment on term loan	—	—	(8,550)
Notes payable, net	(2,818)	(720)	(1,792)
Redemption of convertible subordinated notes	—	—	(62)
Proceeds from issuance of common stock pursuant to underwritten public offering, net of offering costs	—	248,072	—
Purchase of structured stock repurchase transactions	(52,621)	(110,000)	—
Settlement of structured stock repurchase transactions	166,521	—	—
Purchase of treasury stock	(19,996)	(93,809)	(74)
Net cash provided by financing activities	117,569	64,090	50,402
Effect of exchange rate changes on cash	11,195	6,583	(36)
Net increase in cash and cash equivalents	180,998	6,547	153,457
Cash and cash equivalents at beginning of period	285,554	279,007	125,550
Cash and cash equivalents at end of period	$ 466,552	$ 285,554	$279,007

The accompanying notes are an integral part of these consolidated financial statements.

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

Business

Activision, Inc. ("Activision" or "we") is a leading international publisher of interactive entertainment software products. We have built a company with a diverse portfolio of products that spans a wide range of categories and target markets and that is used on a variety of game hardware platforms and operating systems. We have created, licensed and acquired a group of highly recognizable brands, which we market to a variety of consumer demographics.

Our products cover game categories such as action/adventure, action sports, racing, role-playing, simulation, first-person action and strategy. Our target customer base ranges from game enthusiasts and children to mass-market consumers and "value" buyers. We currently offer our products primarily in versions that operate on the Sony PlayStation 2 ("PS2"), Nintendo GameCube ("GameCube") and Microsoft Xbox ("Xbox") console systems, Nintendo Game Boy Advance ("GBA") hand-held device and the personal computer ("PC"). In prior years, we have also offered our products on the Sony PlayStation ("PS1") and Nintendo 64 ("N64") console systems and Nintendo Game Boy Color ("GBC") hand-held device. In addition, Sony announced that it would be entering the hand-held hardware market with the introduction of its hand-held gaming device, PlayStation Portable ("PSP"). Nintendo also announced that it plans to launch a new dual-screened, portable game system Nintendo Dual Screen ("NDS"). We are currently developing titles for the PSP and NDS. We are also planning to develop titles for the next-generation console systems expected to be developed by Sony, Microsoft and Nintendo for release in the next two to three years.

Our publishing business involves the development, marketing and sale of products directly, by license or through our affiliate label program with certain third-party publishers. Our distribution business consists of operations in Europe that provide logistical and sales services to third-party publishers of interactive entertainment software, our own publishing operations and manufacturers of interactive entertainment hardware.

We maintain operations in the United States, Canada, the United Kingdom ("UK"), Germany, France, Italy, Japan, Australia, Sweden and the Netherlands. In fiscal year 2004, international operations contributed approximately 53% of net revenues.

Principles of Consolidation

The consolidated financial statements include the accounts of Activision, Inc., a Delaware corporation, and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

Cash, Cash Equivalents and Short-term Investments

Cash and cash equivalents include cash, money markets and short-term investments with original maturities of not more than 90 days.

Short-term investments generally mature between three months and two years. Investments with maturities beyond one year may be classified as short-term based on their liquid nature and because such securities represent the investment of cash that is available for current operations. All of our short-term investments are classified as available-for-sale and are carried at fair market value with unrealized appreciation (depreciation) reported as a component of accumulated other comprehensive income (loss) in shareholders' equity. The specific identification method is used to determine the cost of securities disposed with realized gains and losses reflected in investment income, net.

Concentration of Credit Risk

Financial instruments which potentially subject us to concentration of credit risk consist principally of temporary cash investments and accounts receivable. We place our temporary cash investments with financial institutions. At various times during the fiscal years ended March 31, 2004 and 2003, we had deposits in excess of the Federal Deposit Insurance Corporation ("FDIC") limit at these financial institutions.

Notes to Consolidated Financial Statements

Our customer base includes retail outlets and distributors, including mass-market retailers, consumer electronics stores, discount warehouses and game specialty stores in the United States and countries worldwide. We perform ongoing credit evaluations of our customers and maintain allowances for potential credit losses. We generally do not require collateral or other security from our customers. As of and for the years ended March 31, 2004, 2003 and 2002, we had one customer that accounted for 20%, 16% and 14%, respectively, of consolidated net revenues and 39%, 46% and 22%, respectively, of consolidated accounts receivable, net. This customer was the same customer in all periods and was a customer of both our publishing and distribution businesses.

Financial Instruments

The estimated fair values of financial instruments have been determined using available market information and valuation methodologies described below. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates presented herein may not be indicative of the amounts that we could realize in a current market exchange. The use of different market assumptions or valuation methodologies may have a material effect on the estimated fair value amounts.

The carrying amounts of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses approximate fair value due to their short-term nature. Short-term investments are carried at fair value with fair values being estimated based on quoted market prices.

We account for derivative instruments in accordance with Statement of Financial Accounting Standard ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities, an amendment of SFAS 133" and SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." SFAS Nos. 133, 138 and 149 require that all derivatives, including foreign exchange contracts, be recognized in the balance sheet in other current assets or accrued expenses at their fair value.

We utilize forward contracts in order to reduce financial market risks. These instruments are used to hedge foreign currency exposures of underlying assets, liabilities, or certain forecasted foreign currency denominated transactions. Our accounting policies for these instruments are based on whether they meet the criteria for designation as hedging transactions. Changes in fair value of derivatives that are designated as cash flow hedges, are highly effective, and qualify as hedging instruments, are recorded in other comprehensive income until the underlying hedged item is recognized in earnings within the financial statement line item consistent with the hedged item. Any ineffective portion of a derivative change in fair value is immediately recognized in earnings. Changes in fair value of derivatives that do not qualify as hedging instruments are recorded in earnings. The fair value of foreign currency contracts is estimated based on the spot rate of the various hedged currencies as of the end of the period. As of March 31, 2004 and 2003, we had no outstanding foreign exchange forward contracts.

Equity Investments

From time to time, we may make a capital investment and hold a minority interest in a third-party developer in connection with entertainment software products to be developed by such developer for us. We account for those capital investments over which we have the ability to exercise significant influence using the equity method. For those investments over which we do not have the ability to exercise significant influence, we account for our investment using the cost method.

Software Development Costs

Software development costs include payments made to independent software developers under development agreements, as well as direct costs incurred for internally developed products.

We account for software development costs in accordance with SFAS No. 86, "Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed." Software development costs are capitalized once technological feasibility of a product is established and such costs are determined to be recoverable. Technological feasibility of a product encompasses both technical design documentation and game design documentation. For products where proven technology exists, this may occur early in the development cycle. Technological feasibility is evaluated on a product-by-product basis. Prior to a product's release, we expense, as part of cost of sales—software royalties and amortization, capitalized costs when we believe such amounts are not recoverable. Capitalized costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation. Amounts related to software development which are not capitalized are charged immediately to product development expense. We evaluate the future recoverability of capitalized amounts on a quarterly basis. The recoverability of capitalized software development costs is evaluated based on the expected performance of the specific products for which the costs relate. Criteria used to evaluate expected product performance include: historical performance of comparable products using comparable technology; orders for the product prior to its release; and estimated performance of a sequel product based on the performance of the product on which the sequel is based.

Commencing upon product release, capitalized software development costs are amortized to cost of sales—software royalties and amortization based on the ratio of current revenues to total projected revenues, generally resulting in an amortization period of six months or less. For products that have been released in prior periods, we evaluate the future recoverability of capitalized amounts on a quarterly basis. The primary evaluation criterion is actual title performance.

Significant management judgments and estimates are utilized in the assessment of when technological feasibility is established, as well as in the ongoing assessment of the recoverability of capitalized costs. In evaluating the recoverability of capitalized costs, the assessment of expected product performance utilizes forecasted sales amounts and estimates of additional development costs to be incurred. If revised forecasted or actual product sales are less than and/or revised forecasted or actual costs are greater than the original forecasted amounts utilized in the initial recoverability analysis, the actual impairment charge may be larger than originally estimated in any given quarter.

Intellectual Property Licenses

Intellectual property license costs represent license fees paid to intellectual property rights holders for use of their trademarks, copyrights, software, technology or other intellectual property or proprietary rights in the development of our products. Depending upon the agreement with the rights holder, we may obtain the rights to use acquired intellectual property in multiple products over multiple years, or alternatively, for a single product.

We evaluate the future recoverability of capitalized intellectual property licenses on a quarterly basis. The recoverability of capitalized intellectual property license costs is evaluated based on the expected performance of the specific products in which the licensed trademark or copyright is to be used. As many of our intellectual property licenses extend for multiple products over multiple years, we also assess the recoverability of capitalized intellectual property license costs based on certain qualitative factors such as the success of other products and/or entertainment vehicles utilizing the intellectual property, whether there are any future planned theatrical releases or television series based on the intellectual property and the rights holder's continued promotion and exploitation of the intellectual property. Prior to the related product's release, we expense, as part of cost of sales—intellectual property licenses, capitalized intellectual property costs when we believe such amounts are not recoverable. Capitalized intellectual property costs for those products that are cancelled or abandoned are charged to product development expense in the period of cancellation. Criteria used to evaluate expected product performance include: historical performance of comparable products using comparable technology; orders for the product prior to its release; and estimated performance of a sequel product based on the performance of the product on which the sequel is based.

Notes to Consolidated Financial Statements

Commencing upon the related product's release, capitalized intellectual property license costs are amortized to cost of sales—intellectual property licenses based on the ratio of current revenues for the specific product to total projected revenues for all products in which the licensed property will be utilized. As intellectual property license contracts may extend for multiple years, the amortization of capitalized intellectual property license costs relating to such contracts may extend beyond one year. For intellectual property included in products that have been released, we evaluate the future recoverability of capitalized amounts on a quarterly basis. The primary evaluation criterion is actual title performance.

Significant management judgments and estimates are utilized in the assessment of the recoverability of capitalized costs. In evaluating the recoverability of capitalized costs, the assessment of expected product performance utilizes forecasted sales amounts and estimates of additional development costs to be incurred. If revised forecasted or actual product sales are less than and/or revised forecasted or actual costs are greater than the original forecasted amounts utilized in the initial recoverability analysis, the actual impairment charge may be larger than originally estimated in any given quarter. Additionally, as noted above, as many of our intellectual property licenses extend for multiple products over multiple years, we also assess the recoverability of capitalized intellectual property license costs based on certain qualitative factors such as the success of other products and/or entertainment vehicles utilizing the intellectual property, whether there are any future planned theatrical releases or television series based on the intellectual property and the rights holder's continued promotion and exploitation of the intellectual property. Material differences may result in the amount and timing of charges for any period if management makes different judgments or utilizes different estimates in evaluating these qualitative factors.

Inventories
Inventories are valued at the lower of cost (first-in, first-out) or market.

Property and Equipment
Property and equipment are recorded at cost. Depreciation and amortization are provided using the straight-line method over the shorter of the estimated useful lives or the lease term: buildings, 25 to 33 years; computer equipment, office furniture and other equipment, 2 to 5 years; leasehold improvements, through the life of the lease. When assets are retired or disposed of, the cost and accumulated depreciation thereon are removed and any resultant gains or losses are recognized in current operations.

Goodwill
We account for goodwill using the provisions of SFAS No. 142, "Goodwill and Other Intangibles." SFAS No. 142 addresses financial accounting and reporting requirements for acquired goodwill and other intangible assets. Under SFAS No. 142, goodwill is deemed to have an indefinite useful life and should not be amortized but rather tested at least annually for impairment. An impairment loss should be recognized if the carrying amount of goodwill is not recoverable and its carrying amount exceeds its fair value. In accordance with SFAS No. 142, we have not amortized goodwill during the years ended March 31, 2004, 2003 and 2002.

Revenue Recognition
We recognize revenue from the sale of our products upon the transfer of title and risk of loss to our customers. Revenue from product sales is recognized after deducting the estimated allowance for returns and price protection. With respect to license agreements that provide customers the right to make multiple copies in exchange for guaranteed amounts, revenue is recognized upon delivery of such copies. Per copy royalties on sales that exceed the guarantee are recognized as earned. In addition, in order to recognize revenue for both product sales and licensing transactions, persuasive evidence of an arrangement must exist and collection of the related receivable must be probable. Revenue recognition also determines the timing of certain expenses, including cost of sales—intellectual property licenses and cost of sales—software royalties and amortization.

Sales incentives or other consideration given by us to our customers is accounted for in accordance with the Financial Accounting Standards Board's Emerging Issues Task Force ("EITF") Issue 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." In accordance with EITF Issue 01-9, sales incentives and other consideration that are considered adjustments of the selling price of our products, such as rebates and product placement fees, are reflected as reductions of revenue. Sales incentives and other consideration that represent costs incurred by us for assets or services received, such as the appearance of our products in a customer's national circular ad, are reflected as sales and marketing expenses.

Allowance for Returns and Price Protection

In determining the appropriate unit shipments to our customers, we benchmark our titles using historical and industry data. We closely monitor and analyze the historical performance of our various titles, the performance of products released by other publishers and the anticipated timing of other releases in order to assess future demands of current and upcoming titles. Initial volumes shipped upon title launch and subsequent reorders are evaluated to ensure that quantities are sufficient to meet the demands from the retail markets but at the same time, are controlled to prevent excess inventory in the channel.

We may permit product returns from, or grant price protection to, our customers under certain conditions. In general, price protection refers to the circumstances when we elect to decrease the wholesale price of a product by a certain amount and, when granted and applicable, allows customers a credit against amounts owed by such customers to Activision with respect to open and/or future invoices. The conditions our customers must meet to be granted the right to return products or price protection are, among other things, compliance with applicable payment terms, delivery to us of weekly inventory and sell-through reports, and consistent participation in the launches of our premium title releases. We may also consider other factors, including the facilitation of slow-moving inventory and other market factors. Management must make estimates of potential future product returns and price protection related to current period product revenue. We estimate the amount of future returns and price protection for current period product revenue utilizing historical experience and information regarding inventory levels and the demand and acceptance of our products by the end consumer. The following factors are used to estimate the amount of future returns and price protection for a particular title: historical performance of titles in similar genres, historical performance of the hardware platform, historical performance of the brand, console hardware life cycle, Activision sales force and retail customer feedback, industry pricing, weeks of on-hand retail channel inventory, absolute quantity of on-hand retail channel inventory, Activision warehouse on-hand inventory levels, the title's recent sell-through history (if available), marketing trade programs and competing titles. The relative importance of these factors varies among titles depending upon, among other items, genre, platform, seasonality and sales strategy. Significant management judgments and estimates must be made and used in connection with establishing the allowance for returns and price protection in any accounting period. Historically, total actual returns and price protection have not exceeded our allowance estimates. However, actual returns and price protection could vary materially from our allowance estimates due to a number of reasons including, among others, a lack of consumer acceptance of a title, the release in the same period of a similarly themed title by a competitor, or technological obsolescence due to the emergence of new hardware platforms. Material differences may result in the amount and timing of our revenue for any period if management makes different judgments or utilizes different estimates in determining the allowances for returns and price protection.

Shipping and Handling

Shipping and handling costs, which consist primarily of packaging and transportation charges incurred to move finished goods to customers, are included in cost of sales—product costs.

Notes to Consolidated Financial Statements

Advertising Expenses

We expense advertising as incurred, except for production costs associated with media advertising which are deferred and charged to expense the first time the related ad is run. Advertising expenses for the years ended March 31, 2004, 2003 and 2002 were approximately $76.6 million, $60.0 million and $50.3 million, respectively, and are included in sales and marketing expense in the consolidated statements of operations.

Investment Income, Net

Investment income, net is comprised of the following, (amounts in thousands):

Year ended March 31,	2004	2003	2002
Interest expense	$ (348)	$ (933)	$(1,188)
Interest income	6,502	9,259	3,734
Net realized gain on short-term investments	21	234	—
Investment income, net	$6,175	$8,560	$ 2,546

Income Taxes

We account for income taxes using SFAS No. 109, "Accounting for Income Taxes." Under SFAS No. 109, income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Foreign Currency Translation

The functional currencies of our foreign subsidiaries are their local currencies. All assets and liabilities of our foreign subsidiaries are translated into U.S. dollars at the exchange rate in effect at the end of the period, and revenue and expenses are translated at weighted average exchange rates during the period. The resulting translation adjustments are reflected as a component of accumulated other comprehensive income (loss) in shareholders' equity.

Comprehensive Income

Comprehensive income includes net income, unrealized appreciation (depreciation) on short-term investments, foreign currency translation adjustments, and the effective portion of gains or losses on cash flow hedges that are presented as a component of accumulated other comprehensive income (loss) in shareholders' equity.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities or the disclosure of gain or loss contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Earnings Per Common Share

Basic earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for all periods. Diluted earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding, increased by common stock equivalents. Common stock equivalents are calculated using the treasury stock method and represent incremental shares issuable upon exercise of our outstanding options and warrants and, if applicable in the period, conversion of our convertible debt. However, potential common shares are not included in the denominator of the diluted earnings per share calculation when inclusion of such shares would be anti-dilutive, such as in a period in which a net loss is recorded.

Stock-Based Compensation and Pro Forma Information

Under SFAS No. 123, "Accounting for Stock-Based Compensation," compensation expense is recorded for the issuance of stock options and other stock-based compensation based on the fair value of the stock options and other stock-based compensation on the date of grant or measurement date. Alternatively, SFAS No. 123 allows companies to continue to account for the issuance of stock options and other stock-based compensation in accordance with Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees." Under APB No. 25, compensation expense is recorded for the issuance of stock options and other stock-based compensation based on the intrinsic value of the stock options and other stock-based compensation on the date of grant or measurement date. Under the intrinsic value method, compensation expense is recorded on the date of grant or measurement date only if the current market price of the underlying stock exceeds the stock option or other stock-based compensation exercise price. At March 31, 2004, we had several stock-based employee compensation plans, which are described more fully in Note 15. We account for those plans under the recognition and measurement principles of APB Opinion No. 25 and related Interpretations. The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation (amounts in thousands, except per share data):

Year ended March 31,	2004	2003	2002
Net income, as reported	$ 77,715	$ 66,180	$ 52,238
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	192	—	—
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(18,303)	(21,004)	(12,622)
Pro forma net income	$ 59,604	$ 45,176	$ 39,616
Earnings per share			
Basic—as reported	$ 0.58	$ 0.46	$ 0.46
Basic—pro forma	$ 0.45	$ 0.31	$ 0.35
Diluted—as reported	$ 0.54	$ 0.43	$ 0.39
Diluted—pro forma	$ 0.41	$ 0.29	$ 0.30

The fair value of options granted in the years ended March 31, 2004, 2003 and 2002 has been estimated at the date of grant using a Black-Scholes option-pricing model with the following weighted average assumptions:

	Employee and Director Options and Warrants			Employee Stock Purchase Plan		
	2004	2003	2002	2004	2003	2002
Expected life (in years)	4	3	2	0.5	0.5	0.5
Risk-free interest rate	2.01%	1.51%	3.24%	1.75%	1.13%	2.16%
Volatility	49%	69%	70%	51%	69%	70%
Dividend yield	—	—	—	—	—	—

The Black-Scholes option-pricing model requires the input of highly subjective assumptions, including the expected stock price volatility. We use the historical stock price volatility of our common stock over the most recent period that is generally commensurate with the expected option life as the basis for estimating expected stock price volatility. In prior fiscal years, the historical stock price volatility used was based on the daily, low stock price of our common stock, which, in recent years, resulted in an expected volatility ranging from approximately 65% to 70%. For options granted during

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each of the quarters in the year ended March 31, 2004, the historical stock price volatility used was based on a weekly stock price observation, using an average of the high and low stock prices of our common stock, which resulted in an expected stock price volatility ranging from 47% to 52%. Management believes such amounts are more representative of prospective trends. For purposes of the above pro forma disclosure, the fair value of options granted is amortized to stock-based employee compensation cost over the period(s) in which the related employee services are rendered. Accordingly, the pro forma stock-based compensation cost for any period will typically relate to options granted in both the current period and prior periods.

For options granted during fiscal 2004, 2003 and 2002, the per share weighted average fair value of options with exercise prices equal to market value on the date of grant was $2.77, $4.37 and $3.05, respectively. The per share weighted average estimated fair value of Employee Stock Purchase Plan shares granted during the years ended March 31, 2004, 2003 and 2002 was $1.50, $2.17 and $1.96, respectively.

The effects on pro forma disclosures of applying SFAS No. 123 are not likely to be representative of the effects on pro forma disclosures of future years.

Common stock warrants are granted to non-employees in connection with the development of software and acquisition of licensing rights for intellectual property. In accordance with EITF No. 96-18, "Accounting for Equity Instruments that are Issued to Other Than Employees for Acquiring or in Connection With Selling Goods or Services," the fair value of common stock warrants granted is determined as of the measurement date and is capitalized, expensed and amortized consistent with our policies relating to software development and intellectual property license costs.

Related Parties

In August 2001, we elected to our Board of Directors an individual who is a partner in a law firm that has provided legal services to Activision for more than 10 years. For the years ended March 31, 2004, 2003 and 2002, the fees we paid to the law firm account for less than 1% of the firm's total revenues. We believe that the fees charged to us by the law firm are competitive with the fees charged by other law firms.

Reclassifications

Certain amounts in the consolidated financial statements have been reclassified to conform with the current year's presentation. These reclassifications had no effect on net income, shareholders' equity or net increase in cash and cash equivalents.

2. Stock Splits

In April 2003, the Board of Directors approved a three-for-two split of our outstanding common shares effected in the form of a 50% stock dividend. The split was paid on June 6, 2003 to shareholders of record as of May 16, 2003. In February 2004, the Board of Directors approved a second three-for-two split of our outstanding common shares effected in the form of a 50% stock dividend. The split was paid on March 15, 2004 to shareholders of record as of February 23, 2004. The par value of our common stock was maintained at the pre-split amount of $.000001. The consolidated financial statements and Notes thereto, including all share and per share data, have been restated as if the stock splits had occurred as of the earliest period presented.

3. Acquisitions

During the three years ended March 31, 2004, we separately completed the acquisition of six privately held interactive software development companies. We accounted for these acquisitions in accordance with SFAS No. 141, "Business Combinations." SFAS No. 141 addresses financial accounting and reporting for business combinations, requiring that the purchase method be used to account and report for all business combinations. These acquisitions have further enabled us to implement our multi-platform development strategy by bolstering our internal product development capabilities for console systems and personal computers and strengthening our position in the first-person action, action and action sports game categories. A significant portion of the purchase price for all of these acquisitions was assigned to goodwill as the primary asset we acquired in each of the transactions was an assembled workforce with proven technical and design talent with a history of high quality product creation. Pro forma consolidated statements of operations for these acquisitions are not shown, as they would not differ materially from reported results.

Fiscal 2004 Transactions

Acquisition of Infinity Ward. In May 2002, we acquired a 30% interest in the outstanding capital stock of Infinity Ward, Inc. ("Infinity Ward"), a privately held interactive software development company, as well as an option to purchase the remaining 70% of outstanding capital stock. In October 2003, we exercised our option to acquire the remaining 70% of the outstanding capital stock of Infinity Ward for cash of approximately $3.5 million. Goodwill of approximately $3.8 million has been included in the publishing segment of our business and is non-deductible for tax purposes. The results of operations of Infinity Ward are included in our consolidated statement of operations beginning October 24, 2003.

Fiscal 2003 Transactions

Acquisition of Luxoflux. Effective October 4, 2002, we acquired all of the outstanding ownership interests of Luxoflux, Inc. ("Luxoflux"), a privately held interactive software development company, in exchange for $9.0 million in cash. Luxoflux is an experienced, multi-platform, console software developer. In accordance with the original acquisition agreement, approximately 248,000 shares of our common stock may be issued to Luxoflux's equity holders over the course of several years, depending on the satisfaction of certain product performance requirements and other criteria. This contingent consideration will be recorded as an additional element of the purchase price for Luxoflux when those contingencies are resolved.

In the fourth quarter of fiscal 2004, certain of these product performance requirements were met and approximately 166,000 of our common shares with an assigned value of approximately $2.0 million were issued to Luxoflux equity holders. The purchase price of the transaction, including acquisition costs and the contingent consideration issued in the fourth quarter of fiscal 2004, was approximately $11.0 million and has been allocated to assets acquired and liabilities assumed as follows (amounts in thousands):

Current assets	$ 1,461
Property and equipment	83
Other assets	15
Goodwill	12,360
Current liabilities	(2,892)
	$11,027

Acquisition of Z-Axis

Effective May 20, 2002, we acquired all of the outstanding ownership interests of Z-Axis, Ltd. ("Z-Axis"), a privately held interactive software development company, in exchange for $12.5 million in cash and 560,678 shares of our common stock valued at approximately $8.2 million. Z-Axis is an experienced, multi-platform, console software developer. In accordance with the original acquisition agreement, approximately 210,000 additional shares of our common stock may be issued to Z-Axis' equity holders over the course of several years, depending on the satisfaction of certain product performance requirements and other criteria. This contingent consideration will be recorded as an additional element of the purchase price for Z-Axis when those contingencies are resolved.

Notes to Consolidated Financial Statements

In the fourth quarter of fiscal 2004, certain of these product performance requirements were met and approximately 70,000 of our common shares with an assigned value of approximately $1.0 million were issued to Z-Axis equity holders. The purchase price of the transaction, including acquisition costs and the contingent consideration issued in the fourth quarter of fiscal 2004, was approximately $21.9 million and has been allocated to assets acquired and liabilities assumed as follows (amounts in thousands):

Current assets	$ 1,946
Other intangibles	113
Property and equipment	172
Other assets	20
Goodwill	20,667
Current liabilities	(1,058)
	$21,860

For both of the acquisitions, goodwill has been included in the publishing segment of our business and is non-deductible for tax purposes. The results of operations of Luxoflux and Z-Axis are included in our consolidated statement of operations beginning October 4, 2002 and May 20, 2002, respectively.

Fiscal 2002 Transactions

Acquisition of Shaba. On March 27, 2002, we acquired all of the outstanding ownership interests of Shaba Games, Inc. ("Shaba"), a privately held interactive software development company, in exchange for 581,897 shares of our common stock. Shaba is an experienced, multi-platform console software developer with a focus on action and action sports video games. Under the original acquisition agreement, approximately 155,000 additional shares of our common stock may be issued to Shaba's equity holders over the course of several years, depending on the satisfaction of certain product performance requirements and other criteria. This contingent consideration will be recorded as an additional element of the purchase price for Shaba when those contingencies are resolved.

In the fourth quarter of fiscal 2004, certain of these product performance requirements were met and approximately 23,000 of our common shares with an assigned value of approximately $0.3 million were issued to Shaba equity holders. The purchase price of the transaction, including acquisition costs and the contingent consideration issued in the fourth quarter of fiscal 2004, was approximately $7.6 million with approximately $6.4 million of the purchase price being assigned to goodwill. This goodwill has been included in the publishing segment of our business and is deductible for tax purposes. The results of operations of Shaba are included in our consolidated statement of operations beginning March 27, 2002. As of March 31, 2004, approximately 45,000 shares of our common stock remain in escrow and are contingently issuable in accordance with the original Shaba acquisition agreement.

Acquisition of Gray Matter. On December 30, 1999, we acquired a 40% interest in the outstanding capital stock of Gray Matter Interactive Studios, Inc., formerly known as Video Games West ("Gray Matter"), a privately held software development company, as well as an option to purchase the remaining 60% of outstanding capital stock. Effective January 9, 2002, we exercised our option to acquire the remaining 60% of outstanding capital stock of Gray Matter in exchange for 300,803 shares of our common stock. The purchase price of the transaction, including acquisition costs, was valued at approximately $3.6 million with $3.3 million of the purchase price being assigned to goodwill. This goodwill has been included in the publishing segment of our business and is non-deductible for tax purposes. The results of operations of Gray Matter are included in our consolidated statement of operations beginning January 9, 2002.

Acquisition of Treyarch Effective October 1, 2001, we acquired all of the outstanding ownership interests of Treyarch Invention, LLC ("Treyarch"), a privately held interactive software development company, in exchange for 1,842,663 shares of our common stock. Treyarch is an experienced, multi-platform console software developer with a focus on action and action sports video games. As part of the original acquisition agreement, approximately 540,000 additional shares of our common stock could also be issued to Treyarch's equity holders and employees over the course of several years, depending on the satisfaction of certain product performance requirements and other criteria. This contingent consideration would be recorded as an additional element of the purchase price for Treyarch when those contingencies were resolved. In July 2002, in connection with the satisfaction of certain of those product performance requirements, we issued to Treyarch equity holders and employees 228,680 of our common shares with an assigned value of $2.7 million. The purchase price of the transaction, including the contingent consideration issued in July 2002, forgiveness of a note receivable and acquisition costs, was valued at approximately $18.2 million with approximately $17.2 million of the purchase price being assigned to goodwill. This goodwill has been included in the publishing segment of our business and is non-deductible for tax purposes. The results of operations of Treyarch are included in our consolidated statement of operations beginning October 1, 2001. As of March 31, 2004, all contingencies relating to the issuance of additional shares as consideration have been resolved.

4. Cash, Cash Equivalents, and Short-Term Investments

The following table summarizes our cash, cash equivalents and short-term investments as of March 31, 2004 (amounts in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents:				
Cash and time deposits	$101,414	$ —	$ —	$101,414
Money market funds	60,006	—	—	60,006
Commercial paper	3,700	—	—	3,700
Auction rate notes	301,432	—	—	301,432
Cash and cash equivalents	466,552	—	—	466,552
Short-term investments:				
Corporate bonds	21,047	13	(24)	21,036
U.S. agency issues	71,817	76	(4)	71,889
Asset-backed bonds	23,113	74	(38)	23,149
Municipal bonds	5,023	—	—	5,023
Short-term investments	121,000	163	(66)	121,097
Cash, cash equivalents and short-term investments	$587,552	$163	$(66)	$587,649

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The following table summarizes our cash, cash equivalents and short-term investments as of March 31, 2003 (amounts in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents:				
Cash and time deposits	$ 87,348	$ —	$ —	$ 87,348
Money market funds	35,507	—	—	35,507
Auction rate notes	162,699	—	—	162,699
Cash and cash equivalents	285,554	—	—	285,554
Short-term investments:				
Corporate bonds	16,712	34	—	16,746
Taxable senior debt	2,253	—	—	2,253
U.S. agency issues	52,055	65	(12)	52,108
Asset-backed bonds	39,224	122	(75)	39,271
Municipal bonds	11,022	—	—	11,022
Short-term investments	121,266	221	(87)	121,400
Cash, cash equivalents and short-term investments	$406,820	$221	$(87)	$406,954

The following table summarizes the maturities of our investments in debt securities as of March 31, 2004 (amounts in thousands):

	Amortized Cost	Fair Value
Due in one year or less	$326,694	$326,699
Due after one year through two years	76,325	76,381
	403,019	403,080
Asset-backed securities	23,113	23,149
Total	$426,132	$426,229

For the year ended March 31, 2004, net realized gains on short-term investments consisted of $25,000 of gross realized gains and $4,000 of gross realized losses. For the year ended March 31, 2003, net realized gains on short-term investments consisted of $350,000 of gross realized gains and $116,000 of gross realized losses. As of March 31, 2002, we held no short-term investments and had no gross realized gains or losses for the year then ended.

5. Software Development Costs and Intellectual Property Licenses

As of March 31, 2004, capitalized software development costs included $35.3 million of internally developed software costs and $51.5 million of payments made to third-party software developers. As of March 31, 2003, capitalized software development costs included $26.0 million of internally developed software costs and $36.1 million of payments made to third-party software developers. Capitalized intellectual property licenses were $48.5 million and $45.8 million as of March 31, 2004 and 2003, respectively. Amortization and write-offs of capitalized software development costs and intellectual property licenses, combined, was $87.9 million, $100.4 million and $62.5 million for the years ended March 31, 2004, 2003 and 2002, respectively.

During the three months ended December 31, 2003, we executed a realignment of our product portfolio driven by the evolution of the video game market, which is increasingly dominated by high quality products that are based on recognizable franchises and supported with big marketing programs. We completed a comprehensive review of our product portfolio in which we evaluated each product based on a number of criteria, including: the strength of the franchise, the projected product quality, the potential responsiveness of the product to aggressive marketing support and the financial risk in the event of product failure. As a result of this review, we believe that we have an extensive slate of high-potential properties in development. However, we also found that certain projects had a lower likelihood of achieving acceptable levels of operating performance and that continued pursuit of these projects would create a substantial opportunity cost as it related to our slate of high-potential projects. Accordingly, in the three months ended December 31, 2003, we canceled the development of ten products which we believed were unlikely to produce an acceptable level of return on our investment. In connection with the cancellation of these products, we recorded a pre-tax charge of approximately $21 million which is included in the consolidated statement of operations in product development expense.

For the year ended March 31, 2003, amortization and write-offs of capitalized software development costs and intellectual property licenses included approximately $15.0 million recorded in the fourth quarter as the result of the assessment of the recoverability of capitalized development costs relating to certain projects and certain of our investments in long-term licensing agreements.

6. Inventories

Our inventories consist of the following (amounts in thousands):

March 31,	2004	2003
Purchased parts and components	$ 392	$ 1,129
Finished goods	26,035	18,448
	$ 26,427	$ 19,577

7. Property and Equipment, Net

Property and equipment, net was comprised of the following (amounts in thousands):

March 31,	2004	2003
Land	$ 557	$ 441
Buildings	4,379	5,029
Computer equipment	34,076	31,483
Office furniture and other equipment	13,687	9,724
Leasehold improvements	5,540	4,893
Total cost of property and equipment	58,239	51,570
Less accumulated depreciation	(32,700)	(29,305)
Property and equipment, net	$ 25,539	$ 22,265

Depreciation expense for the years ended March 31, 2004, 2003 and 2002 was $10.0 million, $8.1 million and $6.2 million, respectively.

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8. Goodwill

The changes in the carrying amount of goodwill were as follows (amounts in thousands):

	Publishing	Distribution	Total
Balance as of March 31, 2002	$31,626	$4,366	$35,992
Goodwill acquired during the year	29,348	—	29,348
Issuance of contingent consideration	2,668	—	2,668
Adjustment—prior period purchase allocation	(448)	—	(448)
Effect of foreign currency exchange rates	—	459	459
Balance as of March 31, 2003	63,194	4,825	68,019
Goodwill acquired during the year	3,763	—	3,763
Issuance of contingent consideration	3,246	—	3,246
Adjustment—prior period purchase allocation	695	—	695
Effect of foreign currency exchange rates	—	770	770
Balance as of March 31, 2004	$70,898	$5,595	$76,493

9. Accrued Expenses

Accrued expenses were comprised of the following (amounts in thousands):

March 31,	2004	2003
Accrued royalties payable	$ 7,218	$ 6,430
Accrual for settlement of treasury stock purchases	—	7,553
Accrued selling and marketing costs	11,456	8,737
Income tax payable	9,897	6,940
Accrued bonus and vacation pay	20,042	12,287
Other	14,592	16,709
Total	$63,205	$58,656

10. Operations by Reportable Segments and Geographic Area

Based upon our organizational structure, we operate two business segments: (i) publishing of interactive entertainment software and (ii) distribution of interactive entertainment software and hardware products.

Publishing refers to the development, marketing and sale of products directly, by license or through our affiliate label program with certain third-party publishers. In the United States, we primarily sell our products on a direct basis to mass-market retailers, consumer electronics stores, discount warehouses and game specialty stores. We conduct our international publishing activities through offices in the UK, Germany, France, Italy, Australia, Sweden, Canada and Japan. Our products are sold internationally on a direct-to-retail basis and through third-party distribution and licensing arrangements and through our wholly-owned distribution subsidiaries located in the UK, the Netherlands and Germany.

Distribution refers to our operations in the UK, the Netherlands and Germany that provide logistical and sales services to third-party publishers of interactive entertainment software, our own publishing operations and manufacturers of interactive entertainment hardware.

Resources are allocated to each of these segments using information on their respective net revenues and operating profits before interest and taxes.

The accounting policies of these segments are the same as those described in the Summary of Significant Accounting Policies. Transactions between segments are eliminated in consolidation.

Information on the reportable segments for the three years ended March 31, 2004 is as follows (amounts in thousands):

Year ended March 31, 2004	Publishing	Distribution	Total
Total segment revenues	$665,732	$281,924	$947,656
Revenue from sales between segments	(67,859)	67,859	—
Revenues from external customers	$597,873	$349,783	$947,656
Operating income	$ 93,223	$ 16,594	$109,817
Total assets	$859,874	$108,943	$968,817
Year ended March 31, 2003			
Total segment revenues	$615,975	$248,141	$864,116
Revenue from sales between segments	(57,462)	57,462	—
Revenues from external customers	$558,513	$305,603	$864,116
Operating income	$ 79,139	$ 15,708	$ 94,847
Total assets	$619,132	$ 85,684	$704,816
Year ended March 31, 2002			
Total segment revenues	$549,508	$236,926	$786,434
Revenue from sales between segments	(50,632)	50,632	—
Revenues from external customers	$498,876	$287,558	$786,434
Operating income	$ 68,675	$ 11,899	$ 80,574
Total assets	$455,432	$101,455	$556,887

Geographic information is based on the location of the selling entity. Revenues from external customers by geographic region were as follows (amounts in thousands):

Year ended March 31,	2004	2003	2002
United States	$446,812	$432,261	$404,905
Europe	479,224	413,125	368,799
Other	21,620	18,730	12,730
Total	$947,656	$864,116	$786,434

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Revenues by platform were as follows (amounts in thousands):

Year ended March 31,	2004	2003	2002
Console	$732,220	$674,621	$480,695
Hand-held	43,306	64,069	159,042
PC	172,130	125,426	146,697
Total	$947,656	$864,116	$786,434

A significant portion of our revenues is derived from products based on a relatively small number of popular brands each year. In fiscal 2004, 31% of our consolidated net revenues (44% of worldwide publishing net revenues) was derived from two brands, one of which accounted for 17% and the other of which accounted for 14% of consolidated net revenues (24% and 20%, respectively, of worldwide publishing net revenues). In fiscal 2003, 38% of our consolidated net revenues (52% of worldwide publishing net revenues) was derived from two brands, one of which accounted for 20% and the other of which accounted for 18% of consolidated net revenues (27% and 25%, respectively, of worldwide publishing net revenues). In fiscal 2002, 35% of our consolidated net revenues (50% of worldwide publishing net revenues) was derived from two brands, one of which accounted for 31% and the other of which accounted for 4% of consolidated net revenues (44% and 6%, respectively, of worldwide publishing net revenues).

11. Computation of Earnings Per Share

The following table sets forth the computations of basic and diluted earnings per share (amounts in thousands, except per share data):

Year ended March 31,	2004	2003	2002
Numerator:			
Numerator for basic and diluted earnings per share—income available to common shareholders	$ 77,715	$ 66,180	$ 52,238
Denominator:			
Denominator for basic earnings per share—weighted average common shares outstanding	133,249	144,359	113,966
Effect of dilutive securities:			
Employee stock options and stock purchase plan	11,042	10,278	18,648
Warrants to purchase common stock	602	846	1,161
Potential dilutive common shares	11,644	11,124	19,809
Denominator for diluted earnings per share—weighted average common shares outstanding plus assumed conversions	144,893	155,483	133,775
Basic earnings per share	$ 0.58	$ 0.46	$ 0.46
Diluted earnings per share	$ 0.54	$ 0.43	$ 0.39

Options to purchase approximately 9,471,000, 7,799,000 and 237,000 shares of common stock for the years ended March 31, 2004, 2003 and 2002, respectively, were not included in the calculation of diluted earnings per share because their effect would be antidilutive.

12. Income Taxes

Domestic and foreign income before income taxes and details of the income tax provision are as follows (amounts in thousands):

Year ended March 31,	2004	2003	2002
Income before income taxes:			
Domestic	$ 84,339	$ 78,761	$ 67,553
Foreign	31,653	24,646	15,567
	$115,992	$103,407	$ 83,120
Income tax expense (benefit):			
Current:			
Federal	$ 502	$ 1,703	$ 648
State	311	413	20
Foreign	9,899	7,872	5,053
Total current	10,712	9,988	5,721
Deferred:			
Federal	14,113	1,794	(18,751)
State	(871)	3,065	(4,555)
Foreign	1,906	(1,504)	(46)
Total deferred	15,148	3,355	(23,352)
Add back benefit credited to additional paid-in capital:			
Tax benefit related to stock option and warrant exercises	12,417	23,884	48,513
Income tax provision	$ 38,277	$ 37,227	$ 30,882

The items accounting for the difference between income taxes computed at the U.S. federal statutory income tax rate and the income tax provision for each of the years are as follows:

Year ended March 31,	2004	2003	2002
Federal income tax provision at statutory rate	35.0%	35.0%	35.0%
State taxes, net of federal benefit	2.3	2.4	3.5
Research and development credits	(8.0)	(6.0)	(1.8)
Incremental (decremental) effect of foreign tax rates	(2.3)	(0.2)	(1.4)
Increase of valuation allowance	5.8	2.1	2.4
Rate changes	—	0.8	—
Other	0.2	1.9	(0.5)
	33.0%	36.0%	37.2%

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Deferred income taxes reflect the net tax effects of temporary differences between the amounts of assets and liabilities for accounting purposes and the amounts used for income tax purposes. The components of the net deferred tax asset and liability are as follows (amounts in thousands):

March 31,	2004	2003
Deferred asset:		
Allowance for doubtful accounts	$ 634	$ 1,538
Allowance for sales returns	8,334	10,511
Inventory reserve	385	775
Vacation and bonus reserve	2,771	2,409
Amortization and depreciation	5,036	4,794
Tax credit carryforwards	36,599	25,741
Net operating loss carryforwards	25,851	47,399
Other	2,248	3,946
Deferred asset	81,858	97,113
Valuation allowance	(18,857)	(27,606)
Net deferred asset	63,001	69,507
Deferred liability:		
Capitalized research expenses	25,252	18,775
State taxes	2,558	2,120
Deferred liability	27,810	20,895
Net deferred asset	$ 35,191	$ 48,612

The tax benefits associated with certain net operating loss carryovers relate to employee stock options. Pursuant to SFAS No. 109, net operating losses have been reduced by $12.7 million relating to these items which will be credited to additional paid-in capital when realized.

As of March 31, 2004, our available federal net operating loss carryforward of approximately $62.0 million is subject to certain limitations as defined under Section 382 of the Internal Revenue Code. The net operating loss carryforwards expire between 2020 and 2023. We have various state net operating loss carryforwards which are not subject to limitations under Section 382 of the Internal Revenue Code. We have tax credit carryforwards of $22.8 million and $13.8 million for federal and state purposes, respectively, which begin to expire in 2006.

At March 31, 2004, our deferred income tax asset for tax credit carryforwards and net operating loss carryforwards was reduced by a valuation allowance of $18.9 million as compared to $27.6 million in the prior fiscal year. Realization of the deferred tax assets is dependent upon the continued generation of sufficient taxable income prior to expiration of tax credits and loss carryforwards. Although realization is not assured, management believes it is more likely than not that the net carrying value of the deferred tax asset will be realized.

Cumulative undistributed earnings of foreign subsidiaries for which no deferred taxes have been provided approximated $52.7 million at March 31, 2004. Deferred income taxes on these earnings have not been provided as these amounts are considered to be permanent in duration.

13. Long-Term Debt

Mortgage Notes Payable

As of March 31, 2003, long-term debt and the current portion of long-term debt of $2.8 million were comprised of the mortgage note payable related to the land, office and warehouse facilities of our German subsidiary. The German mortgage note bore interest at 5.45%, was due in bi-annual installments of Euro ("EUR") 73,900 ($89,958), was collateralized by the related assets and was scheduled to mature in December 2018. The German mortgage note was repaid in full in fiscal 2004.

Credit Facilities

We have revolving credit facilities with our Centresoft subsidiary located in the UK (the "UK Facility") and our NBG subsidiary located in Germany (the "German Facility"). The UK Facility provided Centresoft with the ability to borrow up to Great British Pounds ("GBP") 8.0 million ($14.6 million) and GBP 8.6 million ($13.5 million), including issuing letters of credit, on a revolving basis as of March 31, 2004 and 2003, respectively. Furthermore, under the UK Facility, Centresoft provided a GBP 0.3 million ($0.5 million) and a EUR 1.0 million ($1.1 million) guarantee for the benefit of our CD Contact subsidiary as of March 31, 2004 and 2003, respectively. The UK Facility bore interest at LIBOR plus 2.0% and LIBOR plus 1.5% as of March 31, 2004 and 2003, respectively, is collateralized by substantially all of the assets of the subsidiary and expires in November 2004. The UK Facility also contains various covenants that require the subsidiary to maintain specified financial ratios related to, among others, fixed charges. As of March 31, 2004 and 2003, we were in compliance with these covenants. No borrowings were outstanding against the UK Facility as of March 31, 2004 or 2003. The German Facility provided for revolving loans up to EUR 0.5 million ($0.6 million) and EUR 0.8 million ($0.8 million) as of March 31, 2004 and 2003, respectively, bore interest at a Eurocurrency rate plus 2.5%, is collateralized by certain of the subsidiary's property and equipment and has no expiration date. No borrowings were outstanding against the German Facility as of March 31, 2004 or 2003.

Private Placement of Convertible Subordinated Notes

In December 1997, we completed the private placement of $60.0 million principal amount of 6¾% convertible subordinated notes due 2005 (the "Notes"). The Notes were convertible, in whole or in part, at the option of the holder at any time after December 22, 1997 (the date of original issuance) and prior to the close of business on the business day immediately preceding the maturity date, unless previously redeemed or repurchased, into our common stock at a conversion price of $5.593 per share, subject to adjustment in certain circumstances. During the three months ended June 30, 2001, we called for the redemption of the Notes. In connection with that call, holders converted to common stock approximately $58.7 million aggregate principal amount of their Notes, net of conversion costs. The remaining Notes were redeemed for cash.

14. Commitments and Contingencies

Developer and Intellectual Property Contracts

In the normal course of business, we enter into contractual arrangements with third parties for the development of products, as well as for the rights to intellectual property. Under these agreements, we commit to provide specified payments to a developer, or intellectual property holder, based upon contractual arrangements. Typically, the payments to third-party developers are conditioned upon the achievement by the developers of contractually specified development milestones. These payments to third-party developers and intellectual property holders typically are deemed to be

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advances and are recoupable against future royalties earned by the developer or intellectual property holder based on the sale of the related game. Assuming all contractual provisions are met, the total future minimum contract commitment for contracts in place as of March 31, 2004 is approximately $89.3 million, which is scheduled to be paid as follows (amounts in thousands):

Year ended March 31,	
2005	$62,529
2006	17,328
2007	4,545
2008	1,895
2009	3,020
Total	$89,317

The commitment schedule above excludes approximately $9.3 million of commitments originally scheduled to be paid between fiscal 2004 through fiscal 2007 relating to an intellectual property rights agreement with a third party. Effective June 30, 2003, we terminated the agreement and filed a breach of contract suit against the third party.

Marketing Commitments

In connection with certain intellectual property right acquisitions and development agreements, we will commit to spend specified amounts for marketing support for the related game(s) which is to be developed or in which the intellectual property will be utilized. Assuming all contractual provisions are met, the total future minimum marketing commitment for contracts in place as of March 31, 2004 is approximately $66.4 million, which is scheduled to be paid as follows (amounts in thousands):

Year ended March 31,	
2005	$39,919
2006	11,500
2007	15,000
Total	$66,419

Lease Obligations

We lease certain of our facilities under non-cancelable operating lease agreements. Total future minimum lease commitments as of March 31, 2004 are as follows (amounts in thousands):

Year ended March 31,	
2005	$ 8,936
2006	7,520
2007	6,870
2008	4,033
2009	2,993
Thereafter	16,222
Total	$46,574

Facilities rent expense for the years ended March 31, 2004, 2003 and 2002 was approximately $8.7 million, $7.6 million and $5.3 million, respectively.

Legal Proceedings

On March 5, 2004, a class action lawsuit was filed against us and certain of our current and former officers and directors. The complaint, which asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 based on allegations that our revenues and assets were overstated during the period between February 1, 2001 and December 17, 2002, was filed in the United States District Court, Central District of California by the Construction Industry and Carpenters Joint Pension Trust for Southern Nevada purporting to represent a class of purchasers of Activision stock. Five additional purported class actions have subsequently been filed by Gianni Angeloni, Christopher Hinton, Stephen Anish, the Alaska Electrical Pension Fund, and Joseph A. Romans asserting the same claims. Five of the six actions have been transferred to the same court where the first-filed complaint was pending. In addition, on March 12, 2004, a shareholder derivative lawsuit was filed, purportedly on behalf of Activision, which in large measure asserts the identical claims set forth in the federal class action lawsuit. That complaint was filed in Superior Court for the County of Los Angeles. We strongly deny these allegations and will vigorously defend these cases.

On July 11, 2003, we were informed by the staff of the Securities and Exchange Commission that the Securities and Exchange Commission has commenced a non-public formal investigation captioned "In the Matter of Certain Video Game Manufacturers and Distributors." The investigation appears to be focused on certain accounting practices common to the interactive entertainment industry, with specific emphasis on revenue recognition. In connection with this inquiry, the Securities and Exchange Commission submitted to us a request for information. We responded to this inquiry on September 2, 2003. To date, we have not received a request from the Securities and Exchange Commission for any additional information. The Securities and Exchange Commission staff also informed us that other companies in the video game industry received similar requests for information. The Securities and Exchange Commission has advised us that this request for information should not be construed as an indication from the Securities and Exchange Commission or its staff that any violation of the law has occurred, nor should it reflect negatively on any person, entity or security. We have cooperated and intend to continue to cooperate fully with the Securities and Exchange Commission in the conduct of this inquiry.

On June 30, 2003, we terminated our Star Trek Merchandising License Agreement with Viacom Consumer Products, Inc. and filed a complaint in the Superior Court of the State of California for breach of contract and constructive trust against Viacom Consumer Products and Viacom International, Inc. ("Viacom"). On August 15, 2003, Viacom filed its response to our complaint as well as a cross-complaint alleging, among other matters, a breach of contract by Activision and seeking claimed damages in excess of $50 million. We strongly dispute the claims by Viacom, consider the damages alleged by Viacom to be speculative and without merit, and intend to defend vigorously and aggressively against the cross-complaint.

In addition, we are party to other routine claims and suits brought by us and against us in the ordinary course of business, including disputes arising over the ownership of intellectual property rights, contractual claims and collection matters. In the opinion of management, after consultation with legal counsel, the outcome of such routine claims will not have a material adverse effect on our business, financial condition, results of operations or liquidity.

15. Stock Compensation and Employee Benefit Plans

Stock Option Plans

We sponsor several stock option plans for the benefit of officers, employees, consultants and others.

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On September 23, 1998, the shareholders of Activision approved the Activision 1998 Incentive Plan, as amended (the "1998 Plan"). The 1998 Plan permits the granting of "Awards" in the form of non-qualified stock options, ISOs, SARs, restricted stock awards, deferred stock awards and other common stock-based awards to directors, officers, employees, consultants and others. The total number of shares of common stock available for distribution under the 1998 Plan is 10,125,000. The 1998 Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. There were approximately 11,800 shares remaining available for grant under the 1998 Plan as of March 31, 2004.

On April 26, 1999, the Board of Directors approved the Activision 1999 Incentive Plan, as amended (the "1999 Plan"). The 1999 Plan permits the granting of "Awards" in the form of non-qualified stock options, ISOs, SARs, restricted stock awards, deferred share awards and other common stock-based awards to directors, officers, employees, consultants and others. The total number of shares of common stock available for distribution under the 1999 Plan is 16,875,000. The 1999 Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. There were approximately 50,400 shares remaining available for grant under the 1999 Plan as of March 31, 2004.

On August 23, 2001, the shareholders of Activision approved the Activision 2001 Incentive Plan, as amended (the "2001 Plan"). The 2001 Plan permits the granting of "Awards" in the form of non-qualified stock options, ISOs, SARs, restricted stock awards, deferred stock awards and other common stock-based awards to directors, officers, employees, consultants and others. The total number of shares of common stock available for distribution under the 2001 Plan is 5,062,500. The 2001 Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. There were approximately 100,000 shares remaining available for grant under the 2001 Plan as of March 31, 2004.

On April 4, 2002, the Board of Directors approved the Activision 2002 Incentive Plan (the "2002 Plan"). The 2002 Plan permits the granting of "Awards" in the form of non-qualified stock options, ISOs, SARs, restricted stock awards, deferred share awards and other common stock-based awards to officers (other than executive officers), employees, consultants, advisors and others. The 2002 Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. The total number of shares of common stock available for distribution under the 2002 Plan is 9,787,500. There were approximately 2,032,100 shares remaining available for grant under the 2002 Plan as of March 31, 2004.

On September 19, 2002, the shareholders of Activision approved the Activision 2002 Executive Incentive Plan (the "2002 Executive Plan"). The 2002 Executive Plan permits the granting of "Awards" in the form of non-qualified stock options, ISOs, SARs, restricted stock awards, deferred share awards and other common stock-based awards to officers, employees, directors, consultants and advisors. The total number of shares of common stock available for distribution under the 2002 Executive Plan is 5,625,000. The 2002 Executive Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. There were approximately 248,600 shares remaining available for grant under the 2002 Executive Plan as of March 31, 2004.

On December 16, 2002, the Board of Directors approved the Activision 2002 Studio Employee Retention Incentive Plan, as amended (the "2002 Studio Plan"). The 2002 Studio Plan permits the granting of "Awards" in the form of non-qualified stock options and restricted stock awards to key studio employees (other than executive officers) of Activision, our subsidiaries and affiliates and to contractors and others. The 2002 Studio Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. The total number of shares of common stock available for distribution under the 2002 Studio Plan is 3,375,000. There were approximately 62,300 shares remaining available for grant under the 2002 Studio Plan as of March 31, 2004.

On April 29, 2003, our Board of Directors approved the Activision 2003 Incentive Plan (the "2003 Plan"). The 2003 Plan permits the granting of "Awards" in the form of non-qualified stock options, SARs, restricted stock awards, deferred stock awards and other common stock-based awards to directors, officers, employees, consultants and others. The 2003 Plan requires available shares to consist in whole or in part of authorized and unissued shares or treasury shares. The total number of shares of common stock available for distribution under the 2003 Plan is 13,500,000. There were approximately 13,353,800 shares remaining available for grant under the 2003 Plan as of March 31, 2004.

The exercise price for Awards issued under the 1998 Plan, 1999 Plan, 2001 Plan, 2002 Plan, 2002 Executive Plan, 2002 Studio Plan and 2003 Plan (collectively, the "Plans") is determined at the discretion of the Board of Directors (or the Compensation Committee of the Board of Directors, which administers the Plans), and for ISOs, is not to be less than the fair market value of our common stock at the date of grant, or in the case of non-qualified options, must exceed or be equal to 85% of the fair market value of our common stock at the date of grant. Options typically become exercisable in installments over a period not to exceed seven years and must be exercised within 10 years of the date of grant. However, certain options granted to executives vest immediately. Historically, stock options have been granted with exercise prices equal to or greater than the fair market value at the date of grant.

Other Employee Stock Options

In connection with prior employment agreements between Activision and Robert A. Kotick, Activision's Chairman and Chief Executive Officer, and Brian G. Kelly, Activision's Co-Chairman, Mr. Kotick and Mr. Kelly were granted options to purchase common stock. The Board of Directors approved the granting of these options. Relating to such grants, as of March 31, 2004, approximately 7,816,400 shares were outstanding with a weighted average exercise price of $2.81.

We additionally have approximately 209,500 options outstanding to employees as of March 31, 2004, with a weighted average exercise price of $6.19. The Board of Directors approved the granting of these options. Such options have terms similar to those options granted under the Plans.

Director Warrants

During the fiscal year ended March 31, 1997, we issued warrants to purchase 135,000 shares of our common stock, at exercise prices ranging from $3.50 to $4.11 to two of our outside directors in connection with their election to the Board. Such warrants vested 25% on the first anniversary of the date of grant, and 12.5% each six months thereafter and expire within 10 years from the date of grant. Relating to such warrants, as of March 31, 2004, approximately 67,500 shares with a weighted average exercise price of $4.01 were outstanding.

Employee Stock Purchase Plans

On July 22, 2002, the Board of Directors approved the 2002 Employee Stock Purchase Plan for eligible domestic employees. The shareholders of Activision subsequently approved the 2002 Employee Stock Purchase Plan on September 19, 2002. Then, on February 11, 2003, the Board of Directors approved the 2002 Employee Stock Purchase Plan for International Employees. The primary terms of the 2002 Employee Stock Purchase Plan and the 2002 Employee Stock Purchase Plan for International Employees (collectively the "2002 Purchase Plans") are the same. Under the 2002 Purchase Plans, up to 1,125,000 shares of our common stock may be purchased by eligible employees during two overlapping, twelve-month offering periods that commence each April 1 and October 1 (the "Offering Period"). At any point in time, employees may participate in only one Offering Period. The first day of each Offering Period is referred to as the "Offering Date." Common stock is purchased by 2002 Purchase Plans participants at 85% of the lesser of fair market value on the Offering Date for the Offering Period that includes the common stock purchase date or the fair market value on the common stock purchase date. Employees may purchase shares having a value not exceeding 15% of their gross compensation during an Offering Period, limited to a maximum of 11,250

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common shares per common stock purchase date. During the year ended March 31, 2004, employees purchased approximately 242,300, 60,000 and 255,300 shares at a price of $5.48, $7.06 and $5.48 per share, respectively, within the 2002 Purchase Plans' Offering Periods.

Prior to the 2002 Purchase Plans, we had an employee stock purchase plan for all eligible domestic employees (the "Prior Purchase Plan"). Under the Prior Purchase Plan, shares of our common stock could be purchased at six-month intervals at 85% of the lower of the fair market value on the first or last day of each six-month period. Employees could purchase shares having a value not exceeding 10% of their gross compensation during each six-month period. Employees purchased approximately 114,750 and 209,250 shares at a price of $9.47 and $5.57 per share during the six months ended September 30, 2002 and March 31, 2003, respectively. The Prior Purchase Plan expired on March 31, 2003.

Activity of Employee and Director Options and Warrants

Activity of all employee and director options and warrants during the last three fiscal years was as follows (amounts in thousands, except weighted average exercise price amounts):

	2004		2003		2002	
	Shares	Wtd. Avg. Ex. Price	Shares	Wtd. Avg. Ex. Price	Shares	Wtd. Avg. Ex. Price
Outstanding at beginning of year	36,710	$6.35	28,943	$4.17	40,311	$2.87
Granted	6,795	7.22	14,423	9.48	9,246	7.25
Exercised	(4,585)	4.87	(5,675)	3.22	(19,533)	2.99
Forfeited	(2,282)	8.07	(981)	5.77	(1,081)	3.27
Outstanding at end of year	36,638	$6.59	36,710	$6.35	28,943	$4.17
Exercisable at end of year	19,600	$5.26	17,244	$4.29	14,252	$3.67

For the years ended March 31, 2004, 2003 and 2002, all options were granted at an exercise price equal to the fair market value on the date of grant.

The following tables summarize information about all employee and director stock options and warrants outstanding as of March 31, 2004 (share amounts in thousands):

	Outstanding Options			Exercisable Options	
	Shares	Remaining Wtd. Avg. Contractual Life (in years)	Wtd. Avg. Exercise Price	Shares	Wtd. Avg. Exercise Price
Range of exercise prices:					
$ 1.41 to $ 2.81	3,048	6.08	$ 1.88	2,784	$ 1.87
$ 2.93 to $ 3.11	6,205	5.00	3.11	6,119	3.11
$ 3.13 to $ 6.01	7,001	6.37	4.89	3,116	3.95
$ 6.08 to $ 6.29	5,363	7.45	6.25	3,018	6.23
$ 6.30 to $ 7.85	4,277	8.44	7.19	1,129	7.36
$ 7.94 to $10.20	5,270	8.50	9.79	985	9.77
$10.30 to $12.27	4,783	8.11	11.97	2,285	12.07
$12.29 to $14.23	666	8.68	13.36	157	13.35
$14.46 to $14.46	18	8.14	14.46	5	14.46
$14.77 to $14.77	7	8.18	14.77	2	14.77
	36,638	7.09	$ 6.59	19,600	$ 5.26

Non-Employee Warrants

In prior years, we have granted stock warrants to third parties in connection with the development of software and the acquisition of licensing rights for intellectual property. The warrants generally vest upon grant and are exercisable over the term of the warrant. The exercise price of third-party warrants is generally greater than or equal to the fair market value of our common stock at the date of grant. No third-party warrants were granted during the year ended March 31, 2004. As of March 31, 2004, 1,539,000 third-party warrants to purchase common stock were outstanding with a weighted average exercise price of $9.50 per share. During the year ended March 31, 2003, we granted warrants to a third party to purchase 337,500 shares of our common stock at an exercise price of $13.22 per share in connection with, and as partial consideration for, a license agreement that allows us to utilize intellectual property owned by the third party in conjunction with an Activision product. The warrants vested upon grant and have a three-year term. The fair value of the warrants was determined using the Black-Scholes pricing model, assuming a risk-free rate of 4.18%, a volatility factor of 70% and expected term as noted above. The per share weighted average estimated fair value of the third-party warrants granted during the year ended March 31, 2003 was $6.47 per share. As of March 31, 2003, 1,984,500 third-party warrants to purchase common stock were outstanding with a weighted average exercise price of $6.25 per share. No third-party warrants were granted during the year ended March 31, 2002. As of March 31, 2002, 1,747,500 third-party warrants to purchase common stock were outstanding with a weighted average exercise price of $7.81 per share.

In accordance with EITF 96-18, we measure the fair value of the securities on the measurement date. The fair value of each warrant is capitalized and amortized to expense when the related product is released and the related revenue is recognized. Additionally, as more fully described in Note 1, the recoverability of capitalized software development costs and intellectual property licenses is evaluated on a quarterly basis with amounts determined as not recoverable being charged to expense. In connection with the evaluation of capitalized software development costs and intellectual property licenses, any capitalized amounts for related third-party warrants are additionally reviewed for recoverability with amounts determined as not recoverable being amortized to expense. For the years ended March 31, 2004, 2003 and 2002, $0.2 million, $3.6 million and $1.1 million, respectively, was amortized and included in cost of sales—software royalties and amortization and/or cost of sales—intellectual property licenses.

Employee Retirement Plan

We have a retirement plan covering substantially all of our eligible employees. The retirement plan is qualified in accordance with Section 401(k) of the Internal Revenue Code. Under the plan, employees may defer up to 15% of their pre-tax salary, but not more than statutory limits. Effective January 1, 2003, we contribute 20% of each dollar contributed by a participant. Prior to January 1, 2003, we contributed 5% of each dollar contributed by a participant. Our matching contributions to the plan were approximately $700,000, $320,000 and $82,000 during the years ended March 31, 2004, 2003 and 2002, respectively.

16. Capital Transactions

Buyback Program

During fiscal 2003, our Board of Directors authorized a buyback program under which we can repurchase up to $350.0 million of our common stock. Under the program, shares may be purchased as determined by management, from time to time and within certain guidelines, in the open market or in privately negotiated transactions, including privately negotiated structured stock repurchase transactions and through transactions in the options markets. Depending on market conditions and other factors, these purchases may be commenced or suspended at any time or from time to time without prior notice.

Under the buyback program, we repurchased approximately 1.9 million shares of our common stock for $12.4 million and 16.2 million shares our common stock for $101.4 million, during the years ended March 31, 2004 and 2003,

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respectively. In addition, approximately 1.7 million shares of common stock were acquired in the year ended March 31, 2004 as a result of the settlement of $10.0 million of structured stock repurchase transactions entered into in fiscal 2003. Structured stock repurchase transactions are settled in cash or stock based on the market price of our common stock on the date of the settlement. Upon settlement, we either have our capital investment returned with a premium or receive shares of our common stock, depending, respectively, on whether the market price of our common stock is above or below a pre-determined price agreed in connection with each such transaction. These transactions are recorded in shareholders' equity in the accompanying consolidated balance sheets. As of March 31, 2004, we had approximately $226.2 million available for utilization under the buyback program and no outstanding structured stock repurchase transactions. In any period, cash provided by or used in financing activities related to common stock repurchase transactions may differ from the comparable change in shareholders' equity, reflecting timing differences between the recognition of share repurchase transactions and their settlement for cash.

Shelf Registrations

In August 2003, we filed with the Securities and Exchange Commission two amended shelf registration statements, including the base prospectuses therein. The first shelf registration statement, on Form S-3, allows us, at any time, to offer any combination of securities described in the base prospectus in one or more offerings with an aggregate initial offering price of up to $500.0 million. Unless we state otherwise in the applicable prospectus supplement, we expect to use the net proceeds from the sale of the securities for general corporate purposes, including capital expenditures, working capital, repayment or reduction of long-term and short-term debt and the financing of acquisitions and other business combinations. We may invest funds that we do not immediately require in marketable securities.

The second shelf registration statement, on Form S-4, allows us, at any time, to offer any combination of securities described in the base prospectus in one or more offerings with an aggregate initial offering price of up to $250.0 million in connection with our acquisition of the assets, business or securities of other companies whether by purchase, merger, or any other form of business combination.

Shareholders' Rights Plan

On April 18, 2000, our Board of Directors approved a shareholders' rights plan (the "Rights Plan"). Under the Rights Plan, each common shareholder at the close of business on April 19, 2000, received a dividend of one right for each share of common stock held. Each right represents the right to purchase one one-hundredths (1/100) of a share of our Series A Junior Preferred Stock at an exercise price of $40.00. Initially, the rights are represented by our common stock certificates and are neither exercisable nor traded separately from our common stock. The rights will only become exercisable if a person or group acquires 15% or more of the common stock of Activision, or announces or commences a tender or exchange offer which would result in the bidder's beneficial ownership of 15% or more of our common stock.

In the event that any person or group acquires 15% or more of our outstanding common stock each holder of a right (other than such person or members of such group) will thereafter have the right to receive upon exercise of such right, in lieu of shares of Series A Junior Preferred Stock, the number of shares of common stock of Activision having a value equal to two times the then current exercise price of the right. If we are acquired in a merger or other business combination transaction after a person has acquired 15% or more of our common stock, each holder of a right will thereafter have the right to receive upon exercise of such right a number of the acquiring company's common shares having a market value equal to two times the then current exercise price of the right. For persons who, as of the close of business on April 18, 2000, beneficially own 15% or more of the common stock of Activision, the Rights Plan "grandfathers" their current level of ownership, so long as they do not purchase additional shares in excess of certain limitations.

We may redeem the rights for $.01 per right at any time until the first public announcement of the acquisition of beneficial ownership of 15% of our common stock. At any time after a person has acquired 15% or more (but before any person has acquired more than 50%) of our common stock, we may exchange all or part of the rights for shares of common stock at an exchange ratio of one share of common stock per right. The rights expire on April 18, 2010.

17. Accumulated Other Comprehensive Income (Loss)

The components of accumulated other comprehensive income (loss) were as follows (amounts in thousands):

	Foreign Currency	Unrealized Appreciation (Depreciation) on Investments	Accumulated Other Comprehensive Income (Loss)
Balance, March 31, 2003	$ (3,568)	$134	$ (3,434)
Comprehensive income (loss)	13,432	(37)	13,395
Balance, March 31, 2004	$ 9,864	$ 97	$ 9,961

The amounts above are shown net of taxes. The income taxes related to other comprehensive income were not significant, as income taxes were not provided for foreign currency translation items as these are considered indefinite investments in non-U.S. subsidiaries.

18. Supplemental Cash Flow Information

Non-cash investing and financing activities and supplemental cash flow information are as follows (amounts in thousands):

Year ended March 31,	2004	2003	2002
Non-cash investing and financing activities:			
Conversion of convertible subordinated notes, net of conversion costs	$ —	$ —	$58,651
Subsidiaries acquired with common stock	3,246	10,861	25,481
Issuance of options and common stock warrants	—	2,184	3,217
Stock offering costs	—	781	—
Change in unrealized appreciation on short-term investments	(37)	134	—
Supplemental cash flow information:			
Cash paid for income taxes	$10,463	$ 5,491	$ 3,041
Cash paid (received) for interest, net	(6,213)	(7,804)	(2,942)

19. Quarterly Financial and Market Information (Unaudited)

	Quarter ended				
(Amounts in thousands, except per share data)	June 30	Sept. 30	Dec. 31	Mar. 31	Year ended
Fiscal 2004:					
Net revenues	$158,725	$117,523	$508,511	$162,897	$947,656
Operating income (loss)	5,146	(16,933)	116,961	4,643	109,817
Net income (loss)	4,163	(10,093)	76,981	6,664	77,715
Basic earnings (loss) per share	0.03	(0.08)	0.58	0.05	0.58
Diluted earnings (loss) per share	0.03	(0.08)	0.53	0.04	0.54
Common stock price per share:					
High	8.99	9.58	12.73	16.17	16.17
Low	6.01	7.23	7.71	11.38	6.01
Fiscal 2003:					
Net revenues	$191,258	$169,172	$378,685	$125,001	$864,116
Operating income (loss)	31,196	11,334	66,761	(14,444)	94,847
Net income (loss)	20,704	9,086	44,347	(7,957)	66,180
Basic earnings (loss) per share	0.15	0.06	0.30	(0.06)	0.46
Diluted earnings (loss) per share	0.14	0.06	0.28	(0.06)	0.43
Common stock price per share:					
High	15.60	14.02	10.61	7.00	15.60
Low	11.70	9.91	5.42	5.79	5.42

Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is quoted on the Nasdaq National Market under the symbol "ATVI."

The following table sets forth for the periods indicated the high and low reported sale prices for our common stock. As of May 26, 2004, there were approximately 2,840 holders of record of our common stock.

	High	Low
Fiscal 2003		
First Quarter ended June 30, 2002	$15.60	$11.70
Second Quarter ended September 30, 2002	14.02	9.91
Third Quarter ended December 31, 2002	10.61	5.42
Fourth Quarter ended March 31, 2003	7.00	5.79
Fiscal 2004		
First Quarter ended June 30, 2003	$ 8.99	$ 6.01
Second Quarter ended September 30, 2003	9.58	7.23
Third Quarter ended December 31, 2003	12.73	7.71
Fourth Quarter ended March 31, 2004	16.17	11.38

On May 26, 2004, the last reported sales price of our common stock was $15.88.

Dividends

We paid no cash dividends in 2004 or 2003 nor do we anticipate paying any cash dividends at any time in the foreseeable future. We expect that earnings will be retained for the continued growth and development of the business. Future dividends, if any, will depend upon our earnings, financial condition, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

Stock Splits

In April 2003, the Board of Directors approved a three-for-two split of our outstanding common shares effected in the form of a 50% stock dividend. The split was paid on June 6, 2003 to shareholders of record as of May 16, 2003. In February 2004, the Board of Directors approved a second three-for-two split of our outstanding common shares effected in the form of a 50% stock dividend. The split was paid on March 15, 2004 to shareholders of record as of February 23, 2004.

Corporate Information

Officers

Robert A. Kotick
Chairman and Chief Executive Officer

Brian G. Kelly
Co-Chairman

Ronald Doornink
President, Activision, Inc. and Chief Executive Officer, Activision Publishing, Inc.

Kathy P. Vrabeck
President, Activision Publishing

William J. Chardavoyne
Chief Financial Officer and Executive Vice President

Michael J. Rowe
Executive Vice President, Human Resources

Richard A. Steele
President, Activision Distribution and Executive Vice President, International Distribution

George L. Rose
Senior Vice President, Business and Legal Affairs, General Counsel and Secretary

Board of Directors

Robert A. Kotick
Chairman and Chief Executive Officer

Brian G. Kelly
Co-Chairman

Ronald Doornink
President, Activision, Inc. and Chief Executive Officer, Activision Publishing, Inc.

Robert J. Corti
Chief Financial Officer, Avon Products, Inc.

Kenneth L. Henderson
Partner, Bryan Cave LLP

Barbara S. Isgur
Former Senior Vice President, Stratagem

Robert J. Morgado
Chairman, Maroley Media Group

Peter J. Nolan
Managing Partner, Leonard Green & Partners, L.P.

Transfer Agent

Continental Stock Transfer
& Trust Company
17 Battery Place
New York, New York 10004
(212) 509-4000

Auditor

PricewaterhouseCoopers LLP
Los Angeles, California

Bank

US Bank
Los Angeles, California

Corporate Counsel

Bryan Cave LLP
New York, New York

Corporate Headquarters

Activision, Inc.
3100 Ocean Park Boulevard
Santa Monica, California 90405
(310) 255-2000

Domestic Offices

Dallas, Texas
Eagan, Minnesota
Eden Prairie, Minnesota
Encino, California
Hayward, California
Los Angeles, California
Madison, Wisconsin
New York, New York
San Francisco, California
Woodland Hills, California

International Offices

Bezons, France
Birmingham, United Kingdom
Breda, The Netherlands
Burglengenfeld, Germany
Legnano, Italy
Madrid, Spain
Ontario, Canada
Slough, United Kingdom
Stockholm, Sweden
Sydney, Australia
Tokyo, Japan
Venlo, The Netherlands

Forward-Looking Statements

The statements contained in this report that are not historical facts are "forward-looking statements." The company cautions readers of this report that a number of important factors could cause Activision's actual future results to differ materially from those expressed in any such forward-looking statements. These important factors, and other factors that could affect Activision, are described in Activision's Annual Report on Form 10-K for the fiscal year ended March 31, 2004, which was filed with the United States Securities and Exchange Commission. Readers of this Annual Report are referred to this filing.

World Wide Web Site

http://www.activision.com

E-Mail

IR@activision.com

Annual Meeting

September 21, 2004
The Peninsula Hotel
9882 South Santa Monica Blvd.
Beverly Hills, California 90212

Annual Report on Form 10-K

Activision's Annual Report on Form 10-K for the year ended March 31, 2004 is available to shareholders without charge upon request from our corporate offices.

Designed by Curran & Connors, Inc. / www.curran-connors.com

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