ACTIVISION INC /NY
Form 10-Q
January 31, 2003

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

ý **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended December 31, 2002

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____________ to _____________
Commission File Number 0-12699

ACTIVISION, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-4803544** (I.R.S. Employer Identification No.)
3100 Ocean Park Boulevard, Santa Monica, CA (Address of principal executive offices)	**90405** (Zip Code)

(310) 255-2000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

The number of shares of the registrant's Common Stock outstanding as of January 23, 2003 was 66,166,964.

ACTIVISION, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION.

Item 1. Financial Statements.

ACTIVISION, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	December 31, 2002	March 31, 2002
	(Unaudited)	
Assets		

	December 31, 2002	March 31, 2002
Current assets:		
Cash and cash equivalents	$ 358,984	$ 279,007
Short-term investments	169,874	
Accounts receivable, net of allowances of $76,728 and $42,019 at December 31, 2002 and March 31, 2002, respectively	158,393	76,733
Inventories	37,284	20,736
Software development	43,657	36,263
Intellectual property licenses	10,612	6,326
Deferred income taxes	27,345	22,608
Other current assets	11,553	15,200
Total current assets	817,702	456,873
Software development	7,818	3,254
Intellectual property licenses	42,221	10,899
Property and equipment, net	19,741	17,832
Deferred income taxes	11,806	28,795
Other assets	3,729	3,242
Goodwill	68,100	35,992
Total assets	$ 971,117	$ 556,887
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt	$ 145	$ 168
Accounts payable	106,658	64,410
Accrued expenses	93,815	59,096
Total current liabilities	200,618	123,674
Long-term debt, less current portion	2,676	3,122
Total liabilities	203,294	126,796
Commitments and contingencies (Note 14)		
Shareholders' equity:		
Preferred stock, $.000001 par value, 3,750,000 shares authorized, no shares issued at December 31, 2002 and March 31, 2002		
Series A Junior Preferred stock, $.000001 par value, 1,250,000 shares authorized, no shares issued at December 31, 2002 and March 31, 2002		
Common stock, $.000001 par value, 125,000,000 shares authorized, 71,428,422 and 61,034,263 shares issued and 65,284,867 and 56,705,504 shares outstanding at December 31, 2002 and March 31, 2002, respectively		
Additional paid-in capital	675,779	397,528
Retained earnings	138,521	64,384
Less: Treasury stock, at cost, 6,143,555 and 4,328,759 shares at December 31, 2002 and March 31, 2002, respectively	(44,182)	(20,323)
Accumulated other comprehensive loss	(2,295)	(11,498)
Total shareholders' equity	767,823	430,091

	December 31, 2002		March 31, 2002	
Total liabilities and shareholders' equity	$	971,117	$	556,887

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

ACTIVISION, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share data)

	For the three months ended December 31,				For the nine months ended December 31,			
	2002		2001		2002		2001	
Net revenues	$	378,685	$	371,341	$	739,115	$	621,523
Costs and expenses:								
Cost of sales product costs		204,881		195,560		369,004		347,840
Cost of sales software royalties and amortization		33,503		34,997		67,396		47,699
Cost of sales intellectual property licenses		14,918		23,087		32,704		33,546
Product development		13,758		10,848		38,768		29,059
Sales and marketing		33,875		31,883		84,644		67,064
General and administrative		10,989		13,165		37,308		32,603
Total costs and expenses		311,924		309,540		629,824		557,811
Operating income		66,761		61,801		109,291		63,712
Investment income, net		2,533		271		6,554		1,923
Income before income tax provision		69,294		62,072		115,845		65,635
Income tax provision		24,947		22,962		41,708		24,281
Net income	$	44,347	$	39,110	$	74,137	$	41,354
Basic earnings per share	$	0.66	$	0.75	$	1.15	$	0.84
Weighted average common shares outstanding		66,806		52,359		64,559		49,254
Diluted earnings per share	$	0.63	$	0.66	$	1.06	$	0.73
Weighted average common shares outstanding assuming dilution		70,815		59,293		69,881		56,635

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

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ACTIVISION, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	For the nine months ended December 31, 2002	2001
Cash flows from operating activities:		
Net income	$ 74,137	$ 41,354
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred income taxes	12,817	(27,009)
Depreciation and amortization	6,826	5,085
Amortization and write-offs of capitalized software development costs and intellectual property licenses	75,800	52,141
Tax benefit of stock options and warrants exercised	24,053	44,535
Loss on equity investments and other	224	
Changes in operating assets and liabilities (net of effects of acquisitions):		
Accounts receivable	(80,649)	(128,697)
Inventories	(16,548)	13,258
Software development and intellectual property licenses	(123,366)	(60,958)
Other assets	4,970	1,875
Accounts payable	41,984	60,172
Accrued expenses and other liabilities	28,802	42,667
Net cash provided by operating activities	49,050	44,423
Cash flows from investing activities:		
Capital expenditures	(6,941)	(6,583)
Proceeds from disposal of property and equipment	505	624
Purchases of short-term investments	(384,117)	
Proceeds from sales and maturities of short-term investments	214,817	
Cash payment to effect business combinations, net of cash acquired	(21,199)	
Minority capital investment	(1,500)	
Other		(129)
Net cash used in investing activities	(198,435)	(6,088)
Cash flows from financing activities:		
Proceeds from issuance of common stock to employees	18,862	39,987
Payment on term loan		(8,550)
Other borrowings, net	(717)	(1,384)
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 agreements	(25,000)	
Purchase of treasury stock	(18,929)	(74)

	For the nine months ended December 31,	
Net cash provided by financing activities	222,288	29,917
Effect of exchange rate changes on cash	7,074	889
Net increase in cash and cash equivalents	79,977	69,141
Cash and cash equivalents at beginning of period	279,007	125,550
Cash and cash equivalents at end of period	$ 358,984	$ 194,691

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

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ACTIVISION, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
For the nine months ended December 31, 2002
(Unaudited)
(In thousands)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock		Accumulated Other Comprehensive Income (Loss)	Shareholders' Equity
	Shares	Amount			Shares	Amount		
Balance, March 31, 2002	**61,034**	**$**	**$ 397,528**	**$ 64,384**	**(4,329)**	**$ (20,323)**	**$ (11,498)**	**$ 430,091**
Components of comprehensive income:								
Net income				74,137				74,137
Unrealized appreciation on short-term investments							498	498
Foreign currency translation adjustment							8,705	8,705
Total comprehensive income								83,340
Issuance of common stock pursuant to underwritten public offering	7,500		247,291					247,291
Issuance of common stock pursuant to employee stock option and stock purchase plans and common stock warrants	2,543		18,862					18,862
Issuance of common stock warrants			2,184					2,184
Tax benefit attributable to employee stock options and common stock warrants			24,053					24,053
Issuance of common stock to effect business combinations	351		10,861					10,861
Structured stock repurchase transactions			(25,000)					(25,000)

							Accumulated Other Comprehensive Income (Loss)	
Purchase of treasury stock					(1,815)	(23,859)		(23,859)
Balance, December 31, 2002	**71,428**	**$**	**$ 675,779**	**$ 138,521**	**(6,144)**	**$ (44,182) $**	**(2,295)**	**$ 767,823**

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

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ACTIVISION, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (Unaudited)
For the three and nine months ended December 31, 2002

1. Basis of Presentation

The accompanying consolidated financial statements include the accounts of Activision, Inc. and its subsidiaries ("Activision" or "we"). The information furnished is unaudited and reflects all adjustments that, in the opinion of management, are necessary to provide a fair statement of the results for the interim periods presented. The consolidated financial statements should be read in conjunction with the consolidated financial statements included in our Annual Report on Form 10-K for the year ended March 31, 2002 as filed with the Securities and Exchange Commission.

Certain amounts in the consolidated financial statements have been reclassified to conform to the current period's presentation. These reclassifications had no impact on previously reported working capital or results of operations.

2. Acquisitions

Effective October 4, 2002, we acquired all of the outstanding ownership interests of Luxoflux Corp., ("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. This acquisition further enables us to implement our multi-platform development strategy by augmenting our internal product development capabilities for console systems. The purchase price of the transaction, including acquisition costs, was approximately $9.2 million and has been allocated to assets acquired and liabilities assumed as follows (amounts in thousands):

Current assets	$	537
Property and equipment		83
Other assets		15
Goodwill		9,098
Current liabilities		(508)
	$	9,225

Goodwill has been included in the publishing segment of our business and is non-deductible for tax purposes. A significant portion of the purchase price for this acquisition was assigned to goodwill as the primary asset we acquired in the transaction was an assembled workforce with proven technical and design talent with a history of high quality product creation. The results of operations of Luxoflux are included in our consolidated statement of operations beginning October 4, 2002. Pro forma consolidated statements of operations are not shown, as they would not differ materially from reported results.

Approximately 110,000 shares of our common stock may be issued to Luxoflux'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 will be recorded as an additional element of the purchase price for Luxoflux when those contingencies are resolved.

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 249,190 shares of our common stock valued at approximately $8.2 million. Z-Axis is an experienced, multi-platform, console software developer. This acquisition further enables us to implement our multi-platform development strategy by augmenting our internal product development capabilities for console systems. The purchase price of the transaction, including acquisition costs, was valued at approximately $20.9 million and has been allocated to assets acquired and liabilities assumed as follows (amounts in thousands):

Current assets	$ 1,645
Other intangibles	113
Property and equipment	172
Other assets	20
Goodwill	20,239
Current liabilities	(1,323)
	$ 20,866

Goodwill has been included in the publishing segment of our business and is non-deductible for tax purposes. A significant portion of the purchase price for this acquisition was assigned to goodwill as the primary asset we acquired in the transaction was an assembled workforce with proven technical and design talent with a history of high quality product creation. The results of operations of Z-Axis are included in our consolidated statement of operations beginning May 20, 2002. Pro forma consolidated statements of operations are not shown, as they would not differ materially from reported results.

Approximately 93,000 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.

3. Short-term Investments

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 separate component of accumulated other comprehensive loss in shareholders' equity.

The following table summarizes our investments in securities as of December 31, 2002 (amounts in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents				
Cash and time deposits	$ 137,914	$	$	$ 137,914
Money market instruments	110,992			110,992
Auction rate notes	110,141		(63)	110,078
Cash and cash equivalents	359,047		(63)	358,984
Short-term investments				
Corporate bonds	32,113	107	(5)	32,215
Taxable municipal bonds	3,502			3,502
U.S. agency issues	62,626	91	(12)	62,705
Asset-backed securities	71,072	610	(230)	71,452

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Short-term investments	169,313	808	(247)	169,874
Cash, cash equivalents and short-term investments	$ 528,360	$ 808	$ (310)	$ 528,858

The following table summarizes the maturities of our investments in debt securities as of December 31, 2002 (amounts in thousands):

	Amortized Cost	Fair Value
Due in one year or less	$ 147,109	$ 147,152
Due after one year through two years	61,273	61,348
	208,382	208,500
Asset-backed securities	71,072	71,452
Total	$ 279,454	$ 279,952

The specific identification method is used to determine the cost of securities disposed with realized gains and losses reflected in investment income, net. For the three months ended December 31, 2002, net realized gains on short-term investments consisted of $188,000 of gross realized gains and $56,000 of gross realized losses. For the nine months ended December 31, 2002, net realized gains on short-term investments consisted of $191,000 of gross realized gains and $116,000 of gross realized losses.

4. Inventories

Inventories are valued at the lower of cost (first-in, first-out) or market. Our inventories consist of the following (amounts in thousands):

	December 31, 2002	March 31, 2002
Purchased parts and components	$ 1,763	$ 892
Finished goods	35,521	19,844
	$ 37,284	$ 20,736

5. Goodwill and Other Intangible Assets

Goodwill

The changes in the carrying amount of goodwill for the nine months ended December 31, 2002 are as follows (amounts in thousands):

	Publishing	Distribution	Total
Balance as of March 31, 2002	$ 31,626	$ 4,366	$ 35,992
Goodwill acquired during the period	29,337		29,337
Issuance of contingent consideration	2,668		2,668
Adjustment to original purchase allocation	(447)		(447)
Effect of foreign currency exchange rates		550	550

	Publishing	Distribution	Total
Balance as of December 31, 2002	$ 63,184	$ 4,916	$ 68,100

In July 2002 in connection with the satisfaction of certain product performance requirements as specified in the prior fiscal year acquisition agreement with Treyarch Invention, LLC, we issued 101,635 of our common shares with an assigned value of $2.7 million.

Acquired Intangible Assets

Acquired intangible assets are as follows (amounts in thousands):

	December 31, 2002		March 31, 2002	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized Intangible Assets				
Acquired software development and royalty agreements	$ 113	$ (113)	$ 84	$

Acquired intangible assets are included in the consolidated balance sheets in other current assets. For the nine months ended December 31, 2002, aggregate amortization expense related to acquired intangible assets was $113,400. There was no such amortization for the three months ended December 31, 2002 or for the three and nine months ended December 31, 2001.

6. Income Taxes

The income tax provision of $24.9 million and $41.7 million for the three and nine months ended December 31, 2002, respectively, reflects our effective income tax rate of approximately 36%. The income tax provision of $23.0 million and $24.3 million for the three and nine months ended December 31, 2001, respectively, reflects our effective income tax rate of approximately 37%. For both periods, the significant item that generated the variance between our effective rate and our statutory rate of 35% was state taxes, partially offset by research and development tax credits.

7. Software Development Costs and Intellectual Property Licenses

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 Standards ("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 game engine 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. 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. The following criteria are used to evaluate expected product performance: historical performance of comparable products; the commercial acceptance of prior products released on a given game engine; orders for the product prior to its release; estimated performance of a sequel product based on the performance of the product on which the sequel is based; and actual development costs of a product as compared to our budgeted amount.

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.

Intellectual property license costs represent license fees paid to intellectual property rights holders for use of their trademarks or copyrights in the development of our products.

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 used. 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. The following criteria are used to evaluate expected product performance: historical performance of comparable products; the commercial acceptance of prior products released on a given game engine; orders for the product prior to its release; estimated performance of a sequel product based on the performance of the product on which the sequel is based; and actual development costs of a product as compared to our budgeted amount.

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 trademark or copyright 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 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.

As of December 31, 2002, capitalized software development costs included $16.3 million of internally developed software costs and $35.2 million of payments made to independent software developers. As of March 31, 2002, capitalized software development costs included $16.0 million of internally developed software costs and $23.5 million of payments made to independent software developers. Capitalized intellectual property licenses were $52.8 million and $17.2 million as of December 31, 2002 and March 31, 2002, respectively. Amortization and write-offs of capitalized software development costs and intellectual property licenses, combined, was $41.1 million and $34.6 million for the three months ended December 31, 2002 and 2001, respectively. Amortization and

write-offs of capitalized software development costs and intellectual property licenses, combined, was $75.8 million and $52.1 million for the nine months ended December 31, 2002 and 2001, respectively.

8. Comprehensive Income

The components of comprehensive income for the three and nine months ended December 31, 2002 and 2001 were as follows (amounts in thousands):

	Three months ended December 31,		Nine months ended December 31,	
	2002	**2001**	**2002**	**2001**
Net income	$ 44,347	$ 39,110	$ 74,137	$ 41,354
Other comprehensive income (loss)				
Foreign currency translation adjustment	2,529	(435)	8,705	1,077
Unrealized appreciation on short-term investments	624		498	
Other comprehensive income (loss)	3,153	(435)	9,203	1,077

	Three months ended December 31,		Nine months ended December 31,	
Comprehensive income	$ 47,500	$ 38,675	$ 83,340	$ 42,431

9. Revenue Recognition

We recognize revenue from the sale of our products upon the transfer of title and risk of loss to our customers. We may permit product returns from or grant price protection to our customers on unsold merchandise under certain conditions. Price protection policies, when granted and applicable, allow customers a credit against amounts they owe us with respect to merchandise unsold by them. 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 from product sales is reflected after deducting the estimated allowance for returns and price protection. 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 based upon historical experience, customer inventory levels and changes in the demand and acceptance of our products by the end consumer.

10. Investment Income, Net

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

	Three months ended December 31,		Nine months ended December 31,	
	2002	2001	2002	2001
Interest expense	$ (138)	$ (615)	$ (810)	$ (1,732)
Interest income	2,539	886	7,289	3,655
Net realized gain on investments	132		75	
Investment income, net	$ 2,533	$ 271	$ 6,554	$ 1,923

11. Supplemental Cash Flow Information

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

	Nine months ended December 31,	
	2002	2001
Non-cash investing and financing activities		
Conversion of convertible subordinated notes, net of conversion costs	$	$ 58,651
Subsidiaries acquired with common stock	10,861	15,553
Issuance of options and common stock warrants	2,184	3,217
Stock offering costs	781	
Change in unrealized appreciation on short-term investments	498	
Supplemental cash flow information		
Cash paid for income taxes	$ 3,847	$ 2,085
Cash paid (received) for interest, net	(5,933)	(1,665)

12. 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, either directly, by license or through our affiliate label program with third party publishers. In the United States, our products are sold primarily on a direct basis to mass-market retailers, consumer electronics stores, discount warehouses and office super-stores. We conduct our international publishing activities through offices in the United Kingdom, Germany, France, 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.

Distribution refers to our European operations located in the United Kingdom, 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 segments are not evaluated based on assets or depreciation.

The accounting policies of these segments are the same as those described in the Summary of Significant Accounting Policies in our Annual Report on Form 10-K for the year ended March 31, 2002. Revenue derived from sales between segments is eliminated in consolidation.

Information on the reportable segments for the three and nine months ended December 31, 2002 and 2001 is as follows (amounts in thousands):

	Three months ended December 31, 2002		
	Publishing	Distribution	Total
Total segment revenues	$ 256,729	$ 121,956	$ 378,685
Revenues from sales between segments	(26,345)	26,345	
Revenues from external customers	$ 230,384	$ 148,301	$ 378,685
Operating income	$ 54,926	$ 11,835	$ 66,761
Goodwill	$ 63,184	$ 4,916	$ 68,100
Total assets	$ 818,659	$ 152,458	$ 971,117

	Three months ended December 31, 2001		
	Publishing	Distribution	Total
Total segment revenues	$ 260,737	$ 110,604	$ 371,341
Revenues from sales between segments	(25,178)	25,178	
Revenues from external customers	$ 235,559	$ 135,782	$ 371,341
Operating income	$ 53,497	$ 8,304	$ 61,801
Goodwill	$ 21,045	$ 4,452	$ 25,497

	Three months ended December 31, 2001		
Total assets	$ 425,659	$ 168,543	$ 594,202

	Nine months ended December 31, 2002		
	Publishing	Distribution	Total
Total segment revenues	$ 536,972	$ 202,143	$ 739,115
Revenues from sales between segments	(51,535)	51,535	
Revenues from external customers	$ 485,437	$ 253,678	$ 739,115
Operating income	$ 96,659	$ 12,632	$ 109,291
Goodwill	$ 63,184	$ 4,916	$ 68,100
Total assets	$ 818,659	$ 152,458	$ 971,117

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	Nine months ended December 31, 2001		
	Publishing	Distribution	Total
Total segment revenues	$ 441,195	$ 180,328	$ 621,523
Revenues from sales between segments	(38,659)	38,659	
Revenues from external customers	$ 402,536	$ 218,987	$ 621,523
Operating income	$ 54,311	$ 9,401	$ 63,712
Goodwill	$ 21,045	$ 4,452	$ 25,497
Total assets	$ 425,659	$ 168,543	$ 594,202

Geographic information for the three and nine months ended December 31, 2002 and 2001 is based on the location of the selling entity. Revenues from external customers by geographic region were as follows (amounts in thousands):

	Three months ended December 31,		Nine months ended December 31,	
	2002	2001	2002	2001
United States	$ 179,643	$ 194,497	$ 380,045	$ 332,441
Europe	190,030	171,531	342,561	278,902
Other	9,012	5,313	16,509	10,180
Total	$ 378,685	$ 371,341	$ 739,115	$ 621,523

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

	Three months ended December 31,		Nine months ended December 31,	
	2002	2001	2002	2001
Console	$ 320,528	$ 254,353	$ 582,160	$ 376,496
Hand-held	25,632	50,438	56,859	137,072
PC	32,525	66,550	100,096	107,955
Total	$ 378,685	$ 371,341	$ 739,115	$ 621,523

As of and for the three and nine months ended December 31, 2002, we had one customer that accounted for 17% of consolidated net revenues and 29% of consolidated accounts receivable, net. As of and for the three and nine months ended December 31, 2001, we had one customer that accounted for 15% of consolidated net revenues and 23% 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.

13. 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):

	Three months ended December 31,		Nine months ended December 31,	
	2002	2001	2002	2001
Numerator				
Numerator for basic and diluted earnings per share income available to common shareholders	$ 44,347	$ 39,110	$ 74,137	$ 41,354
Denominator				
Denominator for basic earnings per share weighted average common shares outstanding	66,806	52,359	64,559	49,254
Effect of dilutive securities:				
Employee stock options and stock purchase plan	3,761	6,454	4,948	6,742
Warrants to purchase common stock	248	480	374	639
Potential dilutive common shares	4,009	6,934	5,322	7,381
Denominator for diluted earnings per share weighted average common shares outstanding plus assumed conversions	70,815	59,293	69,881	56,635
Basic earnings per share	$ 0.66	$ 0.75	$ 1.15	$ 0.84
Diluted earnings per share	$ 0.63	$ 0.66	$ 1.06	$ 0.73

Options to purchase 4,702,748 shares of common stock at exercise prices ranging from $18.61 to $33.24 and options to purchase 2,254,633 shares of common stock at exercise prices ranging from $24.98 to $33.24 were outstanding for the three and nine months ended December 31, 2002, respectively, but were not included in the calculation of diluted earnings per share because their effect would be antidilutive.

Options to purchase 100,094 shares of common stock at exercise prices ranging from $23.39 to $25.81 and options to purchase 80,713 shares of common stock at exercise prices ranging from $21.63 to $25.81 were outstanding for the three and nine months ended December 31, 2001, respectively, but were not included in the calculation of diluted earnings per share because their effect would be antidilutive.

14. Commitments

Credit Facilities and Other

In June 1999, we obtained a $100.0 million revolving credit facility and a $25.0 million term loan with a syndicate of banks (the "U.S. Facility"). The revolving portion of the U.S. Facility provided us with the ability to borrow up to $100.0 million, including issuing letters of credit up to $80.0 million, on a revolving basis against eligible accounts receivable and inventory. The term loan had a three-year term with principal amortization on a straight-line quarterly basis beginning December 31, 1999, a borrowing rate based on the banks' base rate (which was generally equivalent to the published prime rate) plus 2% or LIBOR plus 3% and was to expire June 2002. The revolving portion of the U.S. Facility had a borrowing rate based on the banks' base rate plus 1.75% or LIBOR plus 2.75%. In May 2001, we accelerated our repayment of the outstanding balance under the term loan portion of the U.S. Facility. In connection with the accelerated repayment, we amended the U.S. Facility (the

"Amended and Restated U.S. Facility"). The Amended and Restated U.S. Facility eliminated the term loan, reduced the revolver to $78.0 million and reduced the interest rate to the banks' base rate plus 1.25% or LIBOR plus 2.25%. The Amended and Restated U.S. Facility was collateralized by substantially all of our assets and expired in August 2002. Due to our improved financial position, including significant cash, cash equivalent and short-term investment balances and minimal debt, we did not seek additional bank financing upon the expiration of the Amended and Restated U.S. Facility.

We have a revolving credit facility through our CD Contact subsidiary in the Netherlands (the "Netherlands Facility"). The Netherlands Facility permitted revolving credit loans and letters of credit up to Euro ("EUR") 2.5 million ($2.6 million) as of December 31, 2002, based upon eligible accounts receivable balances. The Netherlands Facility is due on demand, bears interest at a Eurocurrency rate plus 1.25%, is collateralized by the subsidiary's accounts receivable and inventory and a EUR 0.5 million ($0.5 million) guarantee made by our Centresoft subsidiary through its bank facility and expires August 2003. As of December 31, 2002, there were no borrowings or letters of credit outstanding under the Netherlands Facility.

We also have revolving credit facilities with our CentreSoft subsidiary located in the United Kingdom (the "UK Facility") and our NBG subsidiary located in Germany (the "German Facility"). As of December 31, 2002, the UK Facility provided Centresoft with the ability to borrow up to Great British Pounds ("GBP") 8.0 million ($12.8 million), including issuing letters of credit, on a revolving basis. Furthermore, as of December 31, 2002, under the UK Facility, Centresoft provided a EUR 0.5 million ($0.5 million) guarantee which served as collateral for the Netherlands Facility. The UK Facility bears interest at LIBOR plus 1.5%, is collateralized by substantially all of the assets of the subsidiary and expires in October 2003. The UK Facility also contains various covenants that require the subsidiary to maintain specified financial ratios related to, among others, fixed charges. As of December 31, 2002, we were in compliance with these covenants. No borrowings were outstanding against the UK Facility as of December 31, 2002. The German Facility provided for revolving loans up to EUR 0.8 million ($0.8 million) as of December 31, 2002, bears interest at a Eurocurrency rate plus 2.5%, is collateralized by the subsidiary's accounts receivable, inventory and certain property and equipment and expires June 2003. No borrowings were outstanding against the German Facility as of December 31, 2002.

In connection with our purchases of Nintendo GameCube and Game Boy software for distribution in North America and Europe, Nintendo requires us to provide either standby letters of credit or cash prepayment prior to accepting purchase orders.

Private Placement of Convertible Subordinated Notes

In December 1997, we completed the private placement of $60.0 million principal amount of $6^{3}/_{4}$% 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 $12.583 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.

Software Developer and Intellectual Property License 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. Assuming all contractual provisions are met, the total future minimum contract commitment for contracts in place as of December 31, 2002 is approximately $135.4 million and is scheduled to be paid as follows (amounts in thousands):

Fiscal year ending March 31,		
2003	$	23,681
2004		71,050
2005		19,991
2006		12,300
2007 and thereafter		8,425
Total	$	135,447

Legal Proceedings

We are party to 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, the outcome of such routine claims will not have a material adverse effect on our business, financial condition, results of operations or liquidity.

15. Capital Transactions

On October 4, 2002, our Board of Directors authorized a buyback program under which we can repurchase up to $150.0 million of our common stock. Under the program, shares may be purchased as determined by management from time to time in the open market or in privately negotiated transactions, including privately negotiated structured option 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.

As of December 31, 2002, we had repurchased approximately 1.8 million shares of our common stock at an average cost of $13.15 per share. Additionally under the Board approved buyback program, we entered into a series of structured stock repurchase transactions in the aggregate amount of $25.0 million. These transactions may be settled in cash or stock based on the market price of our common stock on the date of the settlement. Upon settlement, we will either have our capital investment returned with a premium or receive up to approximately 2.1 million 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 sheet as of December 31, 2002.

On December 16, 2002, the Board of Directors approved the Activision 2002 Studio Employee Retention Incentive Plan (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 exercise price for Awards issued under the 2002 Studio Plan is determined at the discretion of the Board of Directors (or the Compensation Committee of the Board of Directors, which administers the 2002 Studio Plan), and 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 five years. Awards must typically be exercised within 10 years of the date of grant. 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 800,000. There were 400,000 shares remaining for grant under the 2002 Studio Plan as of December 31, 2002.

16. 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 ten years. The fees we paid to the law firm account for less than 1% of the firm's total revenues. The rates charged to us were at arm's length, and we believe that the fees are competitive with the fees charged by other law firms.

17. Recently Issued Accounting Standards

In June 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 requires that the liability for costs associated with an exit or disposal activity be initially measured at fair value and recognized when the liability is incurred. The provisions of SFAS No. 146 are required to be applied prospectively to exit or disposal activities initiated after December 31, 2002.

In January 2003, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure, an amendment of FASB Statement No. 123." SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. It also requires disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for annual and interim periods beginning after December 15, 2002. As we have elected not to change to the fair value based method of accounting for stock-based employee compensation, the adoption of SFAS No. 148 will not have an impact upon our financial condition or results of operations.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

OVERVIEW

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 growing variety of consumer demographics.

Our products cover the action/adventure, action sports, racing, role-playing, simulation, first-person action and strategy game categories. We offer our products in versions that operate on the Sony PlayStation 2 ("PS2"), Sony PlayStation ("PS1"), Nintendo GameCube ("GameCube") and Microsoft Xbox ("Xbox") console systems, Nintendo Game Boy Advance ("GBA") hand-held device, as well as on personal computers ("PC").

Our publishing business involves the development, marketing and sale of products, either directly, by license or through our affiliate label program with third party publishers. In the United States, our products are sold primarily on a direct basis to mass-market retailers, consumer electronics stores, discount warehouses and office super-stores. We conduct our international publishing activities through offices in the United Kingdom, Germany, France, 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. In addition to publishing, we maintain distribution operations located in the United Kingdom, 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 segments. Publishing operating margins are substantially higher than margins realized from our distribution segment. Operating margins in our distribution segment are also affected by the mix of hardware and software sales, with software producing higher margins than hardware.

Our focus with respect to future game development will be on big, well-established brands that we believe we can build into successful franchises such as our super heroes and action sports brands. With regards to our super heroes brands, we recently exercised an option to develop and publish the video game based on the "Spider-Man" movie sequel which is expected to be released in the spring of 2004. *Spider-Man: The Movie* was a key release for the first quarter of fiscal 2003 and has continued to perform strongly throughout fiscal 2003. In December 2002, we expanded our long-term alliance with Marvel Enterprises through an exclusive, multi-year, licensing agreement that expires in 2009. The agreement extends our exclusive rights to develop and publish video games based on Marvel's comic book franchises Spider-Man, X-MEN, Fantastic Four and Iron Man. The agreement additionally provides us the rights to develop video games in conjunction with motion pictures and television series involving X-MEN, Fantastic Four and Iron Man. Further, another important strategy of ours is to continue to be a leader in the action sports category. On October 23, 2002, in the action sports category, we released *Tony Hawk's Pro Skater 4* across multiple platforms. We will continue to promote our action sports franchises with the release of titles for existing franchises such as *Tony Hawk's Pro Skater* and *Street Hoops*, as well as new action sports titles, such as *Wakeboarding Unleashed,* as well as titles related to motor cross and snowboarding.

We will also continue to evaluate emerging brands that we believe have potential to become successful franchises. For example, in August, 2002, we entered into 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" that is in development for a feature film by Paramount Pictures and Nickelodeon Movies. In December 2002, we also entered into a multi-year, multi-property, publishing agreement with DreamWorks SKG that grants us the exclusive rights to publish video games based on DreamWork's three upcoming computer-animated films, as well as their sequels.

We intend to utilize these new intellectual property acquisitions and our existing library of intellectual property to further focus our future game development on big, well-established brands that we believe have the potential to become franchise properties with sustainable consumer appeal and brand recognition. We also intend to create a limited number of new intellectual properties that we believe have the potential to join this list of franchise properties. Accordingly, we have chosen to

eliminate certain small and non-core projects from our development plan and expect to reduce the number of titles released in fiscal 2004. Additionally, in order to maintain the competitiveness of our products and to take advantage of increasingly sophisticated technology associated with new hardware platforms, we intend to increase the amount of time spent play testing new products, to conduct more extensive product quality evaluations and to lengthen product development schedules to allow time to make the improvements indicated by the testing and evaluations. This may result in an increase in future product development costs. Further, as a result of the expected increase in the length of product development schedules, the expected release dates of certain fiscal 2004 titles have been shifted to fiscal 2005.

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 in the Notes to the Consolidated Financial Statements in Item 8 of our Annual Report on Form 10-K for the year ended March 31, 2002 as filed with the Securities and Exchange Commission. 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. We may permit product returns from or grant price protection to our customers on unsold merchandise under certain conditions. Price protection policies, when granted and applicable, allow customers a credit against amounts they owe us with respect to merchandise unsold by them. 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. We may permit product returns from or grant price protection to our customers under certain conditions. 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 based upon historical experience, customer inventory levels and changes in the demand and acceptance of our products by the end consumer. 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. Material differences may result in the amount and timing of our revenue for any period if management makes different judgments or utilizes different estimates.

Similarly, management must make estimates of the uncollectibility of our accounts receivable. In estimating the allowance for doubtful accounts, we analyze historical bad debts, customer concentrations, customer credit worthiness, 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 Standards ("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 game engine 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. 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. The following criteria are used to evaluate expected product performance: historical performance of comparable products; the commercial acceptance of prior products released on a given game engine; orders for the product prior to its release; estimated performance of a sequel product based on the performance of the product on which the sequel is based; and actual development costs of a product as compared to our budgeted amount.

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 judgment 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.

Intellectual Property Licenses. Intellectual property license costs represent license fees paid to intellectual property rights holders for use of their trademarks or copyrights in the development of our products.

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 used. 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. The following criteria are used to evaluate expected product performance: historical performance of comparable products; the commercial acceptance of prior products released on a given game engine; orders for the product prior to its release; estimated performance of a sequel product based on the performance of the product on which the sequel is based; and actual development costs of a product as compared to our budgeted amount.

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 trademark or copyright 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 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 judgment and estimates are utilized in the assessment of the recoverability of capitalized costs.

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

	Three months ended December 31,				Nine months ended December 31,			
	2002		2001		2002		2001	
Net revenues	$ 378,685	100%	$ 371,341	100%	$ 739,115	100%	$ 621,523	100%
Costs and expenses:								
Cost of sales product costs	204,881	54	195,560	53	369,004	50	347,840	56
Cost of sales software royalties and amortization	33,503	9	34,997	9	67,396	9	47,699	8
Cost of sales intellectual property licenses	14,918	4	23,087	6	32,704	4	33,546	5
Product development	13,758	3	10,848	3	38,768	5	29,059	5
Sales and marketing	33,875	9	31,883	9	84,644	12	67,064	11
General and administrative	10,989	3	13,165	3	37,308	5	32,603	5
Total costs and expenses	311,924	82	309,540	83	629,824	85	557,811	90
Operating income	66,761	18	61,801	17	109,291	15	63,712	10
Investment income, net	2,533	1	271		6,554	1	1,923	1
Income before income tax provision	69,294	19	62,072	17	115,845	16	65,635	11
Income tax provision	24,947	7	22,962	6	41,708	6	24,281	4
Net income	$ 44,347	12%	$ 39,110	11%	$ 74,137	10%	$ 41,354	7%
NET REVENUES BY TERRITORY:								
United States	$ 179,643	47%	$ 194,497	52%	$ 380,045	51%	$ 332,441	53%
Europe	190,030	50	171,531	46	342,561	47	278,902	45
Other	9,012	3	5,313	2	16,509	2	10,180	2
Total net revenues	$ 378,685	100%	$ 371,341	100%	$ 739,115	100%	$ 621,523	100%
ACTIVITY/PLATFORM MIX:								
Publishing:								
Console	$ 211,993	83%	$ 176,081	68%	$ 409,919	77%	$ 255,181	58%
Hand-held	19,574	7	31,879	12	45,061	8	101,479	23
PC	25,162	10	52,777	20	81,992	15	84,535	19
Total publishing net revenues	256,729	68	260,737	70	536,972	73	441,195	71
Distribution:								
Console	108,535	89	78,272	71	172,241	85	121,315	67
Hand-held	6,058	5	18,559	17	11,798	6	35,593	20
PC	7,363	6	13,773	12	18,104	9	23,420	13
Total distribution net revenues	121,956	32	110,604	30	202,143	27	180,328	29
Total net revenues	$ 378,685	100%	$ 371,341	100%	$ 739,115	100%	$ 621,523	100%

	Three months ended December 31,				Nine months ended December 31,			
OPERATING INCOME BY SEGMENT:								
Publishing	$ 54,926	15%	$ 53,497	15%	$ 96,659	13%	$ 54,311	9%
Distribution	11,835	3	8,304	2	12,632	2	9,401	1
Total operating income	$ 66,761	18%	$ 61,801	17%	$ 109,291	15%	$ 63,712	10%

Results of Operations Three and Nine Months Ended December 31, 2002 and 2001

Net Revenues

Net revenues for the three months ended December 31, 2002 increased 2% over the same period last year, from $371.3 million to $378.7 million. Net revenues for the nine months ended December 31, 2002 increased 19% over the same period last year, from $621.5 million to $739.1 million. The increase in the three-month period was generated by our distribution business, offset by a small decrease in publishing net revenues. The increase in the nine-month period was generated by both our publishing and distribution businesses.

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Publishing net revenues for the three months ended December 31, 2002 decreased 2% from $260.7 million to $256.7 million. The following table details our publishing net revenues by platform as a percentage of total publishing net revenues for the three months ended December 31, 2002 and 2001:

	Three months ended December 31, 2002	Three months ended December 31, 2001
Publishing Net Revenues		
PC	**10%**	**20%**
Console	**83%**	**68%**
PlayStation 2	48	33
Microsoft Xbox	13	4
Nintendo GameCube	12	6
PlayStation	10	20
Nintendo 64		4
Sega Dreamcast		1
Hand-held	**7%**	**12%**
Game Boy Advance	6	7
Game Boy Color	1	5
Total publishing net revenues	**100%**	**100%**

There were several factors that affected the fiscal 2003 third quarter net revenue performance of our publishing business. First, positively impacting our performance, was an improvement in console software sales. Our publishing console net revenues for the three months ended December 31, 2002 increased 20% when compared to the same period last year, from $176.1 million to $212.0 million. Publishing console net revenues in the three months ended December 31, 2002 reflect the multi-national, cross-platform release of *Tony Hawk's Pro Skater 4,* which performed well on many platforms, in both the domestic and international markets. Additionally, catalog sales remained strong for *Spider-Man: The Movie*, released in the first quarter of fiscal 2003. We also had strong sales from titles under our Cabela's brand. Second, sales for the legacy console systems and hand-held devices did not perform as expected, particularly PS1 and Nintendo's Game Boy Color, and partially offset an improvement in sales for the current generation of console systems. Another negative impact on third quarter publishing sales was the decline in our PC software sales. Publishing PC net revenues for the three months ended December 31, 2002 decreased 52% when compared to the same period last year, from $52.8 million to $25.2 million. For the three months ending December 31, 2001, we released two premium PC titles, including *Return to Castle Wolfenstein,* which was one of our top performing titles during that period. In contrast, for the three months ended December 31, 2002, we released only one smaller PC title. Lastly, although *Tony Hawk's Pro Skater 4* performed well, the other console titles we released during the three months ended December 31, 2002, did not perform as strongly, negatively impacting publishing console sales.

Distribution net revenues for the three months ended December 31, 2002 increased 10% from $110.6 million to $122.0 million. The overall increase was primarily due to the positive impact of the year-over-year strengthening of the Euro and the Great British Pound ("GBP") in relation to the U.S. dollar. In addition, the product mix of our distribution business changed in the three months ended December 31, 2002 over the same period last year. Distribution console net revenues for the three months ended December 31, 2002 increased 39% over the same period last year, from $78.3 million to $108.5 million. Distribution console net revenues for the three months ended December 31, 2002 benefited from the international hardware launches of Xbox and GameCube in March 2002 and May 2002, respectively. The increase in distribution console net revenues was offset by a decline in distribution hand-held net revenues from $18.6 million for the three months ended December 31, 2001, to $6.1 million for the three months ended December 31, 2002. This decrease reflects the fact that the GBA hardware was launched in June 2001. Distribution hand-held sales for the three months ended December 31, 2001 benefited accordingly. The increase in distribution console net revenues was also offset by a decline in distribution PC net revenues from $13.8 million for the three months ended

December 31, 2001, to $7.4 for the three months ended December 31, 2002, primarily as a result of fewer premium PC titles released into the market in fiscal 2003 when compared to fiscal 2002.

Domestic net revenues declined 8% from $194.5 million for the three months ended December 31, 2001, to $179.6 million for the three months ended December 31, 2002 for the reasons as detailed above in the discussion of our publishing business net revenues. International net revenues increased by 13% from $176.8 million for the three months ended December 31, 2001, to $199.0 million for the three months ended December 31, 2002. International net revenues were positively affected due to the year-over-year strengthening of the Euro and the GBP in relation to the U.S. dollar.

Publishing net revenues for the nine months ended December 31, 2002 increased 22% from $441.2 million to $537.0 million. The following table details our publishing net revenues by platform as a percentage of total publishing net revenues for the nine months ended December 31, 2002 and 2001:

	Three months ended December 31,	
	2002	**2001**
Publishing Net Revenues		
PC	**15%**	**19%**
Console	**77%**	**58%**
PlayStation 2	42	21
Microsoft Xbox	13	2
Nintendo GameCube	13	4
PlayStation	8	23
Nintendo 64	1	7
Sega Dreamcast		1
Hand-held	**8%**	**23%**

	Three months ended December 31,	
Game Boy Advance	7	15
Game Boy Color	1	8
Total publishing net revenues	**100%**	**100%**

The increase in publishing net revenues was primarily attributable to a 61% increase in console software sales, from $255.2 million to $409.9 million due to the simultaneous cross-platform, multi-national release in the first quarter of fiscal 2003 of *Spider-Man: The Movie,* the third quarter fiscal 2003 release of *Tony Hawk's Pro Skater 4* and the benefit from a price reduction in console hardware prices resulting in an increased hardware base. This increase was partially offset by a 56% decrease in publishing hand-held net revenues, from $101.5 million to $45.1 million. This decrease reflects the fact that the GBA hardware was launched in June 2001. Our GBA software sales for the nine months ended December 31, 2001 benefited from the related hardware launch. Additionally, we released fewer titles for the hand-held platforms in the nine months ended December 31, 2002, 11 titles, in comparison to 19 titles in the same period last year.

Distribution net revenues for the nine months ended December 31, 2002 increased 12% from the same period last year, from $180.3 million to $202.1 million, driven by an increase in distribution console net revenues. Distribution console net revenues for the nine months ended December 31, 2002 increased 42% over the same period last year, from $121.3 million to $172.2 million. Distribution console net revenues for the nine months ended December 31, 2002 benefited from the international hardware launches of Xbox and GameCube in March 2002 and May 2002, respectively. Additionally, we 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 described above in the discussion of distribution net revenues for the three months ended December 31, 2002. Distribution net revenues for the nine months ended December 31, 2002 additionally benefited from a year-over-year strengthening of the Euro and the GBP in relation to the U.S. dollar.

Domestic net revenues grew 14% from $332.4 million for the nine months ended December 31, 2001 to $380.0 million for the nine months ended December 31, 2002. International net revenues increased by 24% from $289.1 million for the nine months ended December 31, 2001 to $359.1 million for the nine months ended December 31, 2002. The increase in domestic net revenues is attributable to the improvements in our publishing segment as described above, and the increase in international net revenues is attributable to the improvements in both our publishing and distribution segments as described above.

A significant portion of our publishing net revenues is derived from products based on a relatively small number of popular brands each year. For example, for the three months ended December 31, 2002, approximately 31% of consolidated net revenues and 46% of publishing net revenues were generated by our Tony Hawk brand. We expect that a limited number of popular brands will continue to produce a disproportionately large amount of our publishing net revenues.

Costs and Expenses

Cost of sales product costs represented 54% and 53% of consolidated net revenues for the three months ended December 31, 2002 and 2001, respectively. There were several factors that affected cost of sales product costs as a percentage of consolidated net revenues. First, distribution net revenues as a percentage of total consolidated net revenues increased from 30% for the three months ended December 31, 2001 to 32% for the three months ended December 31, 2002. Distribution net revenues have a higher per unit cost as compared to publishing net revenues. Second, the product mix of our publishing business changed. In the three months ended December 31, 2002, a higher proportion of publishing net revenues were derived from console sales than from PC sales as compared to the three months ended December 31, 2001. Console systems have a higher manufacturing cost per unit than PCs. Lastly, these increases in cost of sales product costs as a percentage of consolidated net revenues were partially offset by the lower proportion of sales from hand-held devices in the three months ended December 31, 2002 as compared to the three months ended December 31, 2001. Hand-held devices generally have the highest manufacturing per unit cost of all platforms. Cost of sales product costs represented 50% and 56% of consolidated net revenues for the nine months ended December 31, 2002 and 2001, respectively. The decrease was due to several factors. First, the product mix of our publishing business for the nine months ended December 31, 2002 reflects a lower proportion of net revenues from hand-held devices, as compared to the nine months ended December 31, 2001. Second, distribution net revenues as a percentage of total consolidated net revenues decreased from 29% for the nine months ended December 31, 2001 to 27% for the nine months ended December 31, 2002. Lastly, our console manufacturing costs for the nine months ended December 31, 2002 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 remained constant as a percentage of publishing net revenues at 13% for the three months ended December 31, 2002 and 2001. Cost of sales software royalties and amortization increased as a percentage of publishing net revenues to 13% for the nine

months ended December 31, 2002, from 11% for the nine months ended December 31, 2001. The increase reflects the change in the product mix of our publishing business. Though GBA titles generally have the highest per unit manufacturing cost of all platforms, they have the lowest product development cost structure. As such, in the nine months ended December 31, 2001 in which GBA titles 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 nine months ended December 31, 2002 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.

Cost of sales intellectual property licenses for the three months ended December 31, 2002 decreased as a percentage of publishing net revenues over the same period last year, from 9% to 6%. In absolute dollars, for the three months ended December 31, 2002 as compared to the three months ended December 31, 2001, cost of sales intellectual property licenses also decreased from $23.1 million to $14.9 million. These decreases were due to the fact that one of our top performing titles released in the third quarter of fiscal 2002 had a higher intellectual property royalty rate structure than any of the top performing titles released in the third quarter of fiscal 2003. Cost of sales intellectual property licenses for the nine months ended December 31, 2002 decreased as a percentage of publishing net revenues over the same period last year, from 8% to 6%. As described above, this is due to one of our top performing titles released in the third quarter of fiscal 2002 having a higher intellectual property royalty rate structure than any of the top performing titles released in the third quarter of fiscal 2003. In absolute dollars, cost of sales intellectual property licenses remained relatively flat at $32.7 million and $33.5 million, for the nine months ended December 31, 2002 and 2001, respectively. This was the result of the overall higher volume of publishing net revenues in the nine months ended December 31, 2002 as compared to the nine months ended December 31, 2001.

Product development expenses as a percentage of publishing net revenues have stayed relatively flat for the three months ended December 31, 2002 and 2001 at 5% and 4%, respectively, as well as for the nine months ended December 31, 2002 and 2001 at 7%. In absolute dollars, product development expense for the three months ended December 31, 2002 increased $3.0 million over the same period last year, from $10.8 million to $13.8 million. In absolute dollars, product development expense for the nine months ended December 31, 2002 increased $9.7 million over the same period last year, from $29.1 million to $38.8 million. These increases in absolute dollars reflect the change in the product mix of titles in development, more console and less hand-held, during the fiscal 2003 periods. The cost to develop titles for 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.

Sales and marketing expenses for the three months ended December 31, 2002 and 2001 remained relatively constant at $33.9 million and $31.9 million, respectively, representing 9% of consolidated net revenues for both periods. Sales and marketing expenses of $84.6 million and $67.1 million for the nine months ended December 31, 2002 and 2001, respectively, represented 12% and 11% of consolidated net revenues, respectively. The increase in sales and marketing expense dollars for the nine months ended December 31, 2002 over the same period last 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, multi-national 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 quarter releases such as *Street Hoops*. Additionally, in the nine months ended December 31, 2002, we also provided sponsorship for select action sports tours/tournaments in support of our Activision O_2 brand. The increase in sales and marketing expense dollars in our distribution business was the 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 expenses for the three months ended December 31, 2002, decreased $2.2 million over the same period last year, from $13.2 million to $11.0 million. As a percentage of consolidated net revenues, general and administrative expenses remained constant at approximately 3% for both periods. The decrease in absolute dollars is primarily the result of reductions in payroll and benefits related costs. General and administrative expenses for the nine months ended December 31, 2002, increased $4.7 million over the same period last year, from $32.6 million to $37.3 million. As a percentage of consolidated net revenues, general and administrative expenses remained constant at approximately 5% for both periods. The increase in absolute dollars was primarily due to an increase in worldwide administrative support needs and headcount related expenses as a result of acquisitions and our continued growth. The increase was also 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

Operating income for the three months ended December 31, 2002, was $66.8 million, compared to $61.8 million in the same period last year. Operating income for the nine months ended December 31, 2002, was $109.3 million, compared to $63.7 million in the same period last year. The increase in operating income for the three months ended December 31, 2002 over the same period last year was due to improvements in our distribution business and, to a lesser degree, our publishing business. Distribution operating income improvement reflects increased control over incremental costs and reductions in headcount related expenses. The increase in operating income for the nine months ended December 31, 2002 over the same period last year was primarily due to an increase in the success of our publishing business due to the benefits generated by cross-platform releases and our continued focus on building operating efficiencies and controlling costs.

Investment Income, Net

Investment income, net for the three months ended December 31, 2002 was $2.5 million as compared to $0.3 million for the three months ended December 31, 2001. Investment income, net for the nine months ended December 31, 2002 was $6.6 million as compared to $1.9 million for the nine months ended December 31, 2001. These increases were primarily due to higher average cash and short-term investment balances. For the nine months ended December 31, 2002, the increase was partially offset by lower interest rates.

Provision for Income Taxes

The income tax provision of $24.9 million and $41.7 million for the three and nine months ended December 31, 2002, respectively, reflects our effective income tax rate of approximately 36%. The significant item that generated the variance between our effective rate and our statutory rate of 35% was state taxes, partially offset by research and development tax credits. 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.

Liquidity and Capital Resources

As of December 31, 2002, our primary source of liquidity is comprised of $359.0 million of cash and cash equivalents and $169.9 million of short-term investments. We believe that we have sufficient working capital ($617.1 million at December 31, 2002), as well as proceeds available from our international credit facilities (described below), 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. 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 and as to our ability to make such acquisitions.

Cash Flows

Our cash and cash equivalents were $359.0 million at December 31, 2002 compared to $279.0 million at March 31, 2002. This $80.0 million increase in cash and cash equivalents for the nine months ended December 31, 2002, included $49.1 million and $222.3 million provided by operating and financing activities, respectively, offset by $198.4 million utilized in investing activities. The principal components comprising cash flows from operating activities included favorable operating results, tax benefits from stock option and warrant exercises and seasonal increases in accounts payable, partially offset by our continued investment in software development and intellectual property licenses and seasonal increases in accounts receivable. Approximately $123.4 million was expended in the nine months ended December 31, 2002 in connection with the acquisition of publishing or distribution rights to 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. The cash used in investing activities primarily was the result of the investment of excess cash balances into 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. Cash used in investing activities was also the result of business combinations and equipment purchases. On 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 249,190 shares of our common stock valued at approximately $8.2 million. Then, on October 4, 2002, we acquired all of the outstanding ownership interests of Luxoflux Corp. ("Luxoflux"), a privately held interactive software development company, in exchange for $9.0 million in cash.

The cash provided by financing activities primarily is the result of proceeds from the June 7, 2002 issuance of 7,500,000 shares of our common stock for proceeds of approximately $247.3 million, net of offering costs, partially offset by cash used to purchase treasury stock and enter into structured stock repurchase transactions. On October 4, 2002, our Board of Directors authorized a buyback program under which we can repurchase up to $150.0 million of our common stock. Under the program, shares may be purchased as determined by management from time to time in the open market or in privately negotiated transactions, including privately negotiated structured option 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. As of December 31, 2002, we had repurchased approximately 1.8 million shares of our common stock at an average cost of $13.15 per share for which $18.9 million was settled in cash as of December 31, 2002 and $5.0 million was settled in cash in January 2003. Additionally, under the Board approved buyback program, we entered into a series of structured stock repurchase transactions in the aggregate amount of $25.0 million. These transactions may be settled in cash or stock based on the market price of our common stock on the date of the settlement. Upon settlement, we will either have our capital investment returned with a premium or receive up to approximately 2.1 million 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.

Credit Facilities

In June 1999, we obtained a $100.0 million revolving credit facility and a $25.0 million term loan with a syndicate of banks (the "U.S. Facility"). The revolving portion of the U.S. Facility provided us with the ability to borrow up to $100.0 million, including issuing letters of credit up to $80.0 million, on a revolving basis against eligible accounts receivable and inventory. The term loan had a three-year term with principal amortization on a straight-line quarterly basis beginning December 31, 1999, a borrowing rate based on the banks' base rate (which was generally equivalent to the published prime rate) plus 2% or LIBOR plus 3% and was to expire June 2002. The revolving portion of the U.S. Facility had a borrowing rate based on the banks' base rate plus 1.75% or LIBOR plus 2.75%. In

May 2001, we accelerated our repayment of the outstanding balance under the term loan portion of the U.S. Facility. In connection with the accelerated repayment, we amended the U.S. Facility (the "Amended and Restated U.S. Facility"). The Amended and Restated U.S. Facility eliminated the term loan, reduced the revolver to $78.0 million and reduced the interest rate to the banks' base rate plus 1.25% or LIBOR plus 2.25%. The Amended and Restated U.S. Facility was collateralized by substantially all of our assets and expired in August 2002. Due to our improved financial position, including significant cash, cash equivalent and short-term investment balances and minimal debt, we did not seek additional bank financing upon the expiration of the Amended and Restated U.S. Facility.

We have a revolving credit facility through our CD Contact subsidiary in the Netherlands (the "Netherlands Facility"). The Netherlands Facility permitted revolving credit loans and letters of credit up to Euro ("EUR") 2.5 million ($2.6 million) as of December 31, 2002, based upon eligible accounts receivable balances. The Netherlands Facility is due on demand, bears interest at a Eurocurrency rate plus 1.25%, is collateralized by the subsidiary's accounts receivable and inventory and a EUR 0.5 million ($0.5 million) guarantee made by our Centresoft subsidiary through its bank facility and expires August 2003. As of December 31, 2002, there were no borrowings or letters of credit outstanding under the Netherlands Facility.

We also have revolving credit facilities with our CentreSoft subsidiary located in the United Kingdom (the "UK Facility") and our NBG subsidiary located in Germany (the "German Facility"). As of December 31, 2002, the UK Facility provided Centresoft with the ability to borrow up to Great British Pounds ("GBP") 8.0 million ($12.8 million), including issuing letters of credit, on a revolving basis. Furthermore, as of December 31, 2002, under the UK Facility, Centresoft provided a EUR 0.5 million ($0.5 million) guarantee which served as collateral for the Netherlands Facility. The UK Facility bears interest at LIBOR plus 1.5%, is collateralized by substantially all of the assets of the subsidiary and expires in October 2003. The UK Facility also contains various covenants that require the subsidiary to maintain specified financial ratios related to, among others, fixed charges. As of December 31, 2002, we were in compliance with these covenants. No borrowings were outstanding against the UK Facility as of December 31, 2002. The German Facility provided for revolving loans up to EUR 0.8 million ($0.8 million) as of December 31, 2002, bears interest at a Eurocurrency rate plus 2.5%, is collateralized by the subsidiary's accounts receivable, inventory and certain property and equipment and expires June 2003. No borrowings were outstanding against the German Facility as of December 31, 2002.

Commitments

In connection with our purchases of Nintendo GameCube and Game Boy software for distribution in North America and Europe, Nintendo requires us to provide either standby letters of credit or cash prepayment prior to accepting purchase orders.

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. Assuming all contractual provisions are met, the total future minimum contract commitment for contracts in place as of December 31, 2002 is approximately $135.4 million and is scheduled to be paid as follows (amounts in thousands):

Fiscal year ending March 31,		
2003	$	23,681
2004		71,050
2005		19,991
2006		12,300
2007 and thereafter		8,425
Total	$	135,447

Recently Issued Accounting Standards

In June 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 requires that the liability for costs associated with an exit or disposal activity be initially measured at fair value and recognized when the liability is incurred. The provisions of SFAS No. 146 are required to be applied prospectively to exit or disposal activities initiated after December 31, 2002.

In January 2003, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure, an amendment of FASB Statement No. 123." SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. It also requires disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for annual and interim periods beginning after December 15, 2002. As we have elected not to change to the fair value based method of accounting for stock-based employee compensation, the adoption of SFAS No. 148 will not have an impact upon our financial condition or results of operations.

Factors Affecting Future Performance

In connection with the Private Securities Litigation Reform Act of 1995 (the "Litigation Reform Act"), we have disclosed certain cautionary information to be used in connection with written materials (including this Quarterly Report on Form 10-Q) and oral statements made by or on behalf of our employees and representatives that may contain "forward-looking statements" within the meaning of the Litigation Reform Act. Such statements consist of any statement other than a recitation of historical fact and can be identified by the use of forward-looking terminology such as "may," "expect," "anticipate," "estimate" or "continue" or the negative thereof or other variations thereon or comparable terminology. The listener or reader is cautioned that all forward-looking statements are necessarily speculative and there are numerous risks and uncertainties that could cause actual events or results to differ materially from those referred to in such forward-looking statements. For a discussion that highlights some of the more important risks identified by management, but which should not be assumed to be the only factors that could affect future performance, see our Annual Report on Form 10-K for the fiscal year ended March 31, 2002 which is incorporated herein by reference. The reader or listener is cautioned that we do not have a policy of updating or revising forward-looking statements and thus he or she should not assume that silence by management over time means that actual events are bearing out as estimated in such forward-looking statements.

Item 3. 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 and foreign currency exchange rates. Our market risk sensitive instruments are classified as "other than trading." Our exposure to market risk as discussed below includes "forward-looking statements" and represents an estimate of possible changes in fair value or future earnings that would occur assuming hypothetical future movements in interest rates or foreign currency exchange rates. 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 foreign currency exchange rates, interest rates 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 December 31, 2002, our cash equivalents and short-term investments included debt securities of $280.0 million.

The following table presents the amounts and related weighted average interest rates of our investment portfolio as of December 31, 2002 (amounts in thousands):

	Average Interest Rate	Amortized Cost	Fair Value
Cash equivalents			
Fixed rate	1.63%	$ 110,141	$ 110,078
Variable rate	1.32	110,992	110,992
Short-term investments			
Fixed rate	2.47%	$ 169,313	$ 169,874

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 December 31, 2002, we had no material outstanding hedging contracts.

Market Price Risk

With regard to the structured stock repurchase transactions described in Note 15 in the Notes to the Consolidated Financial Statements, it is possible that at settlement we could take delivery of shares at an effective repurchase price higher than the then market price.

Item 4. Controls and Procedures

Within 90 days prior to the date of this report, we carried out an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information required to be included in our periodic reports filed with the Securities and Exchange Commission. In addition, we reviewed our internal controls, and there have been no significant changes in our internal controls or in other factors that could significantly affect those internal controls subsequent to the date we carried out our last evaluation.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

We are party to 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, the outcome of such routine claims will not have a material adverse effect on our business, financial condition or results of operations.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

1.1	Underwriting agreement between Activision and Goldman, Sachs & Co. dated June 4, 2002 (incorporated by reference to Exhibit 1.1 of Activision's 8-K, filed June 6, 2002).
3.1	Amended and Restated Certificate of Incorporation, dated June 1, 2000 (incorporated by reference to Exhibit 2.5 of our Current Report on Form 8-K, filed on June 16, 2000).
3.2	Certificate of Amendment of Amended and Restated Certificate of Incorporation, dated June 9, 2000 (incorporated by reference to Exhibit 2.7 of our Current Report on Form 8-K, filed on June 16, 2000).
3.3	Certificate of Amendment of Amended and Restated Certificate of Incorporation, dated August 23, 2001 (incorporated by reference to Exhibit 3.3 of Amendment No. 1 to our Registration Statement on Form S-3, Registration No. 333-66280, filed on August 31, 2001).
3.4	Certificate of Designation of Series A Junior Preferred Stock, dated December 27, 2001 (incorporated by reference to Exhibit 3.4 of our Quarterly Report on Form 10-Q for the quarterly period ended December 31, 2001).
3.5	Amended and Restated By-laws dated August 1, 2000 (incorporated by reference to Exhibit 3.2 of our Current Report on Form 8-K, filed July 11, 2001).
4.1	Rights Agreement dated as of April 18, 2000, between us and Continental Stock Transfer & Trust Company, which includes as exhibits the form of Right Certificates as Exhibit A, the Summary of Rights to Purchase Series A Junior Preferred Stock as Exhibit B and the form of Certificate of Designation of Series A Junior Preferred Stock of Activision as Exhibit C (incorporated by reference to our Registration Statement on Form 8-A, Registration No. 001-15839, filed April 19, 2000).
10.1	Employment agreement dated November 20, 2002, between Activision Publishing, Inc. and George Rose.
10.2	Activision, Inc. 2002 Studio Employee Retention Incentive Plan.
99.1	Certification of Robert A. Kotick pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.2	Certification of Ronald Doornink pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.3	Certification of William J. Chardavoyne pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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(b) Reports on Form 8-K

1.1	

We filed a Form 8-K on October 11, 2002, reporting under "Item 7. Financial Statements, Pro Forma Financial Statements and Exhibits" and "Item 9. Regulation FD Disclosure" issuing a press release announcing a buyback program under which we can repurchase up to $150 million of our common stock and issuing a press release announcing our acquisition of Luxoflux Corporation.

1.2 We filed a Form 8-K on December 17, 2002, reporting under "Item 7. Financial Statements, Pro Forma Financial Statements and Exhibits" and "Item 9. Regulation FD Disclosure" issuing a press release announcing revenue and earnings guidance for the third and fourth fiscal quarters for the 2003 fiscal year and for the full 2003 and 2004 fiscal years.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: January 31, 2003

ACTIVISION, INC.

/s/ WILLIAM J. CHARDAVOYNE

William J. Chardavoyne
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

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CERTIFICATIONS

CERTIFICATION

I, Robert A. Kotick, Chairman and Chief Executive Officer of Activision, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Activision, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

    a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: January 31, 2003

/s/ ROBERT A. KOTICK

Robert A. Kotick
Chairman and Chief Executive Officer

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CERTIFICATION

I, Ronald Doornink, President of Activision Inc., and Chief Executive Officer of Activision Publishing, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Activision, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4.

The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: January 31, 2003

/s/ RONALD DOORNINK

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

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CERTIFICATION

I, William J. Chardavoyne, Executive Vice President and Chief Financial Officer of Activision, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Activision, Inc.;

2.

Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

   c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: January 31, 2003

/s/ WILLIAM J. CHARDAVOYNE

William J. Chardavoyne
Executive Vice President and Chief Financial Officer

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