Quarterly Report 3 / 2010

Zapf Creation AG
Mönchrödener Straße 13
96472 Rödental
GERMANY

Phone: +49 (0) 9563/72 51 – 0
Fax: +49 (0) 9563/72 51 – 116
E-mail: info@zapf-creation.de
Internet: www.zapf-creation.de

Key Figures for the Group (IFRS)	Q3/2010 € million	Q3/2009 € million	Q1-Q3/2010 € million	Q1-Q3/2009 € million	Q1-Q3 + / - %	FY/2009 € million
Adjusted financial performance (excluding restructuring costs and one-off items)						
Continuing operations						
EBITDA	7.1	7.4	4.9	0.5	>100	-0.6
EBIT	6.3	6.4	2.4	-2.3	-	-4.5
EBIT margin (%)	22.3	22.9	4.7	-4.8	-	-5.6
EBT	5.4	5.6	-0.5	-5.1	90	-9.5
Net profit (loss) from continuing operations	4.5	4.9	-0.5	-4.5	89	-11.0
Discontinued operations						
Net profit (loss) from discontinued operations	-0.6	-0.2	0.3	0.0	>100	0.0
Group						
Net profit (loss) for the period	3.9	4.7	-0.2	-4.4	96	-10.9
Earnings per share (€) 1)	0.21	0.25	-0.01	-0.24	96	-0.58
Financial performance as reported on the income statement (including restructuring costs and one-off items)						
Continuing operations						
Sales revenue	28.2	28.0	50.5	47.7	6	79.3
Gross margin (%)	40.8	44.8	40.2	38.3	-	37.1
EBITDA	7.0	7.4	3.7	0.5	>100	-0.8
EBIT	6.2	6.4	1.2	-2.3	-	-4.6
EBIT margin (%)	21.9	22.9	2.3	-4.8	-	-5.8
EBT	5.3	5.6	-1.7	-5.1	66	-9.6
Net profit (loss) from continuing operations	4.4	4.9	-1.7	-4.5	61	-11.1
Restructuring costs and one-off items included	0.1	0.0	1.2	0.0	-	0.1
Depreciation and amortization expense included	0.8	1.0	2.6	2.8	-9	3.8
Discontinued operations						
Net profit (loss) from discontinued operations	-0.6	-0.2	0.3	0.0	>100	0.0
Restructuring costs and one-off items included	0.0	0.0	0.0	0.0	-	0.0
Depreciation and amortization expense included	0.0	0.0	0.0	0.0	-	0.0
Group						
Net profit (loss) for the period	3.8	4.7	-1.4	-4.4	69	-11.1
Earnings per share (€) 1)	0.20	0.25	-0.07	-0.24	69	-0.59
Balance sheet						
Total assets	-	-	67.7	79.3	-15	75.7
Non-current assets	-	-	16.8	20.4	-18	18.8
Capital expenditure	0.3	0.2	0.7	0.8	-13	1.2
Current assets	-	-	50.9	58.9	-14	56.9
Equity	-	-	11.0	19.0	-42	12.5
Equity ratio (%)	-	-	16.3	24.0	-	16.5
Liabilities to banks	-	-	28.5	32.0	-11	33.3
Net debt	-	-	21.8	25.4	-14	25.3
Cash flow						
Cash flow from operating activities	-2.1	-2.6	6.6	5.9	13	8.4
Cash flow from operating activities per share (€)	-0.11	-0.14	0.35	0.31	12	0.45
Net cash flow	-3.1	-3.4	-1.3	-0.9	-51	0.5
Employees						
Number of employees as at the balance sheet date 2)	-	-	161	219	-26	224

The figures for the 2010 financial yyear to date have been prepared on a going-concern basis.
The Consolidated Financial Statements for the year ended December 31, 2009 so far have been prepared in preliminary form only and have not yet been published; for additional disclosures please refer to the Group Management Report and Notes.
1) Basic = diluted; 2) Excluding Management Board and trainees
The key figures have been rounded and are shown in millions of euros. This may result in some discrepancies in totals and ratios compared with the interim consolidated financial statements.

Interim Group Management Report for the Period ended September 30, 2010

1. Summary

The Zapf Creation Group's performance in the first nine months of 2010 was better than the corresponding period 2009. Sales revenue increased. Further strategic development of the Group and the savings achieved had a positive impact on financial performance and liquidity.

2. Significant Events of the Reporting Period

Significant events during the first nine months of 2010 were the negotiations with the syndicate of banks and the changes to the Management Board personnel. For further information, please refer to the detailed reports on these items in the 2010 half-yearly report.

3. Performance of the Zapf Creation Group

3.1. Important Note

The consolidated December 31, 2009 financial statements of the Zapf Creation Group were only available in draft form and as yet had not been audited at the time this quarterly report was prepared. The reasons for this were the negotiations with the syndicate of lending banks – which were still ongoing as of September 30, 2010 – regarding the adjustment of the Group's long-term financing arrangements.

The following disclosures on performance indicators for 2009 are published here subject to the proviso that they still need to be retroactively confirmed by the independent auditors.

3.2. Sales Revenue Performance

In the first nine months of 2010, sales revenue in the Zapf Creation Group climbed by 5.9 percent year on year to €50.5 million (Q1-Q3 2009: €47.7 million). In Q3 the Zapf Creation Group achieved growth of 0.5 percent to €28.2 million (Q3 2009: €28.0 million).

3.3. Earnings Performance

The gross profit achieved in the first nine months of 2010 rose to €20.3 million (Q1-Q3 2009: €18.3 million), an increase of 11.2 percent and therefore better than the increase in sales revenue. As a result, the gross profit margin in the Zapf Creation Group climbed to 40.2 percent compared with 38.3 percent in the first nine months of 2009. This positive trend was attributable to lower procurement costs and the high-margin product categories. In the third quarter of 2010 the gross profit margin was 40.8 percent (Q3 2009: 44.8 percent). This drop is largely attributable to the dramatic hike in freight costs since the beginning of July.

The Group succeeded in reducing its overall operating expenses in Q3 2010. Notable savings were achieved in sales and distribution expenses. Marketing and administrative expenses were also reduced.

Earnings before interest and tax (EBIT) for the nine months of the period under review improved by €3.4 million to €1.2 million (Q1-Q3 2009: minus €2.3 million). Adjusted for one-off items (largely severance pay) and restructuring costs, consolidated EBIT amounted to €2.4 million (Q1-Q3 2009: minus €2.3 million). In Q3 2010, the Group generated an EBIT figure of €6.2 million (adjusted: €6.3 million) as against €6.4 million in Q3 2009.

With a slight deterioration in net finance costs, the loss before tax from continuing operations for the first nine months of 2010 amounted to €1.7 million (Q1-Q3 2009: loss of €5.1 million) - Q3 profit €5.3 million (Q3 2009: profit of €5.6 million). The loss after tax from continuing operations improved to €1.7 million (Q1-Q3 2009: loss of €4.5 million); the prior year figure had also benefited from a tax credit. The drop in profit in Q3 to €4.4 million (Q3 2009: €4.9 million) was largely attributable to the effects of exchange rate movements, as described above.

The profit from discontinued operations for the first nine months of 2010 amounted to €0.35 million (Q1-Q3 2009: €0.01 million), although the third quarter registered a loss of €0.6 million (Q3 2009: loss of €0.2 million). The figures represent the measurement of a loan as at the balance sheet date from Zapf Creation AG to its US subsidiary which had ceased operations on December 31, 2006.

The net loss for the first nine months of 2010 improved to €1.4 million (Q1-Q3 2009: loss of €4.4 million); in Q3 there was a net profit of €3.8 million (Q3 2009: €4.7 million). Earnings per share for the first nine months of 2010 were minus €0.07 (Q1-Q3 2009: minus €0.24), and for Q3 alone plus €0.20 (Q3 2009: plus €0.25).

3.4. Financial Position

As of September 30, 2010, total assets in the Zapf Creation Group reduced to €67.7 million (December 31, 2009: €75.7 million; September 30, 2009: €79.3 million). On the same balance sheet date, non-current assets had decreased to €16.8 million (December 31, 2009: €18.8 million; September 30, 2009: €20.4 million).

Current assets decreased to €50.9 million as of September 30, 2010 (December 31, 2009: €56.9 million; September 30, 2009: €58.9 million). Cash and cash equivalents amounted to €6.6 million compared with €8.0 million as of December 31, 2009 and €6.5 million as of September 30, 2009.

Current liabilities as of September 30, 2010 declined to €56.6 million (December 31, 2009: €63.2 million; September 30, 2009: €60.3 million). This was largely attributable to the change in short-term bank debt, which the Group reduced to €28.5 million (December 31, 2009: €33.3 million; September 30, 2009: €32.0 million). Trade payables amounted to €23.2 million (December 31, 2009: €21.8 million; September 30, 2009: €23.9 million).

As of September 30, 2010, net debt had been reduced to €21.8 million (December 31, 2009: €25.3 million; September 30, 2009: €25.4 million). Equity as of September 30, 2010 had decreased to €11.0 million (December 31, 2009: €12.5 million; September 30, 2009: €19.0 million). The equity ratio as of September 30, 2010 was 16.3 percent compared with 16.5 percent as of December 31, 2009 and 24.0 percent on the equivalent date in 2009.

There was an improvement in liquidity year on year over the first nine months of 2010. Cash flow from operating activities increased to €6.6 million (Q1-Q3 2009: €5.9 million). This allowed the Group to increase its repayments of loan principal, reflected in an increase in the net cash used for financing activities to €7.8 million (Q1-Q3 2009: net cash used of €6.2 million). The net cash used for investing activities was reduced to €0.3 million (Q1-Q3 2009: net cash used of €0.8 million).

4. Significant Events after the Balance Sheet Date

On October 4, 2010, Zapf Creation AG successfully concluded negotiations to secure the long-term funding of the Group by signing an agreement in principle. Investors have been found who will replace a bank loan amounting to €20.1 million. The replacement loan, the terms of which will be aligned with the needs of the Company, will mature in 2013. These new arrangements reduce the remaining outstanding loan with the syndicate of banks to just €9.0 million (Term Loan); this outstanding loan amount will be repaid early and in full by January 31, 2011.

The Supervisory Board of Zapf Creation AG has appointed Mr. Jaime Ferri Llorens as member of the Management Board as per January 1, 2011 and as Chairman of the Management Board as per February 16, 2011. As planned he will succeed Mr. Ron Oboler, who has managed the Company on an interim basis since Februar 2010 and who will fully concentrate on his current position as Executive Vice President International with MGA Entertainment, Inc. from February 16, 2011 onwards.

5. Opportunities and Risks

The Zapf Creation Group provided comprehensive detailed information regarding opportunities and risks in the combined management report of Zapf Creation AG and the Group for the 2008 financial year. There has been no material change in the Group's opportunities and risk profile since the disclosures made in that report. Therefore, please refer to the disclosures in the report concerned for further information.

However, the following risk should be noted:

Following the signing of the agreement in principle for the replacement of bank loans amounting to

€20.1 million, the additional risks arising from the failure to comply with the covenants from the fourth quarter of 2008 onward have been mitigated. The residual outstanding bank loan amount of just €9 million is to be repaid early and in full by January 31, 2011.

6. Outlook

The Management Board remains convinced that financial performance for the full year 2010 will represent an improvement over 2009. The long-term funding arrangements for the Group secured at the start of October 2010 are of immense importance for the future of the business. With these new foundations, we can continue to systematically drive forward the process that we have already initiated, namely to develop the Group into an international provider of toys for girls.

Rödental, November 10, 2010

Ron Oboler	Ron Brawer	José Antonio Santana
Chairman of the Management Board	Member of the Management Board	Member of the Management Board

Zapf Creation AG
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Consolidated Income Statement
for the Period January 1, 2010 to September 30, 2010

	Q3/2010 €'000	**Q3/2009 €'000**	**Q1-Q3/2010 €'000**	**Q1-Q3/2009 €'000**	**FY/2009 €'000**
Sales revenue	28,184	28,046	50,485	47,664	79,331
Cost of sales	-16,672	-15,485	-30,174	-29,391	-49,936
Gross profit	**11,512**	**12,561**	**20,311**	**18,273**	**29,395**
Sales and distribution expenses	-1,854	-2,719	-6,844	-7,794	-11,520
Marketing expenses	-963	-1,114	-3,225	-3,799	-9,882
Administrative expenses	-2,975	-3,250	-10,318	-9,817	-14,890
Other income	549	591	1,514	1,676	3,495
Other expenses	-96	342	-286	-831	-1,195
Profit (loss) from operations	**6,173**	**6,411**	**1,152**	**-2,292**	**-4,597**
(of which restructuring costs	*-101*	*0*	*-1,216*	*0*	*-137)*
(of which one-off costs, mainly consultancy	*0*	*0*	*0*	*0*	*0)*
(resulting adjusted profit (loss) from operations	*6,274*	*6,411*	*2,368*	*-2,292*	*-4,460)*
Financial income	14	8	63	58	64
Finance costs	-935	-833	-2,925	-2,841	-5,076
Profit (loss) before tax from continuing operations	**5,252**	**5,586**	**-1,710**	**-5,075**	**-9,609**
Income taxes	-893	-722	-17	623	-1,504
Profit (loss) after tax from continuing operations	**4,359**	**4,864**	**-1,727**	**-4,452**	**-11,113**
Profit (loss) before tax from discontinued operations	-552	-167	346	6	47
Income taxes on discontinued operations	0	0	0	0	0
Net profit (loss) for the period	**3,807**	**4,697**	**-1,381**	**-4,446**	**-11,066**

	Q3/2010 €	**Q3/2009 €**	**Q1-Q3/2010 €**	**Q1-Q3/2009 €**	**GJ/2009 €**
Average number of shares outstanding (thousands)	18,803	18,723	18,803	18,723	18,725
Earnings per share from continuing operations	0.23	0.26	-0.09	-0.24	-0.59
Earnings per share from discontinued operations	-0.03	-0.01	0.02	0.00	0.00
Earnings per share (basic/diluted)	**0.20**	**0.25**	**-0.07**	**-0.24**	**-0.59**

The Notes form an integral part of the Interim Consolidated Financial Statements

The Consolidated Financial Statements for the year ended December 31, 2009 so far have been prepared in preliminary form only and have not yet been published;
for additional disclosures please refer to the Group Management Report and Notes.

Zapf Creation AG
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Consolidated Statement of Comprehensive Income
for the Period January 1, 2010 to September 30, 2010

	Q3/2010 €'000	Q3/2009 €'000	Q1-Q3/2010 €'000	Q1-Q3/2009 €'000	FY/2009 €'000
Net profit (loss) for the period	**3,807**	**4,697**	**-1,381**	**-4,446**	**-11,066**
Adjustment from currency translation	23	-552	131	945	1,125
Deferred taxes	160	226	-130	-217	-296
Derivative financial instruments	0	0	0	0	0
Other comprehensive income (loss)	**183**	**-326**	**1**	**728**	**829**
Comprehensive income (loss) for the period	**3,990**	**4,371**	**-1,380**	**-3,718**	**-10,237**

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Consolidated Balance Sheet as of September 30, 2010

Assets	Sep. 30, 2010 €'000	Dec. 31, 2009 €'000	Sep. 30, 2009 €'000
Current assets	**50,905**	**56,877**	**58,914**
Cash and cash equivalents	6,636	7,971	6,543
Trade receivables	25,749	35,746	28,028
Inventories	12,577	5,668	15,789
Income tax assets	116	627	599
Other assets	5,827	6,865	7,955
Non-current assets	**16,771**	**18,803**	**20,395**
Property, plant and equipment	11,792	13,315	13,884
Intangible assets	4,049	4,692	4,907
Other assets	0	0	0
Deferred tax assets	930	796	1,604
Total assets	**67,676**	**75,680**	**79,309**

Equity and liabilities	Sep. 30, 2010 €'000	Dec. 31, 2009 €'000	Sep. 30, 2009 €'000
Current liabilities	**56,616**	**63,209**	**60,273**
Liabilities to banks	28,485	33,311	31,974
Trade payables	23,199	21,806	23,917
Income tax liabilities	2,118	2,464	1,433
Other liabilities	2,178	3,204	2,194
Provisions	636	2,424	755
Non-current liabilities	**48**	**18**	**36**
Liabilities to banks	0	0	0
Deferred tax liabilities	48	18	36
Equity	**11,012**	**12,453**	**19,000**
Subscribed capital	19,296	19,296	19,296
Capital reserves	31,698	31,759	33,374
Profit (loss) for the period and profit (loss) brought forward	-28,594	-27,213	-20,593
Accumulated other comprehensive income (loss)	-1,617	-1,618	-1,719
Treasury shares	-9,771	-9,771	-11,358
Total equity and liabilities	**67,676**	**75,680**	**79,309**

The Notes form an integral part of the Interim Consolidated Financial Statements

The Consolidated Financial Statements for the year ended December 31, 2009 so far have been prepared in preliminary form only and have not yet been published; for additional disclosures please refer to the Group Management Report and Notes.

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Consolidated Statement of Changes in Equity for the Period January 1, 2010 to September 30, 2010

	Outstanding shares (thousands)	Subscribed capital €'000	Capital reserves €'000	Net profit (loss) for the period and profit (loss) brought forward €'000	Accumulated other comprehensive income (loss): Adjustment from currency translation €'000	Accumulated other comprehensive income (loss): Derivative financial instruments €'000	Treasury shares €'000	Total equity €'000
Balance as at January 1, 2009	**18,723**	**19,296**	**33,240**	**-16,147**	**-2,447**	**0**	**-11,358**	**22,584**
Net profit (loss) for the period				-4,446				-4,446
Change in other comprehensive income					728	0		728
Comprehensive income (loss) for the period				**-4,446**	**728**	**0**		**-3,718**
Share-based payment			134					134
Balance as at September 30, 2009	**18,723**	**19,296**	**33,374**	**-20,593**	**-1,719**	**0**	**-11,358**	**19,000**
Balance as at January 1, 2010	**18,803**	**19,296**	**31,759**	**-27,213**	**-1,618**	**0**	**-9,771**	**12,453**
Net profit (loss) for the period				-1,381				-1,381
Change in other comprehensive income					1	0		1
Comprehensive income (loss) for the period				**-1,381**	**1**	**0**		**-1,380**
Share-based payment			-61					-61
Balance as at September 30, 2010	**18,803**	**19,296**	**31,698**	**-28,594**	**-1,617**	**0**	**-9,771**	**11,012**

The Notes form an integral part of the Interim Consolidated Financial Statements

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Consolidated Cash Flow Statement
for the Period January 1, 2010 to September 30, 2010

	Q1-Q3/2010 €'000	Q1-Q3/2009 €'000
Cash flow from operating activities:		
Loss before tax	-1,364	-5,069
Depreciation and amortization expense	2,564	2,821
Gains/losses from the disposal of non-current assets	-85	4
Net finance costs	2,862	2,783
Share-based payment	-61	134
Other non-cash income and expenses	0	0
Increase/decrease in assets and liabilities:		
Trade receivables	9,994	19,540
Inventories	-6,909	-3,370
Other assets	1,024	-2,793
Liabilities and provisions	-1,314	-7,747
Income taxes paid	-86	-415
Cash flow from operating activities	**6,625**	**5,888**
Cash flow from investing activities:		
Proceeds from the disposal of property, plant and equipment, and intangible assets	417	19
Payments to acquire property, plant and equipment, and intangible assets	-728	-841
Cash flow from investing activities	**-311**	**-822**
Cash flow from financing activities:		
Proceeds from bank borrowings	0	0
Payments in connection with liabilities to banks and other fees	-537	-22
Repayments of liabilities to banks	-2,247	-2,000
Changes in liabilities related to drawdowns under short-term borrowing facilities	-2,432	-1,806
Interest paid	-2,627	-2,454
Interest received	61	53
Issuance of treasury shares	0	0
Cash flow from financing activities	**-7,782**	**-6,229**
Effects of changes in exchange rates	133	281
Net change in cash and cash equivalents	**-1,335**	**-882**
Cash and cash equivalents at the beginning of the period	7,971	7,425
Cash and cash equivalents at the end of the period	6,636	6,543

The Notes form an integral part of the Interim Consolidated Financial Statements
The Consolidated Financial Statements for the year ended December 31, 2009 so far have been prepared in preliminary form only and have not yet been published; for additional disclosures please refer to the Group Management Report and Notes.

Zapf Creation AG

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Notes to the
Interim Consolidated Financial Statements
for the Period ended September 30, 2010

Contents:

1. General Disclosures

1.1. Information on the Company

Zapf Creation AG – hereinafter also referred to as 'Company' or 'Zapf Creation' – is Europe's leading brand manufacturer of play and functional dolls including accessories.

The Company markets branded play concepts that consist of a doll and a world of matching accessories as well as themed play sets and collectable figures developed to a high standard of quality, design, safety and play value. The Company's most popular brands include BABY born®, Baby Annabell®, and CHOU CHOU. These globally successful play concepts have been conceived particularly for the Company's core target group – girls between three and eight years of age.

Zapf Creation AG, as the Company is now known, was originally established as 'Max Zapf Puppen- und Spielwarenfabrik' in Rödental by Max Zapf and his wife Rosa in 1932. The initial public offering for the Company took place on April 26, 1999. Zapf Creation AG is listed on the Official Market of the Frankfurt Stock Exchange in the Prime Standard segment.

The registered office of Zapf Creation AG is situated in Germany at Mönchrödener Strasse 13, 96472 Rödental.

1.2. Basis of Presentation

The interim consolidated financial statements of Zapf Creation AG for the period ended September 30, 2010 have been prepared on the basis of IAS 34 ("Interim Financial Reporting"). They have not been reviewed by an auditor or audited in accordance with section 317 German Commercial Code (HGB).

The interim consolidated financial statements do not contain all the notes and disclosures required for consolidated financial statements and must therefore be read in conjunction with the consolidated financial statements for the year ended December 31, 2009, which were prepared, as required by section 315a HGB ("Consolidated financial statements in accordance with international accounting standards"), in accordance with the International Financial Reporting Standards (IFRS) published by the International Accounting Standards Board (IASB) and the associated pronouncements of the International Financial Reporting Interpretations Committee (IFRIC), as adopted by the European Union (EU) in accordance with article 4 of Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of July 19, 2002. The requirements specified by section 315a (1) HGB were also observed in the preparation of these consolidated financial statements. All IFRSs and associated interpretations adopted by the EU that were mandatory for the 2009 financial year were applied in the consolidated financial statements of Zapf Creation AG for the year ended December 31, 2009.

At the time of this publication, the consolidated financial statements of Zapf Creation AG for the year ended December 31, 2009 have been prepared in preliminary form only and are not yet published. As a result, events within the meaning of IAS 10 ("Events after the Balance Sheet Date") might subsequently arise that could have an impact on the consolidated financial statements for the year ended December 31, 2009; any necessary changes in this regard would also cause changes to the values in the opening balance sheet of the interim consolidated financial statements for the period ended September 30, 2010.

1.3. Consolidation

The basis of consolidation in the interim consolidated financial statements for the period ended September 30, 2010 is the same as that applied in the preliminary consolidated financial statements for the year ended December 31, 2009 which have not yet been published; for further information, please refer to the consolidated financial statements for the year ended December 31, 2008 which were prepared using the same basis of consolidation.

In addition to Zapf Creation AG, which is the parent company in the Group, the basis of consolidation includes all the parent company's direct and indirect subsidiaries. During the first nine months of 2010, the following change took place in the basis of consolidation: the merger of the French subsidiary Zapf Creation (France) S.à.r.l. into Zapf Creation AG came into effect at the end of August 31, 2010. Zapf Creation (France) S.à.r.l. was wound up at this point; Zapf Creation AG is the legal successor to this subsidiary in all respects.

1.4. Accounting Policies

The accounting policies applied in the interim consolidated financial statements for the period ended September 30, 2010 are the same as those applied in the preliminary consolidated financial statements for the year ended December 31, 2009 which have not yet been published;

for further information, please refer to the consolidated financial statements for the year ended December 31, 2008 which were prepared using the same accounting policies.

As a result, in addition to reporting profit (loss) from operations, the Zapf Creation Group has also reported an adjusted profit (loss) from operations figure in the consolidated income statement forming part of the interim consolidated financial statements for the period ended September 30, 2010. The adjusted profit (loss) from operations eliminates the restructuring costs and one-off items included in profit (loss) from operations and reflects the performance indicators used internally within the Group. The purpose of reporting this figure in the consolidated income statement is to increase transparency as regards the sustainability of the operating profit generated by the Company from its ongoing operating business. Any restructuring expenses incurred in the Zapf Creation Group, together with other particular one-off expense items, are allocated in the income statement to the function area responsible for incurring the costs concerned. In the period under review, there were restructuring expenses of €1.216 million; there were no one-off items. Neither restructuring expenses nor one-off costs were incurred in the corresponding period in 2009.

Recognition and measurement in the interim consolidated financial statements for the period ended September 30, 2010 and in the preliminary consolidated financial statements for the year ended December 31, 2009 which have not yet been published are based on the assumption that the Zapf Creation Group will continue as a going concern. At the present time, the Management Board of Zapf Creation AG is operating on the assumption that the business remains a going concern.

1.5. Use of Estimates

The preparation of the interim consolidated financial statements requires the management to make assumptions and estimates that could affect the application of financial reporting standards in the Group, and that could have an impact on the recognition and measurement of assets, liabilities, income, expenses, and contingent liabilities.

The Company's management continuously reviews both the estimates and the underlying assumptions. Although the estimates are based on present events and action taken, and are accurate to the best of the management's knowledge and belief, actual amounts may turn out to be different from these estimates. Adjustments to estimates relevant to accounting are recognized solely in the period of the change if the change only affects the period concerned. If the change affects both the reporting period and subsequent periods, the adjustment is recognized both in the reporting period and in subsequent periods.

2. Consolidated Financial Statements, Disclosures

2.1. General

The classification of the items presented in the interim consolidated financial statements for the period ended September 30, 2010 is the same as the classification in the preliminary consolidated financial statements for the year ended December 31, 2009 which have not yet been published; for further information, please refer to the consolidated financial statements for the year ended December 31, 2008 which were prepared using the same classification.

The trends in the individual items in the consolidated financial statements over the period under review, particularly the changes in the level of sales revenue, reflect the typical seasonal changes in the operating activities of the Company over the course of a year; for further information in this regard, please refer to the interim group management report for the third quarter of 2010.

The segment report is attached to these notes as an ***annex***.

2.2. Discontinued Operations

As in 2009, income and expenses attributable to Zapf Creation (U.S.) Inc., one of the subsidiaries in the Group, are separately reported under profit (loss) from discontinued operations in accordance with IFRS 5 (“Non-current Assets Held for Sale and Discontinued Operations”).

The breakdown of income and expenses attributable to discontinued operations is as follows:

	Q1-Q3/2010	Q1-Q3/2009
	€'000	€'000
Sales revenue	0	32
Administrative expenses	- 12	- 11
Other income	358	0
Other expenses	0	-15
Profit from discontinued operations	346	6

As in the corresponding period in 2009, the profit from discontinued operations in the first nine months of 2010 essentially resulted from the effects of exchange rate movements.

The breakdown of cash flow from operating, investing, and financing activities attributable to discontinued operations is as follows:

	Q1-Q3/2010	Q1-Q3/2009
	€'000	€'000
Cash flow from operating activities	0	- 27
Cash flow from investing activities	0	0
Cash flow from financing activities	0	0
Effects of changes in exchange rates	1	1
Cash flow from discontinued operations	1	- 26

2.3. Other Income Statement Disclosures

In the period under review, the staff costs included in the operating expenses of the Zapf Creation Group amounted to €7.709 million (Q1-Q3 2009: €9.221 million).

The breakdown of staff costs by function of expense is as follows:

	Q1-Q3/2010	Q1-Q3/2009
	€'000	€'000
Sales and distribution	3,412	4,401
Marketing	288	743
Other administration	4,009	4,077
Staff costs	7,709	9,221

2.4. Liabilities to Banks

Under a financing agreement dated November 30, 2007, a syndicated loan with the original principal amount of €65 million was made available to Zapf Creation AG on December 7, 2007 for the purposes of funding its operating business over the short and medium terms.

On October 1, 2009, the existing financing agreement dated November 30, 2007 was amended and replaced to the effect that the banking syndicate would continue to make sufficient credit available to Zapf Creation AG, subject to a temporary time limit until the end of April 2010 (waiver limited in time); the loan volume made available had decreased by €8 million in this connection. The participating banks did not retest the stipulated financial indicators as long as the waiver was in effect; the banks agreed with Zapf Creation to initially waive the fixing of new covenants adjusted to the changed parameters until the end of April 2010. At that point in time, the participating banks once again conducted a review of the Company's overall situation, as agreed. From this point forward, the banks remaining in the consortium stated during the negotiations with the Zapf Creation Group on its long-term financing that they would be willing to waive compliance with the covenants on a month-to-month basis ending June 30, 2010; the lending volume in this connection fell by €17 million as of April 30, 2010, but has been continuing at an adequate volume since then. Although the banks did not prolong the waiver which lapsed on June 30, 2010, the constructive negotiations between the Group and the banks have been carried on; for additional information, please refer to section 4 of the management report (Events after the Balance Sheet Date).

As of September 30, 2010, the residual bank debt after taking into account repayments (excluding interest liabilities and transaction costs) amounted to €29.1 million.

As in 2009, the bank debt as of September 30, 2010 has been reported in full as current liabilities to banks because the Company has not complied with all the covenants agreed in connection with the above funding arrangements. The Company has not been able to comply with the following covenants: the total leverage covenant, a covenant based on the ratio of net debt to EBITDA; the interest coverage covenant, a covenant based on the ratio of EBITDA to net interest expense; and, the equity capital covenant, a covenant based on the ratio of the Zapf Creation Group's equity to total equity and liabilities. However, the Company has been able to comply with the capital expenditure covenant, a covenant based on a performance indicator related to the volume of capital expenditure.

2.5. Equity

Capital measures

As in the equivalent period in 2009, no capital measures were carried out during the first nine months of 2010.

Treasury shares

By resolution of the Annual Shareholders' Meeting dated December 15, 2009, the Company is authorized to purchase treasury shares in order to:

a) be able to offer such shares as consideration in connection with business combinations or the acquisition of companies, business units or equity investments in companies; or

b) issue such shares in return for the transfer to the Company of one or more loan and/or interest payables under loans granted to it; or

c) offer such shares as employee shares to employees of the Company or companies considered its affiliates under Sections 15 et seq. German Stock Corporation Act for purchase or, if employee shares were acquired by way of securities loans or securities lending, for purposes of satisfying obligations thereunder; or

d) grant such shares to members of the Management Board as components of their compensation; or

e) use such shares to fulfill options issued under the authorization resolved by the Annual Shareholders' Meeting on December 15, 2009; or

f) sell repurchased treasury shares in ways other than on the stock exchange or by means of an offering to all shareholders in return for cash at a price that is not substantially lower than the exchange price of the Company's shares of the same class at the time of the disposal; or

g) retire the shares so acquired without another resolution of the Annual Shareholders' Meeting, subject to reduction of the share capital.

The authorization is limited to the purchase of treasury shares having a pro rata share of 10% in the Company's share capital existing on December 15, 2009, the day on which the Annual Shareholders' Meeting adopts the resolution (€19,295,853.00). The treasury shares so acquired — along with other treasury shares that are in the Company's possession or are allocable to it under Section 71a et seq. German Stock Corporation Act — may not, at any time, exceed 10% of the share capital. In addition, any such buyback shall be permitted only if, at the time of the purchase, the Company would be able to recognize reserves equivalent to the amount of the expenditure required for the buyback without reducing the share capital or any reserves that are required under the law or the Company's Articles of Incorporation and may not be used for payments to shareholders.

The authorization to acquire treasury shares shall remain in effect until December 14, 2014 (inclusive). The authorization adopted by the Company's Annual Shareholders' Meeting on May 27, 2008, to use the treasury shares that the Company is already holding at the time the Annual Shareholders' Meeting adopts its resolutions on May 27, 2008, expire at the time this new authorization takes effect. The authorizations regarding the utilization of shares bought back under the resolution dated May 27, 2008, shall apply to those treasury shares that the Company bought back pursuant to the treasury share buyback authorization dated May 27, 2008.

The buyback pursuant to the authorization granted by the resolution of the Annual Shareholders' Meeting on December 15, 2009, may also be executed by Group entities dependent on the Company within the meaning of Section 17 German Stock Corporation Act, or for the account of the Company or a Group entity dependent on it within the meaning of Section 17 German Stock Corporation Act.

Treasury shares held by the Company as of December 15, 2009, may already be utilized for the aims defined in foregoing authorizations a) through g) subject to both the respective requirements and the scope of the extant authorizations.

As of September 30, 2010 (inclusive), the authorization granted by the Annual Shareholders' Meeting on December 15, 2009, to acquire treasury shares or to utilize extant treasury shares was exercised as follows: 80,000 treasury shares were transferred to a member of the Management Board as part of his share-based compensation in December 2009.

The authorization granted by the Annual Shareholders' Meeting on May 27, 2008, to acquire treasury shares (for details please see the consolidated financial statements as of December 31, 2008) had not been exercised as of November 26, 2009 (inclusive) - which is the latest possible date.

Stock option plans

By resolution of the Annual Shareholders' Meeting dated December 15, 2009, the Company is authorized to issue one or several stock option plans pursuant to which options with a term of up to 10 years on up to 500,000 no-par bearer shares ("shares") of Zapf Creation AG may be issued until December 14, 2014 (inclusive), once or repeatedly, to employees of Zapf Creation AG, as well as to executives and to employees of affiliated companies. The Company's shareholders shall have no right to subscribe to the options. Of the 500,000 options overall, up to 280,000 options may be issued to employees of Zapf Creation AG; up to 120,000 options to executives of affiliates; and up to 100,000 options to employees of affiliates. No options may be issued to members of the Management Board of Zapf Creation AG under this authorization.

Each option gives its owner the right to subscribe one share of Zapf Creation AG. Exercising the options granted is subject to compliance with predetermined restrictions thereon, specifically, waiting periods, exercise periods and holding periods. The option model is subject to a performance target of 20% expressed as an issue premium; it makes no sense for the optionee in financial terms to exercise their options prior to achievement of said target. Rules on the transferability, forfeiture and retirement of the options are also in place.

Please see the disclosures on the purchase and use of treasury shares of Zapf Creation AG, as well as the disclosures below on the Contingent Capital 2009, in regards to the alternatives available to the Company for fulfilling optionees' claims at the time they exercise their options by means of treasury shares. In the alternative, the Company may, at its discretion, pay the difference between the exercise price and the current share price on the day on which it receives the respective notice of exercise in money in lieu of delivering new shares (Contingent Capital 2009) or treasury shares that it is already holding.

As of September 30, 2010, the Company had not availed itself of this possibility of making share-based payments.

Contingent Capital 2009

On December 15, 2009, the Annual Shareholders' Meeting resolved to create new contingent capital (Contingent Capital 2009) and amend Article 5 of the Articles of Incorporation (Amount and breakdown of share capital). According to this resolution, the Company's share capital is contingently increased by up to €500,000.00 through the issue of up to 500,000 no par value bearer shares (Contingent Capital 2009). This contingent capital increase shall only be executed to the extent that holders of options issued until December 14, 2014, in accordance with the resolution of the Annual Shareholders' Meeting dated December 15, 2009, exercise their options and to the extent that new shares must be issued in accordance with the option conditions. The new shares in the Company resulting from the exercise of the options shall participate in the Company's profits from the start of the financial year for which the Annual Shareholders' Meeting has not yet adopted any resolution regarding the appropriation of profit at the time options are exercised.

3. Related-party Disclosures

Relationships and transactions with related parties are disclosed in accordance with the requirements of IAS 24 (“Related Party Disclosures”), taking into account the provisions under IAS 34 (“Interim Financial Reporting”).

IAS 24 defines a related party as a person capable of controlling or significantly influencing another person, either alone or together with a third party, or as a person over whom such control or significant influence can be exercised. This definition of related parties includes both natural persons and other entities. In our case, the following have been identified as related parties: the Company's Management Board and Supervisory Board, and MGA Group entities related to the Company.

All transactions with related parties involving the supply of goods and services as part of the normal business activities of the Zapf Creation Group are conducted on an arm's-length basis.

3.1. The Management Board

The following changes were made to the Management Board of Zapf Creation AG during the period under review:

On January 29, 2010, the Supervisory Board of Zapf Creation AG appointed Ron Oboler as a member of the Management Board and Chairman of the Management Board with effect from February 1, 2010. Since then, Ron Oboler has been leading the Company on an interim basis. As Executive Vice President International at MGA Entertainment, Inc., he has extensive experience in the toy industry. The Supervisory Board was endeavoring to make a long-term appointment as Chairman of the Management Board during the course of the year. Stephan F. Brune, who served as a member of the Management Board and as Chairman of the Management Board of Zapf Creation AG from October 1, 2008, resigned from the Company with effect from January 31, 2010. In addition, Ron Brawer, a member of the Supervisory Board, was assigned temporarily to the Management Board on January 29, 2010 in accordance with section 105 (2) German Stock Corporation Act (AktG). Since then, Ron Brawer has been primarily responsible for the continued streamlining of Company structures and the realization of associated potential savings.

Effective June 30, 2010, another member of the Management Board, Jens U. Keil, left the Company in order to pursue other professional opportunities. Jens U. Keil had been responsible for finance, capital markets, IT, logistics, and risk management on the Management Board since March 1, 2007.

On August 6, 2010, Zapf Creation AG announced that the Supervisory Board had appointed Hannelore Schalast, Head of Corporate Finance & Controlling, as Chief Financial Officer (CFO) of the Company effective February 1, 2011. Until then, Hannelore Schalast will serve as Executive Vice President for Finance. Josef Lukas, currently working as a sales and distribution consultant for Zapf Creation covering Germany, Austria and Switzerland, has been appointed to the Management Board with responsibility for sales and distribution, also effective February 1, 2011. As previously announced, Ron Oboler, Chairman of the Management Board, and Ron Brawer, member of the Management Board temporarily assigned from the Supervisory Board, will step down from their respective interim positions on the Management Board as a result of the new appointments. Ron Oboler will resign from the Management Board effective February 15, 2011, and Ron Brawer effective December 31, 2010.

On November 2, 2010 Zapf Creation AG announced that the Supervisory Board had appointed Mr. Jaime Ferri Llorens as a member of the Management Board with effect from January 1, 2011 and as Chairman of the Management Board with effect from February 16, 2011. Jaime Ferri Llorens will be replacing Mr. Ron Oboler, who since February 2010 has been leading the Company on an interim basis.

Section 1 (3) of the Management Board's rules of procedure governing the allocation of responsibilities was last amended in July 2010; the allocation of responsibilities as of September 30, 2010 was as follows:

Ron Oboler, member and Chairman of the Management Board

▪ Sales, international sales, budget (parts thereof), HR, legal issues, subsidiaries, IT, finance, compliance and corporate governance, investor relations, public relations (excluding products)

Ron Brawer, member of the Management Board

▪ Procurement, logistics, restructuring, budget (parts thereof), risk management

José Antonio Santana, member of the Management Board

- Marketing, product research and development, quality management, Zapf Creation (H.K.) Ltd., public relations (products), trademark rights, budget (parts thereof), sales (parts thereof)

In the corresponding period in 2009, the Supervisory Board of Zapf Creation AG had appointed José Antonio Santana to the Management Board, effective March 1, 2009, with responsibility for marketing, design and product development, and quality management. José Antonio Santana took over these responsibilities from the Chairman of the Management Board, Stephan F. Brune, who had been overseeing these areas of the business on an interim basis. The other members of the Management Board of Zapf Creation AG at this time – Stephan F. Brune, Chairman of the Management Board, and Jens U. Keil, CFO – remained unchanged. On September 16, 2009, the Supervisory Board of Zapf Creation AG decided to reappoint Jens U. Keil as CFO before the end of his existing term of appointment.

The total compensation of €737 thousand (Q1-Q3 2009: €745 thousand) paid to the Management Board is the total of cash compensation and the monetary equivalent of benefits in kind; it comprises both fixed and variable components but does not include one-off compensation payments made to former members of the Management Board. In addition to the basic salary paid in cash to the members of the Management Board, the fixed component of compensation includes additional benefits, such as the use of company cars, allowances for accident insurance, and other insurance benefits. The Company is also covering the cost of a German teacher for José Antonio Santana, although the terms and conditions of this benefit are still to be fixed.

The compensation scheme in the form of a phantom stock option plan that was launched in 2006 for members of the Company's Management Board was continued in the period under review; for further information on the structure of the plan, please refer to the consolidated financial statements for the year ended December 31, 2009. Under this plan, a further 27,000 phantom stock options at a base price of €1.00 were granted in full to José Antonio Santana during the first nine months of 2010. The exercise of these options is not linked to the attainment of a specific performance target. In the corresponding period in 2009, 27,000 phantom stock options had been granted to José Antonio Santana at a base price of €0.81 and 10,000 phantom stock options had been granted to Jens U. Keil at a base price of €0.87. There were no further allocations of phantom stock options during the first nine months of 2010 or during the equivalent period in 2009. When phantom stock options are exercised, the beneficiary is paid, for each exercised option, the difference between the closing price of the shares on the issue date and the closing price of the shares on the exercise date. In the period under review, the additions to provisions (additions thus also recognized in profit or loss) for obligations arising from newly granted phantom stock options under the plan amounted to €10 thousand (Q1-Q3 2009: €15 thousand); as a result of changes in the share price, provisions amounting to €52 thousand were reversed and recognized in profit or loss in the first nine months of 2010 (Q1-Q3 2009: €8 thousand). As of September 30, 2010, the provision for obligations under this phantom stock option plan amounted to €41 thousand (September 30, 2009: €25 thousand). A tranche of 30,000 phantom stock options granted to Thomas Pfau, a former member of the Management Board, at a base price of €8.60 and a further tranche of 33,000 phantom stock options also granted to Thomas Pfau at a base price of €4.67 lapsed in the period under review; in the corresponding period in 2009, phantom stock options granted to another former member of the Management Board, Dr. Georg Kellinghusen, and a separate tranche again granted to Thomas Pfau also lapsed. A tranche granted to Jens U. Keil had been withdrawn from the end of September 2009 by mutual agreement.

A commitment has also been made to José Antonio Santana to grant him normal shares as an additional element of his share-based payment; this pay element is designed solely as a variable component of salary and depends on the attainment of specific performance targets. The bonus structure for Jens U. Keil also allowed the Company to pay a proportion of the bonus in the form of shares; there had been a similar form of compensation for Stephan F. Brune in 2009. This compensation component – which is now designed to be a completely variable component – resulted in no share-based payment in the first nine months of 2010 (Q1-Q3 2009: €134 thousand; fixed and variable components).

On March 4, 2010, the Company entered into a severance and settlement agreement with Stephan F. Brune, the former member of the Management Board and Chairman of the Management Board of Zapf Creation AG, in full and final settlement of both parties' claims and obligations related to his employment with the Company. Under these arrangements, a one-off compensation payment of €550 thousand (gross) to Stephan Brune was agreed between the parties. The Company also waived existing claims against Stephan Brune with a value of €25 thousand and paid in full the income tax due from the employee as a result of this waiver of claim. No one-off compensation payments were made to any former members of the Management Board or Supervisory Board in the corresponding period in 2009.

One former member of the Management Board had been granted a variable line of credit up to a maximum amount of €625 thousand until December 31, 2007. As of December 31, 2007, this line of credit had been fully drawn down. The agreed interest rate was 4.25 percent and was fixed until the maturity date of the loan on December 31, 2007. Under settlement arrangements reached in 2008, Zapf Creation AG agreed to waive repayment of €175 thousand of the loan provided certain conditions were met; any tax liability resulting from the benefit in kind had to be borne by the Company. The interest rate was raised to 5 percent per annum effective January 1, 2008; the parties agreed to a repayment plan for the remaining debt including the interest charges incurred. A repayment of €100 thousand was made in 2008; as in 2007, there were no new disbursements in 2008. In 2008, the Company's outstanding interest receivable as of December 31, 2007 amounting to €46 thousand plus invoiced interest of €3 thousand on the arrears (a total of €49 thousand) was paid in full; the interest charge for the 2008 interest period amounting to €23 thousand was also paid in full. In 2009 and in the first nine months of 2010 there were no further repayments of principal relating to the outstanding loan; interest was paid as agreed. As of September 30, 2010, the Company's total loan receivable amounted to €354 thousand (September 30, 2009: €354 thousand) after taking into account the aforementioned waiver of principal, repayments of principal, interest payments received, and the interest receivable for the third quarter of 2010. However, the disbursed loan remains secured by a charge over land with a value of €200 thousand (September 30, 2009: €200 thousand). As in 2009, the residual amount of the debt remains written off in full; the interest receivable for the third quarter of 2010 amounting to €4 thousand was settled in October 2010.

3.2. The Supervisory Board

The following changes occurred in the Supervisory Board of Zapf Creation AG during the period under review:

With reference to article 11 (4) of the Company's articles of incorporation, Nicolas Mathys, member and deputy Chairman of the Supervisory Board, announced on January 11, 2010 that he intended to step down from his position as member and a deputy Chairman of the Supervisory Board subject to a notice period of four weeks.

On January 29, 2010, the Supervisory Board of Zapf Creation AG temporarily assigned Ron Brawer, a member of the Supervisory Board, to the Management Board in accordance with section 105 (2) AktG. Since then, Ron Brawer has been primarily responsible for the continued streamlining of Company structures and the realization of associated potential savings.

The Annual Shareholders' Meeting held on December 15, 2009 had elected Jaime Ferri Llorens, domiciled in Alicante, Spain, to the Supervisory Board of the Company for a term of office starting at the end of the Annual Shareholders' Meeting on December 15, 2009 and ending with the conclusion of the Annual Shareholders' Meeting responsible for formally approving the acts of the Management Board and Supervisory Board in the 2009 financial year. Effective April 26, 2010, the Supervisory Board appointed Jaime Ferri Llorens as a consultant to the Company in all matters relating to strategic orientation, in particular product development and marketing, and development of the Spanish market. By mutual agreement with the Supervisory Board, Jaime Ferri Llorens therefore resigned from the Supervisory Board in accordance with article 11 (4) of the Company's articles of incorporation.

By order of the Coburg local court dated September 13, 2010, Manfred Schneider was appointed a member of the Supervisory Board of Zapf Creation AG pursuant to section 104 AktG.

As of September 30, 2010, the composition of the Company's Supervisory Board was as follows: Dr. Harald Rieger, member and Chairman of the Supervisory Board, Isaac Larian, member of the Supervisory Board, Miguel Perez-Carballo Villar, member of the Supervisory Board, and Manfred Schneider, member of the Supervisory Board.

The following change had occurred in the Supervisory Board of Zapf Creation AG in the corresponding period in 2009:

By order of the Coburg local court dated July 30, 2009, Gustavo Perez, member of the Supervisory Board since May 11, 2005, and member and deputy Chairman until July 28, 2006, had been removed as a member of the Supervisory Board of Zapf Creation AG.

The compensation of the Supervisory Board is determined by the Annual Shareholders' Meeting on recommendation of the Management Board and the Supervisory Board. It is regulated by article 20 of the Company's articles of incorporation. The cash compensation includes a fixed and a dividend-based component, together with compensation linked to the long-term performance of the Company.

In accordance with the articles of incorporation, the fixed compensation component for a full financial year is €35 thousand (net) for the Chairman of the Supervisory Board, €26.25 thousand (net) for the deputy Chairman, and €17.50 thousand (net) for each other member of the Supervisory Board. The compensation for Supervisory Board members not in office for a full financial year is paid pro rata according to the duration of their membership. As in 2009, the addition to the provision for the fixed component of the Supervisory Board compensation as of September 30, 2010 was made pro rata temporis.

As of the end of the corresponding period in 2009, no provision was recognized for the variable compensation component because there was no payment obligation owing to the financial performance of the Company; for further information on the structure of the variable compensation component, please refer to the consolidated financial statements for the year ended December 31, 2008.

As of September 30, 2010, no loans had been made to members of the Supervisory Board, as had also been the case at September 30, 2009.

3.3. Related Entities in the MGA Group

The inclusion of MGA Group companies in the related parties of Zapf Creation AG is due to the close partnership that has been implemented on an operational level in various areas of the business since the beginning of 2007. A summary of the details is as follows:

Since the beginning of 2007, MGA Entertainment, Inc., Van Nuys, California, USA, has been solely responsible as a licensee for selling Zapf Creation's products in American markets; MGA guarantees that the sales volume will exceed the sales revenue most recently generated by Zapf Creation's own subsidiaries in this region by more than 50 percent (Agreement 1: Distribution Agreement). In return, the parties agreed that the Zapf Creation Group would sell MGA products in selected European markets in exchange for payment of a distribution fee (Agreement 2: Consignment and Services Agreement). Zapf Creation Logistics GmbH & Co. KG provides logistics services for the MGA Group (Agreement 3: Logistics Service Agreement). Furthermore, in 2007, MGA Entertainment, Inc. took over the entire process of selecting and monitoring the Asian suppliers of Zapf Creation products, the coordination and handling of merchandise shipments to the sales units, and some parts of technical product development (Agreement 4: Hong Kong / China Services Agreement). In addition, Zapf Creation AG granted MGA Entertainment, Inc., Van Nuys, California, USA, against payment of a license fee, the exclusive right and the exclusive license to utilize and exploit both the products and the intellectual property of Zapf Creation AG, including the right to grant sublicenses (Agreement 5: Merchandising License Agreement). Effective April 1, 2008, the partnership was extended through another agreement (Agreement 6: UK Services Agreement). Since this date, MGA Entertainment UK Ltd. has been providing full sales and marketing services on behalf of Zapf Creation (U.K.) Ltd. in that company's sales areas for an appropriate fee. In return, Zapf Creation (U.K.) Ltd. provides administrative services to MGA Entertainment UK Ltd. for an appropriate fee. In 2009, the strategic partnership was enhanced by another agreement (Agreement 7: Inventions License Agreement). This agreement, which came into effect on January 1, 2009 and which was initially subject to consent from the banks providing finance for the Company, includes the right of Zapf Creation AG to utilize and exploit defined intellectual property of MGA Entertainment, Inc., Van Nuys, California, USA, in return for payment of a license fee.

In the first nine months of 2010, the following income and expenses resulted from this partnership:

Cooperation agreements	Q1-Q3/2010	Q1-Q3/2009
	€'000	€'000
Agreement 1: Distribution Agreement		
Income from Agreement 1	76	452
Agreement 2: Consignment and Services Agreement		
Income from Agreement 2	422	501
Agreement 3: Logistics Service Agreement		
Income from Agreement 3	242	523
Agreement 4: Hong Kong / China Services Agreement		
Expenses from Agreement 4	848	1,138
Agreement 5: Merchandising License Agreement		
Income from Agreement 5	0	32
Agreement 6: UK Services Agreement		
Income from Agreement 6	409	232
Expenses from Agreement 6	123	103
Agreement 7: Inventions License Agreement		
Expenses from Agreement 7	0	0

In addition to the transactions resulting from the cooperation agreements mentioned above (in the narrow sense), other services were also provided between the companies in the Zapf Creation Group and the related entities forming part of the MGA Group, resulting in the following cross charges:

Cross Charges	Q1-Q3/2010	Q1-Q3/2009
	€'000	€'000
Income arising from cross charges	562	1,046
Expenses arising from cross charges	1,026	1,194

Cross charges are charges between the companies in the Zapf Creation Group and the related entities forming part of the MGA Group that arise from the mutual provision of services above and beyond the cooperation agreements mentioned above (in the narrow sense); for the most part, the charges relate to income and expenses arising in connection with shared operating resources (staff, offices, etc.).

Merchandise procurement	Q1-Q3/2010	Q1-Q3/2009
	€'000	€'000
Merchandise procurement in the reporting period	31,020	24,297

Merchandise procurement in the reporting period resulted from the purchase of goods from MGA Entertainment (HK) Ltd by the sales companies in the Zapf Creation Group.

As in the corresponding period in 2009, there were no other direct purchases of goods and services from related entities in the MGA Group.

Again, as in the corresponding period in 2009, there were no other business transactions in the first nine months of 2010.

The receivables and payables in the Zapf Creation Group resulting from the partnership with the related entities in the MGA Group as of September 30, 2010 were as follows:

Balances as of the balance sheet date	Sep. 30, 2010	Sep. 30, 2009
	€'000	€'000
Receivables due from related parties	4,340	4,129
Payables due to related parties	11,300	11,998

4. Events after the Balance Sheet Date

An agreement was reached in October 2010 on the future financing structure of the Zapf Creation Group; the negotiations to secure the long-term funding of the Group were successfully concluded with the signing of an agreement in principle. Investors have been found who will replace a bank loan amounting to €20.1 million (Second Lien Loan). The replacement loan, the terms of which will be adjusted in line with the needs of the Company, will still mature in 2013; the adjustment includes an advance interest payment for three months. These new arrangements reduce the remaining outstanding loan with the syndicate of banks to just €9.0 million (Term Loan); this outstanding loan amount will be repaid early and in full by January 31, 2011. The Management Board is assuming that it will be able to guarantee future repayments of principal and interest payments, and the funding of Zapf Creation AG and the Zapf Creation Group has therefore been adequately secured.

On November 2, 2010 Zapf Creation AG announced that the Supervisory Board had appointed Mr. Jaime Ferri Llorens as a member of the Management Board with effect from January 1, 2011 and as Chairman of the Management Board with effect from February 16, 2011. Jaime Ferri Llorens will be replacing Mr. Ron Oboler, who since February 2010 has been leading the Company on an interim basis.

For additional information, please refer to the Group management report for the third quarter of 2010.

5. Directors' Dealings

During the period January 1 to November 10, 2010, the decision-making bodies of the Company reported the following directors' dealings as required by section 15a German Securities Trading Act (WpHG):

Stephan F. Brune, at that time member of the Management Board and Chairman of the Management Board of the Company, notified Zapf Creation AG on January 12, 2010 in accordance with section 15a WpHG that on January 11, 2010 he had sold a total of 80,000 shares in Zapf Creation AG (ISIN DE 0007806002) at a price of €1.15 per share (total transaction volume: €92,000). According to the information provided by Stephan Brune, the sale of the shares, which were due to him as part of his employment contract and thus transferred by the Company, was for private reasons.

All members of the Management Board and the Supervisory Board have been informed in detail of the obligation to notify all reportable transactions made by members of the Management Board or the Supervisory Board, their spouses or immediate relatives.

Rödental, November 10, 2010

Ron Oboler	Ron Brawer	José Antonio Santana
Chairman of the Management Board	Member of the Management Board	Member of the Management Board

Zapf Creation AG
Rödental

Consolidated Segment Reporting for the Period ended September 30, 2010

Segment Reporting

	Central Europe		Northern Europe		Southern Europe		Eastern Europe		Americas		Asia/Australia		Other		Consolidation		Group		Discontinued operations		Continuing operations	
Q1-Q3/	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009	2010	2009
	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000	€'000
External sales revenue	19,666	21,114	14,821	12,632	8,370	6,716	4,667	5,361	736	32	2,225	1,841	0	0	0	0	50,485	47,696	0	32	50,485	47,664
Intersegment sales revenue	152	1,514	898	472	150	1,272	183	769	0	0	0	0	0	0	-1,383	-4,027	0	0	0	0	0	0
Total segment sales revenue	19,818	22,628	15,719	13,104	8,520	7,988	4,850	6,130	736	32	2,225	1,841	0	0	-1,383	-4,027	50,485	47,696	0	32	50,485	47,664
Earnings before interest, tax and intercompany elimination (EBIT before intercompany elimination)	-5,601	-5,077	3,185	1,717	849	107	1,699	574	636	6	730	387	0	0	0	0	1,498	-2,286	346	6	1,152	-2,292
Earnings before interest and tax (EBIT)	-1,786	-1,923	778	-187	251	-350	1,697	432	636	6	-78	-264	0	0	0	0	1,498	-2,286	346	6	1,152	-2,292

Segment Reporting forms an integral part of the Notes.
The Consolidated Financial Statements for the year ended December 31, 2009 so far have been prepared in preliminary form only and have not yet been published;
for additional disclosures please refer to the Group Management Report and Notes.

Responsibility statement

'To the best of our knowledge, and in accordance with the applicable accounting principles for interim financial reporting, the interim consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Zapf Creation Group, and the interim group management report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal opportunities and risks associated with the Group's expected development for the remaining months of the financial year.'

Rödental, November 10, 2010

Ron Oboler	Ron Brawer	José Antonio Santana
Chairman of the Management Board	Member of the Management Board	Member of the Management Board