Annual Report 2002










Creative LifeStyle Digital Entertainment.

CREATIVE

CREATIVE TECHNOLOGY LTD

LifeStyle Digital Entertainment for Anyone and Everyone!

LifeStyle Digital Entertainment - the byword of the digital millennium. Espousing this outlook, Creative has become a global leader in persistently elevating the standards of digital entertainment. No longer confined to the PC, we design and create products to fit into your lifestyle with the power of choice and flexibility right in your hands to go where you want.

Our vision lies in the enhancement of the quality of life for each and every individual made possible with the best digital entertainment experience. Creative digital entertainment solutions are not just easily attainable and affordable but they also add loads of fun and attitude to your lifestyle.

Audio for Great Living

As a company comprising music aficionados, movie buffs and gaming addicts, we are simply passionate about audio. With audio being the very "soul" of an amazing digital audio experience, we exhort ourselves to achieve nothing short of the highest audio quality standard. We are constantly innovating and forging ahead to deliver to our consumers, complete high quality digital audio solutions to complement and enhance your digital lifestyle wherever you are. More than that, it is about sharing your favorite music, watching movies or playing games with your loved ones. After all, wonderful audio experiences are meant to bring people together.

Creative - continuously reinventing itself!

We understand the key to our success means empowering our consumers while bridging the gap between the PC and CE space. Not satisfied with resting on our laurels, we believe in the necessity of transformation and will always strive to deliver the latest digital audio products that promise exceptional quality and an unforgettable user experience.

Creative's philosophy - breaking down boundaries, taking digital entertainment beyond for an enhanced digital lifestyle.

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CHAIRMAN'S MESSAGE

Dear Shareholders,

Fiscal 2002 continued to be an extremely difficult and challenging year for Creative and the markets we serve. The Company's performance continued to be affected by the severe downturn in the global technology market and decline in the global equity markets which started the previous year and worsened during the year. These ongoing negative market developments have continued to adversely affect our operating results, and have also resulted in the company taking additional write-downs in our investment portfolio.

Despite these challenging market conditions, Creative was still able to realize a number of achievements, in terms of corporate-wide initiatives to improve operating results as well as on the product and technology front.

We had recognized the difficult and uncertain economic environment and, during the year, we aggressively persevered with the measures we had started last year to position Creative to meet the challenges in this tough period. In particular, we continued to focus on profitability and embarked on various operational improvement programs. These include our on-going efforts to redirect our strategy to focus on profitability, by concentrating on revenues from the higher-margin core audio segments, namely sound cards, speakers and personal digital entertainment products. We have also taken further action to institute operational improvement programs, including cost reduction and expense control efforts in all aspects of the business.

The success of these efforts is reflected in the financial results for the year – significant improvements in gross margins and reduction in operating expenses, resulting in an increase in operating profits even with the reduction in revenue.

Sales for fiscal year 2002 were $0.8 billion, a reduction of 34% compared to $1.2 billion for the fiscal year 2001. Gross profit as a percentage of sales was 33% in fiscal 2002 compared to 27% in fiscal 2001. Net loss for fiscal 2002 was $20 million, compared to a net loss of $130 million in fiscal 2001. The loss for fiscal 2002 included net investment losses and write-downs totaling $45 million and a one-time charge of $26 million for in-process technology relating to the acquisition of 3Dlabs, while the loss for fiscal 2001 included net investment losses and write-downs totaling $149 million and restructuring and other charges of $31 million. Excluding these investment losses and other charges, the results would have been a net income of $52 million for fiscal 2002 and $49 million for fiscal 2001.

On the product and technology front, the past year has seen what was probably the most exciting and innovative line of products yet released by Creative. With the launch of these new and exciting products, some of which are set out below, I am proud to say that Creative has matured to become a major force in a whole new market which we had pioneered - the Lifestyle Digital Entertainment market. The latest range of products from Creative, covering the major product categories such as PC audio, Lifestyle Digital Entertainment products, speakers, graphics and entertainment keyboards, include the following :

In the PC audio market, the **Sound Blaster® Audigy™**, launched in August 2001, established itself as the premier PC sound card with an unbeatable combination of superb audio clarity and functionality. The Audigy's EAX® ADVANCED HD™ audio effects have been embraced by the gaming community with exciting software titles taking advantage of its unique features. The new **Sound Blaster Audigy 2**, launched in September 2002, will significantly raise the bar for PC audio standards even higher with new features including 24-bit ADVANCED HD that supports 24-bit/192kHz audio with an astonishing 106 dB signal-to-noise ratio. It is the only PC sound card with Advanced Resolution™ DVD-Audio playback, officially certified Dolby® Digital EX 6.1 surround sound, THX®-certification and super fast connectivity with SB1394, for an exceptional audio experience. The **Sound Blaster Extigy™**, Creative's first external sound card, comes in a stylish enclosure that simply connects to a desktop PC or laptop via a USB connection for hassle-free use. It comes with excellent 24-bit digital audio clarity, Dolby Digital 5.1 surround sound and a host of connections.

For the Lifestyle Digital Entertainment market, new products from Creative include the **NOMAD® Jukebox 3**, **NOMAD Jukebox Zen™** and the **NOMAD MuVo™** digital audio players. The **NOMAD Jukebox 3** boasts a large 20GB storage capacity, a useful scroll wheel for quick navigation, audiophile sound quality and EAX audio technology featuring Smart Volume Management. The **NOMAD Jukebox Zen**, launched in October 2002, is a small pocket-sized hard disk-based MP3 player with both SB1394 and USB connections. Encased in a stylish, pocket-sized anodized aluminium casing, it measures less than an inch thick but yet packs up to 8000 songs. It has a large storage capacity, powerful music management tools, personalised features, high quality audio (signal-to-noise ratio of up to 98dB), SB1394 transfer, EAX technology and over seven minutes of anti-skip cache. It also works as a high speed portable hard drive to enable you to bring all your data files around. The **NOMAD MuVo** is a snazzy product which doubles as a digital audio player and data storage device. Extremely small (the size of a lighter), it can even fit on a keychain to take with you anywhere. It has very high quality sound (more than 90dB signal-to-noise ratio) with virtually skip-free playback. Another must-have feature of the MuVo is that it doubles as a solid-state portable USB hard drive for the PC or notebook, which will basically make obsolete the bulky and slow floppy disk drive.

On the speaker front, the portable **Creative TravelSound™ MP3** speaker system, the world's first multifunctional MP3 speaker system, comes with an integrated stereo digital amplifier and titanium drivers to deliver exceptional audio clarity, an MP3 player, a voice recorder and a 32MB solid state USB hard disk. It fits into the palm of your hand, and can be used as a standalone MP3 player with digitally amplified speaker or as a portable speaker for the NOMAD Jukebox, notebook, portable CD player, MiniDisc player or DVD player. The newly introduced **Creative Inspire 6.1** speaker systems - the first 6.1 speaker systems from Creative, feature 6 satellite speakers (including a rear center channel) and a subwoofer, to take advantage of the 6.1 surround sound capability of the Sound Blaster Audigy 2.

In the graphics market, Creative's participation via its acquisition of 3Dlabs during the year has seen the launch of the new 3Dlabs' **Wildcat VP** series of graphics cards for the professional workstation market. The new graphics cards incorporate ground-breaking "Visual Processing Architecture" that includes a virtual memory subsystem that is not limited by on-board graphics memory, multi-threaded command processor for simultaneous multiple processing and programmable units that support complex operations.

In the entertainment keyboard market, the **Creative Prodikeys™** is the industry's first synergistic music and PC keyboard, targeting a broad base of music lovers from the novice to the professional musicians who wish to interact with music in an exciting new way. It is a unique and refreshing concept combining an ergonomic QWERTY keyboard and 37 touch sensitive MIDI keys with powerful, yet easy-to-use software. It is extremely user-friendly and allows users to pick up basic music skills without going through formal training.

Looking ahead, the business environment remains highly challenging. Market conditions remain highly uncertain and difficult, with continued uncertainty on recovery, at least for the near term. While there are some instances of indications of improvements in the economic outlook, these have been tentative and there has not been any sustained and consistent or broad based economic recovery, particularly in the global technology markets. With these market conditions, we need to carry on with the strategy to focus on profitability and higher-margin core audio, speakers and Lifestyle Digital Entertainment products and with the measures taken to reduce costs and expenses.

With the success of the action we have taken over the past two years, Creative is emerging from these turbulent times a much leaner and focused company with the ability to respond rapidly to changes in business conditions. We have now a much lower cost structure that allows us to weather such difficult prevailing business conditions with a wide range of new product offerings, especially in audio, speakers and Lifestyle Digital Entertainment, which provide us with new growth opportunities. I believe we are now well positioned to meet the challenges ahead.

I would like to record my appreciation to the management and staff of Creative for their dedication and perseverance in helping the company through this difficult period. I would also like to take this opportunity to thank our shareholders for their continuing support.

Sim Wong Hoo
Chairman & Chief Executive Officer

CREATIVE

SELECTED CONSOLIDATED FINANCIAL DATA

The following table contains selected data from Creative's Consolidated Statements of Operations for the five years ended June 30, 2002. The data for the three years ended June 30, 2002 is qualified by reference to, and should be read in conjunction with, the consolidated financial statements and related notes thereto included elsewhere in this Annual Report.

CONSOLIDATED STATEMENTS OF OPERATIONS DATA (US$'000, EXCEPT PER SHARE DATA):

	For the years ended June 30				
	2002(1)	2001	2000	1999	1998(1)
Sales, net (2)	$ 805,905	$ 1,226,068	$ 1,342,192	$ 1,296,403	$ 1,234,136
Cost of goods sold	543,382	894,236	947,157	944,499	848,305
Gross profit	**262,523**	**331,832**	**395,035**	**351,904**	**385,831**
Operating expenses:					
Selling, general and administrative (2)	170,122	230,417	252,321	209,534	162,392
Research and development	38,248	54,022	60,428	46,725	41,723
Other charges (3)	26,080	22,814	20,000	–	68,568
Operating income	**28,073**	**24,579**	**62,286**	**95,645**	**113,148**
(Loss) gain from investments, net	(45,414)	(148,490)	103,443	15,048	18,469
Interest income and other, net	5,155	2,416	5,287	14,621	21,183
(Loss) income before income taxes and minority interest	**(12,186)**	**(121,495)**	**171,016**	**125,314**	**152,800**
Provision for income taxes (4)	(5,698)	(8,409)	(9,472)	(9,920)	(19,805)
Minority interest in (income) loss	(1,843)	(469)	(532)	(312)	1,779
Net (loss) income	**$ (19,727)**	**$ (130,373)**	**$ 161,012**	**$ 115,082**	**$ 134,774**
Basic (loss) earnings per share	$ (0.27)	$ (1.65)	$ 1.96	$ 1.28	$ 1.49
Weighted average ordinary shares outstanding ('000)	73,182	79,049	82,028	89,818	90,654
Diluted (loss) earnings per share	$ (0.27)	$ (1.65)	$ 1.86	$ 1.25	$ 1.42
Weighted average ordinary shares and equivalents outstanding ('000)	73,182	79,049	86,612	92,241	94,964

CONSOLIDATED BALANCE SHEET DATA (US$'000):

	As of June 30				
	2002(1)	2001	2000	1999	1998(1)
Cash and cash equivalents	$ 166,917	$ 168,157	$ 285,757	$ 318,990	$ 417,262
Working capital	165,945	203,180	331,414	400,998	484,792
Total assets	666,378	673,980	1,176,459	805,689	865,113
Long-term debt, net of current maturities	16,782	22,560	27,051	28,642	32,277
Shareholders' equity	423,952	381,886	778,638	560,261	622,314

Notes:

(1) Financial data for fiscal 2002 includes the results of 3Dlabs Inc., Ltd ("3Dlabs"), see Note 15 of "Notes to Consolidated Financial Statements," and for fiscal 1998 includes the results of Cambridge SoundWorks, Inc., ENSONIQ Corporation, Silicon Engineering, Inc., and the NetMedia Division of OPTi Inc. acquired during fiscal 2002 and 1998 respectively, from the date each acquisition was completed.

(2) In fiscal 2002, Creative adopted Emerging Issues Task Force ("EITF") Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products.)" As a result, certain consideration paid to distributors and resellers of its products has been reclassified as a revenue offset rather than as selling, general and administrative expense. Prior years' financial statements have been reclassified to conform to this presentation.

(3) Included in the results of operations are other charges of: $26.1 million in fiscal 2002 for write-off of in-process technology arising from the acquisition of 3Dlabs, see Note 15 of "Notes to Consolidated Financial Statements;" $22.8 million in fiscal 2001 which comprised $8.4 million restructuring charges, $3.2 million fixed assets impairment write-downs and $11.2 million write-off of other assets acquired from Aureal Semiconductor, Inc. ("Aureal"), see Note 12 of "Notes to Consolidated Financial Statements;" in fiscal 2000, the $20.0 million charge relates to the settlement of all outstanding litigation claims between Aureal and Creative; $68.6 million in fiscal 1998 relating to a $60.3 million write-off of acquired in-process technology and a charge of $8.3 million for cessation of certain activities.

(4) As described in Note 9 of "Notes to Consolidated Financial Statements", Creative was granted a Pioneer Certificate in 1990 under which income classified as pioneer status income is exempt from tax in Singapore, subject to certain conditions. The Pioneer Certificate expired in March 2000. Such status had the effect of reducing Creative's provision for income taxes by approximately $15.4 million, $26.4 million and $43.3 million, or $0.18, $0.29 and $0.46 per share, for fiscal 2000, 1999 and 1998 respectively. The corporate income tax rate in Singapore, which would otherwise be applicable, would have been 25.5% for fiscal year 2000, and 26% for fiscal years 1998 to 1999.

Creative has applied for a separate and new Pioneer Certificate. If Creative is awarded this new Pioneer Certificate, profits under the new Pioneer Certificate will be exempted from tax in Singapore. For fiscal 2000 (covering period from April 1, 2000 to June 30, 2000), 2001 and 2002, corporate tax was provided for in full based on the standard tax rates of 25.5%, 24.5% and 22% respectively as the terms and agreements of the new Pioneer Certificate is currently still under negotiation as at to date. The new Pioneer Certificate will result in the reduction of Creative's provision for income taxes, subject to the terms and agreement by the Singapore Comptroller of Income Tax. See MD&A for further discussion.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SAFE HARBOR STATEMENTS UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Except for the historical information contained herein, the matters set forth herein (including all references to future financial performance, products and marketing efforts) are forward-looking statements within the meaning of the safe harbor provisions of The Private Securities Litigation Reform Act of 1995. Readers of this Annual Report are cautioned not to place undue emphasis or reliance on these forward-looking statements which reflect management's analysis, judgement, belief or expectation only as of the date of this Annual Report. These forward-looking statements are subject to certain assumptions, risks and uncertainties that could cause actual results to differ materially from those set forth or implied in the forward looking statements. Such assumptions, risks and uncertainties include, among others: possible disruption in commercial activities, occasioned by terrorist activity and armed conflict which may, among other things, result in delays in, or damage to, the manufacture, shipment, or storage of Creative's products, or customers delaying or canceling purchasing decisions as a result of increased broad economic and safety concerns; the timely development, ramp, shipment, delivery, and market acceptance of new products, including Creative's next generation of audio and personal digital entertainment appliances; the increasing proliferation of sound functionality in new products from new and existing competitors and at the application software, chip and operating system levels; further deterioration of the System Integrator markets and failure of the System Integrators or OEMs to adopt Creative's products; the cost-cutting measures Creative has taken and plans to take may be insufficient or may fail to achieve the anticipated cost reduction benefits; deterioration of the global stock market and overall reduction in demand for computer systems, peripherals and related products in general, and Creative's products specifically; increased exposure to excess and obsolete inventory; higher overhead costs as a percentage of revenue; reduction or cancellation of sales orders for Creative products or other unexpected or unplanned events that could cause Creative to miss its revenue guidance, operating expense projections or negatively impact its margins; reductions in the market value of products sold by Creative, including increases in inventory or declines in demand or prices for storage devices, digital entertainment appliances, board and chip-level products, software, speakers, and other products; reductions in revenues and gross margins due to numerous factors, including declines in average selling prices of Creative's products, failure to reduce costs and increased inventories and pricing pressure from competitors; potential fluctuations in quarterly results due to the seasonality of Creative's business and the difficulty of projecting such fluctuations; the vulnerability of certain markets to current and future currency fluctuations, including the exchange rate of the Euro; labor shortages or work stoppages; credit shortages; effects of restricted fuel availability and rising costs of fuel; Creative's reliance on sole sources for many of its chips and other key components; component shortages which may impact Creative's ability to meet customer demand; Creative's ability to protect its proprietary rights; the volatility of share prices for companies in Creative's industry and the effect of those prices or other events beyond Creative's control, including acts of war, terrorist attacks, or adverse changes in general economic conditions; further fluctuations in the value and liquidity of Creative's investee companies, including any losses that may result from the increased volatility for technology stocks and potential price reductions of carrying values of our investee companies; and other risk factors described herein, in Creative's press release announcing the signing of the definitive agreement to acquire 3Dlabs dated March 11, 2002, and in Creative's filings with the Securities and Exchange Commission over the past twelve months, including without limitation, Creative's Form 20-F dated October 10, 2001. Creative urges you to consider all such factors. Creative undertakes no obligation to publicly release the results of any revisions to such forward-looking statements which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

GENERAL

Management's Discussion and Analysis of Financial Condition and Results of Operations are based upon Creative's Consolidated Condensed Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgements about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management believes the following critical accounting policies affect its more significant estimates and assumptions used in the preparation of its consolidated financial statements:

Revenue recognition;
Allowances for doubtful accounts, returns and discounts;
Valuation of inventories;
Valuation of investments;
Valuation of goodwill and other intangible assets;
Restructuring costs and accruals for excess facilities;
Assessment of the probability of the outcome of current litigation; and
Accounting for income taxes.

REVENUE RECOGNITION

Revenue from product sales is recognised when persuasive evidence of an arrangement exists, delivery has occurred, price is fixed or determinable, and collectibility is probable. Allowances are provided for estimated returns, discounts and warranties. Management analyzes historical returns, current economic trends and changes in customer demand and acceptance of its products when evaluating the adequacy of the sales returns allowance. Such allowances are adjusted periodically to reflect actual and anticipated experience. When recognizing revenue, Creative records estimated reductions to revenue for customer and distributor programs and incentive offerings, including price protection, promotions, other volume-based incentives and rebates. Creative may take action to increase customer incentive offerings possibly resulting in an incremental reduction of revenue at the time the incentive is offered. Significant management judgement and estimates must be used in connection with establishing these allowances in any accounting period. If market conditions were to decline, Creative may take action to increase customer incentive offerings, possibly resulting in an incremental reduction of revenue at the time the incentive is offered.

ALLOWANCES FOR DOUBTFUL ACCOUNTS, RETURNS AND DISCOUNTS

Creative establishes allowances for doubtful accounts, returns and discounts for specifically identified doubtful accounts, returns and discounts based on credit profiles of its customers, current economic trends, contractual terms and conditions and historical payment, return and discount experience. Management performs ongoing credit evaluations of customers' financial condition and uses letters of credit in certain circumstances. Credit insurance coverage is obtained when coverage is available. However, Creative often is not able to procure credit insurance coverage for all customers as insurers have excluded certain customers and geographic markets. In the event actual returns, discounts and bad debts differ from these estimates, or Creative adjust these estimates in future periods, its operating results and financial position could be adversely affected.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

VALUATION OF INVENTORIES

Creative states inventories at the lower of cost or market. Management performs a detailed assessment of inventory at each balance sheet date to establish provisions for excess and obsolete inventories. Evaluation includes a review of, among other factors, historical sales, current economic trends, forecasted sales, demand requirements, product lifecycle and product development plans, quality issues, and current inventory levels. In the event that Creative adjusts its estimates, such as forecasted sales and expected product lifecycles, its operating results and financial position could be adversely affected.

VALUATION OF INVESTMENTS

Creative holds equity investments in various companies from less than 1% to 100% of the issuer's outstanding capital stock. Investments in companies in which Creative acquires more than 50% of the outstanding capital stock, or which are under Creative's effective control, are treated as investments in subsidiaries, and the balance sheets and results of operations are fully consolidated after making an allowance for any minority interests. Companies in which Creative's investments total between 20% and 50% of such company's capital stock are treated as associated companies and recorded on an equity basis, whereby the cost of investment is adjusted to recognise Creative's share of all post acquisition results of operations.

As for investments of less than 20%, non-quoted investments are carried at cost, less provisions for permanent impairment where necessary, and quoted investments are reported at fair value with the unrealised gains and losses included as a separate component of shareholders' equity. The investment portfolio is monitored on a periodic basis for impairment. Creative's investments in these companies are inherently risky because the markets for the technologies or products they have under development are typically in the early stages and may never develop. In the event that the carrying value of an investment exceeds its fair value and the decline in value is determined to be other-than-temporary, an impairment charge is recorded and a new cost basis for the investment is established. Fair values for investments in public companies are determined using quoted market prices. Fair values for investments in privately-held companies are estimated based upon one or more of the following: pricing models using historical and forecasted financial information and current market rates, liquidation values, the values of recent rounds of financing, or quoted market prices of comparable public companies.

In order to determine whether a decline in value is other-than-temporary, Creative evaluates, among other factors: the duration and extent to which the fair value has been less than the carrying value; the financial condition of and business outlook for the company, including key operational and cash flow metrics, current market conditions and future trends in the company's industry, and the company's relative competitive position within the industry; and Creative's intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value.

VALUATION OF GOODWILL AND OTHER INTANGIBLE ASSETS

Creative uses the purchase method of accounting for business combinations, in line with Financial Accounting Standards Board's ("FASB") Statement of Financial Accounting Standard ("SFAS") No. 141 "Business Combinations." The purchase method of accounting for acquisitions requires extensive use of accounting estimates and judgments to allocate the purchase price paid to the fair value of the net tangible and intangible assets acquired, including in-process technology. The allocation of the purchase price was based on independent appraisals. The amounts and useful lives assigned to intangible assets could impact future amortization; the amount assigned to in-process technology is expensed immediately. If the assumptions and estimates used to allocate the purchase price are not correct, purchase price adjustments or future asset impairment charges could be required.

Creative reviews for impairment of goodwill and other intangible assets, whenever events indicate that the carrying amount might not be recoverable. Factors that Creative may consider important which could trigger an impairment review include the followings:

- significant under performance relative to expected historical or projected future operating results;
- significant changes in the manner of use of the acquired assets or the strategy for Creative's overall business;
- significant negative industry or economic trends;
- significant decline in Creative's stock price for a sustained period; and
- Creative's market capitalization relative to net book value.

When Creative determines that the carrying value of goodwill and other intangible assets may not be recoverable based upon the existence of one or more of the above indicators, Creative measures any impairment based on a projected discounted cash flow method using a discount rate determined by the management to be commensurate with the risk inherent in Creative's current business model.

RESTRUCTURING COSTS AND ACCRUALS FOR EXCESS FACILITIES

In accordance with the provisions of EITF Issue No. 94-3, "Accounting for Restructuring Charges," and Staff Accounting Bulletin No. 100, "Restructuring and Impairment Charges," Creative records restructuring costs when it commits to an exit plan and significant changes to the exit plan are not likely. The estimated loss on facilities which Creative intends to sublease is based on estimates of the timing and amount of sublease income. Creative reassesses this liability quarterly based on market conditions. Revisions to the estimates of this liability could materially impact Creative's operating results and financial position in future periods if anticipated events and key assumptions, such as the timing and amounts of sublease rental income do not materialize or change.

ASSESSMENT OF THE PROBABILITY OF THE OUTCOME OF CURRENT LITIGATION

Creative records accruals for loss contingencies when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated.

ACCOUNTING FOR INCOME TAXES

In preparation of the financial statements, Creative estimates its income taxes for each of the jurisdictions in which it operates. This involves estimating the actual current tax exposure and assessing temporary differences resulting from differing treatment of items, such as reserves and accruals for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within Creative's consolidated balance sheet. Significant management judgment is required in determining the provision for income taxes, deferred tax assets and liabilities and future taxable income for purposes of assessing the ability to realize any future benefit from its deferred tax assets. A full valuation allowance has been recorded for Creative's deferred tax assets at June 30, 2002, as management believes substantial uncertainty exists regarding the realizability of these assets.

The Singapore corporate income tax rate is currently at 22.0%, the rate at which Creative is providing taxes on Singapore income. Creative was granted a Pioneer Certificate in 1990 under which income classified as pioneer status income is exempt from tax in Singapore, subject to certain conditions. As the Pioneer Certificate expired in March 2000, Creative has applied for a separate and new Pioneer Certificate. If Creative is awarded this new Pioneer Certificate, the effective tax rate will be reduced as profits under the new Pioneer Certificate will be exempted from tax in Singapore.

In the event that actual results differ from these estimates or Creative adjust these estimates in future periods, its operating results and financial position could be materially affected.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

ACQUISITIONS

In May 2002, Creative completed the acquisition of 3Dlabs, a graphics vendor, supplying graphics accelerator solutions for professionals in Computer Aided Design ("CAD"), Digital Content Creation ("DCC"), and visual simulation markets. Creative believes that the acquisition will provide Creative a significant competitive advantage in the graphics space and allow Creative to re-emphasize graphics products.

To acquire the remaining outstanding capital stock of 3Dlabs, Creative paid approximately $37.0 million in cash, issued approximately 6.3 million shares of Creative's ordinary shares valued at approximately $71.7 million at the time of the closing, and assumed 3Dlabs outstanding options exercisable into approximately 1.6 million shares of Creative ordinary shares valued at approximately $12.0 million at the time of the closing. As a result of the acquisition, Creative also assumed 3Dlabs net liabilities of $21.1 million. In addition, Creative incurred approximately $1.3 million in transaction fees, including legal, valuation and accounting fees. The ordinary shares issued were valued in accordance with EITF Issue No. 99-12, "Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination," using the average closing prices for the Creative ordinary shares during the two days before and two days after (and including) the day on which the total number of Creative shares issuable to holders of 3Dlabs common shares were fixed and determinable. The assumed stock options were valued using the Black-Scholes valuation model, with a volatility rate of 60%, a risk-free interest rate of 2.20% to 4.93%, expected dividend yield of 2.5%, and an estimated vest term of 0.01 years after vest date.

Of the total assumed stock options of 3Dlabs, approximately 1.3 million stock options with an intrinsic value of $7.0 million were unvested. In accordance with FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation," these unvested options were accounted for as deferred stock-based compensation and are being recognized as compensation expense over their related vesting periods. Total stock-based compensation expenses with respect to the unvested options totaled $0.3 million in fiscal 2002.

Creative accounted for the acquisition using the purchase method of accounting and has included the results of 3Dlabs from the acquisition date of May 15, 2002. The allocation of the purchase price to in-process technology and identifiable intangible assets acquired was based on independent appraisals.

In accordance with SFAS 142, "Goodwill and Other Intangible Assets," intangible assets are being amortized over their respective benefit periods, which range from one to six years. Goodwill, which represents the excess of the purchase price over the fair value of the identifiable assets and liabilities of 3Dlabs will not be subject to amortization and the carrying value will be evaluated at least annually for impairment.

In accordance with the prevailing accounting standards, the amount of $26.1 million allocated to acquired in-process technology was written off as other charges in fiscal 2002. It is reasonably possible that the development of this technology could fail because of either prohibitive cost, inability to perform the required efforts to complete the technology or other factors outside of Creative's control such as a change in the market for the resulting developed products. In addition, at such time that the project is completed it is reasonably possible that the completed products do not receive market acceptance or that Creative is unable to produce and market the product cost effectively.

RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, selected statement of operations data as a percentage of sales:

	Years ended June 30		
	2002	2001	2000
Sales, net	100 %	100 %	100 %
Cost of goods sold	67	73	70
Gross profit	**33**	**27**	**30**
Operating expenses:			
Selling, general and administrative	21	19	19
Research and development	5	4	4
Other charges	3	2	2
Operating income	**4**	**2**	**5**
(Loss) gain from investments, net	(6)	(12)	8
Interest income and other, net	1	–	–
(Loss) income before income taxes and minority interest	**(1)**	**(10)**	**13**
Provision for income taxes	(1)	(1)	(1)
Minority interest in (income) loss	–	–	–
Net (loss) income	**(2) %**	**(11) %**	**12 %**

Creative's net sales, by product category, for the past three fiscal years were as follows:

	Percentage of Net Sales for fiscal years ended June 30		
	2002	2001	2000
Audio products	44 %	41 %	39 %
Speakers	21 %	12 %	11 %
Multimedia Upgrade Kits	5 %	22 %	23 %
Graphics & Video products	6 %	6 %	15 %
Personal Digital Entertainment	9 %	9 %	4 %
Communication / Other products	15 %	10 %	8 %

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

YEAR ENDED JUNE 30, 2002 COMPARED TO YEAR ENDED JUNE 30, 2001

Net sales for the year ended June 30, 2002 decreased by 34% compared to the year ended June 30, 2001. The substantially lower revenues in fiscal year 2002, was a result of the strategic shift by Creative to focus on its core products and to de-emphasize lower margin products and the difficult global economic climate. Audio product sales (Sound Blaster audio cards and chipsets) for fiscal year 2002 decreased by 30% compared to fiscal year 2001, but as a percentage of total sales, increased from 41% in fiscal 2001 to 44% in fiscal 2002. Sales of speakers increased by 10% and represented 21% of sales in fiscal 2002 compared with 12% of sales in fiscal 2001. The improvement in speaker sales was primarily a result of the introduction of new models of multi-media speakers. Sales of personal digital entertainment ("PDE") products which includes digital audio players and digital cameras, decreased by 31% and represented 9% of sales in fiscal 2002 and fiscal 2001. Sales of multimedia upgrade kits ("MMUK") which includes data storage, decreased by 84% in fiscal 2002 compared to fiscal 2001 and comprised 5% of sales compared to 22% of sales in the prior fiscal year. The reduction in MMUK sales in fiscal 2002 is in line with Creative's current business strategy of de-emphasizing lower margin products. Similarly, in line with this current strategy, sales of graphics and video products decreased by 36% and represented 6% of sales in both fiscal years 2002 and 2001. Sales of other products, which includes accessories, music products, communication products and other miscellaneous items, increased by 4% and represented 15% of sales in fiscal 2002 compared to 10% of sales in the prior fiscal year. This increase in other product sales was primarily due to an increase in sales of communication products.

Gross profit in fiscal 2002 increased to 33% of net sales, compared to 27% in fiscal 2001. This improvement in gross profit was primarily a result of the strategic shift in business, with emphasis on Creative's core audio products, speakers and PDE products.

Selling, general and administrative ("SG&A") expenses in fiscal 2002 declined by 26% due to management's cost cutting efforts to correspond to the revised revenue expectations. As a percentage of sales, SG&A expenses were 21% of sales for fiscal 2002 and 19% for fiscal 2001. Research and development expenses were 5% of sales in fiscal 2002 and 4% of sales in fiscal 2001.

Other charges of $26.1 million in fiscal 2002 relates to the write off of acquired in-process technology arising from the acquisition of 3Dlabs and represented 3% of sales in fiscal 2002 compared to 2% of sales in fiscal 2001. The write off of acquired in-process technology is in accordance with the prevailing accounting standards. See Note 15 of "Notes to Consolidated Financial Statements."

Net investment loss of $45.4 million in fiscal year 2002 comprised $49.3 million in write-downs of investments, offset partially by a $3.9 million net gain from sales of investments and marketable securities. Net investment loss of $148.5 million in fiscal 2001 included $200.3 million in write-downs of investments, offset partially by a $51.8 million net gain from sales of investments and marketable securities. Net interest and other income increased by $2.7 million to $5.1 million in fiscal 2002 compared to $2.4 million in the prior fiscal year. This increase was primarily due to an exchange gain of $3.9 million in fiscal 2002 versus an exchange loss of $3.7 million in fiscal 2001, offset partially by lower interest income resulting from lower interest rates and lower average cash balances.

Creative's provision for income taxes for fiscal 2002 remained flat at 1% of sales compared to the prior fiscal year. The provision for income taxes as a percentage of income before taxes and minority interest excluding net loss or gain from investments declined from 31% in fiscal 2001 to 17% in fiscal 2002. This reduction was primarily due to changes in the mix of taxable income arising from various geographical regions and utilization of non Singapore net operating losses.

YEAR ENDED JUNE 30, 2001 COMPARED TO YEAR ENDED JUNE 30, 2000

Net sales for the year ended June 30, 2001 decreased by 9% compared to the year ended June 30, 2000. Audio product sales (Sound Blaster audio cards and chipsets) for fiscal year 2001 decreased marginally by 2% compared to fiscal year 2000 primarily due to weaker demand in the system integrator and original equipment manufacturer ("OEM") channels. As a percentage of total sales, audio product sales increased to 41% of sales compared to 39% of sales in fiscal year 2000. Sales of multimedia upgrade kits ("MMUK"), including data storage, decreased by 12% in fiscal year 2001 and represented 22% of sales compared to 23% of sales in the prior fiscal year. Within MMUK, sales of audio upgrade kits and CD-ROM drives declined but their impact on total sales was partially offset by an increase in sales of Compact Disk ReWritable ("CD-RW") drives. The decline in sales of multimedia audio upgrade kits, which comprised a combination of sound cards and CD-ROM drives is mainly due to the downturn in the PC business. Sales of video and graphics products decreased by 63% and represented 6% of sales in fiscal year 2001 compared with fiscal year 2000, when they represented 15% of sales. The decline in sales was due to management's decision to de-emphasize on lower margin graphics products. Sales of personal digital entertainment products ("PDE") which include digital audio players and digital cameras increased by 95% to represent 9% of sales compared to fiscal 2000 when they represented 4% of sales. This increase in sales was primarily due to an increase in sales of the NOMAD Jukebox product introduced in the first quarter of fiscal year 2001. Sales of speakers increased marginally by 2% and represented 12% of sales in fiscal 2001 compared with fiscal 2000, when they represented 11% of sales. This improvement in speaker sales was primarily a result of the introduction of new models of multimedia speakers. Sales of other products, which included accessories, music products, communication products and other miscellaneous items, increased by 7% and represented 10% of sales in fiscal 2001 compared to 8% of sales in the prior fiscal year. This increase in other product sales was primarily due to an increase in sales of communication products.

Gross profit in fiscal 2001 declined by 16% to represent 27% of sales compared to 30% in fiscal 2000. Margins in fiscal 2001 were negatively impacted by a decline in the average selling prices of drives and PDE products and an $8.2 million inventory restructuring charge applied to cost of goods sold.

Selling, general and administrative ("SG&A") expenses in fiscal 2001 declined by 9% and were flat at 19% of sales compared to fiscal 2000. SG&A expenses declined due to management's cost cutting efforts and reduction in expenses incurred on non-revenue generating Internet activities. Research and development expenses in fiscal 2001 remained flat at 4% of sales compared with fiscal 2000.

Other charges of $22.8 million booked in fiscal 2001 comprised restructuring charges totaling $8.4 million, $3.2 million write-downs of fixed assets and write-off of other assets acquired from Aureal amounting to $11.2 million. See Note 12 of "Notes to Consolidated Financial Statements."

In fiscal 2001, Creative's net loss from investments was $148.5 million compared to a net gain of $103.4 million in fiscal 2000. The loss relates to $200.3 million of losses from write-downs of investments, offset partially by a $51.8 million net gain from sales of investments and marketable securities. Net interest and other income decreased by $2.9 million to $2.4 million in fiscal 2001 compared to $5.3 million in the prior fiscal year. This decline was primarily a result of a reduction in interest income arising from a lower average cash balance.

Creative's provision for income taxes for fiscal 2001 remained flat at 1% of sales as compared to the prior fiscal year. The provision for income taxes as a percentage of income before taxes and minority interest excluding net loss or gain from investments increased from 14% in fiscal 2000 to 31% in fiscal 2001. The increase was primarily due to a higher effective tax rate in Singapore due to the expiration of the Singapore pioneer status in March 2000, and changes in the mix of taxable income arising from various geographical regions, where the tax rates range from 0% to 50%. Creative has applied for a separate and new Pioneer Certificate. If Creative is awarded this new Pioneer Certificate, profits under the new Pioneer Certificate will be exempted from tax in Singapore. In the event that Creative fails to obtain the new Pioneer Certificate, future taxable income in Singapore shall be subjected to a statutory tax rate of 22.0%. There can be no assurance that Creative will be awarded a new Pioneer Certificate.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

QUARTERLY RESULTS

The following is a summary of Creative's unaudited quarterly results for the eight quarters ended June 30, 2002, together with the percentage of sales represented by such results. Consistent with the PC peripheral market, demand for Creative's products is generally stronger in the quarter ended December 31, compared to any other quarter of the fiscal year due to consumer buying patterns. In management's opinion, the results detailed below have been prepared on a basis consistent with the audited financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the information for the periods presented when read in conjunction with the financial statements and notes thereto contained elsewhere herein. Creative's business is seasonal in nature and the quarterly results are not necessarily indicative of the results to be achieved in future quarters.

	Unaudited data for quarters ended (in US$'000 except per share data)							
	Jun 30 2002	Mar 31 2002	Dec 31 2001	Sep 30 2001	Jun 30 2001	Mar 31 2001	Dec 31 2000	Sep 30 2000
Sales, net (1)	$ 182,572	$ 193,385	$ 249,506	$ 180,442	$ 233,315	$ 262,009	$ 426,576	$ 304,168
Cost of goods sold	122,291	129,209	167,353	124,529	170,211	199,622	313,069	211,334
Gross profit	**60,281**	**64,176**	**82,153**	**55,913**	**63,104**	**62,387**	**113,507**	**92,834**
Operating expenses:								
Selling, general and administrative (1)	42,815	38,737	45,143	43,427	48,237	54,664	69,614	57,902
Research and development	10,748	8,412	9,480	9,608	12,431	11,380	15,115	15,096
Other charges (2)	26,080	–	–	–	–	22,814	–	–
Operating (loss) income	**(19,362)**	**17,027**	**27,530**	**2,878**	**2,436**	**(26,471)**	**28,778**	**19,836**
Net (loss) gain from investments	(29,845)	128	728	(16,425)	(75,988)	(75,360)	507	2,351
Interest income (expense) and other, net	2,289	151	1,291	1,424	183	1,090	2,055	(912)
(Loss) income before income taxes and minority interest	**(46,918)**	**17,306**	**29,549**	**(12,123)**	**(73,369)**	**(100,741)**	**31,340**	**21,275**
Provision for income taxes	(1,012)	(1,703)	(2,753)	(230)	–	–	(4,624)	(3,785)
Minority interest in (income) loss	(436)	(423)	(489)	(495)	(71)	(289)	(241)	132
Net (loss) income	**$ (48,366)**	**$ 15,180**	**$ 26,307**	**$ (12,848)**	**$ (73,440)**	**$ (101,030)**	**$ 26,475**	**$ 17,622**
Basic (loss) earnings per share	$ (0.65)	$ 0.21	$ 0.36	$ (0.17)	$ (0.94)	$ (1.27)	$ 0.34	$ 0.22
Weighted average ordinary shares outstanding ('000)	74,375	72,134	72,366	73,854	78,084	79,299	78,964	79,848
Diluted (loss) earnings per share	$ (0.65)	$ 0.20	$ 0.36	$ (0.17)	$ (0.94)	$ (1.27)	$ 0.33	$ 0.21
Weighted average ordinary shares and equivalents outstanding ('000)	74,375	76,323	73,664	73,854	78,084	79,299	81,180	84,151

	Unaudited data for quarters ended (as a percentage of sales)							
	Jun 30 2002	Mar 31 2002	Dec 31 2001	Sep 30 2001	Jun 30 2001	Mar 31 2001	Dec 31 2000	Sep 30 2000
Sales, net (1)	100 %	100 %	100 %	100 %	100 %	100 %	100 %	100 %
Cost of goods sold	67	67	67	69	73	76	73	70
Gross profit	**33**	**33**	**33**	**31**	**27**	**24**	**27**	**30**
Operating Expenses:								
Selling, general and administrative (1)	24	20	18	24	21	21	16	19
Research and development	6	4	4	5	5	4	4	5
Other charges (2)	14	–	–	–	–	9	–	–
Operating (loss) income	**(11)**	**9**	**11**	**2**	**1**	**(10)**	**7**	**6**
Net (loss) gain from investments	(16)	–	–	(9)	(32)	(29)	–	1
Interest income (expense) and other, net	1	–	1	–	–	1	–	–
(Loss) income before income taxes and minority interest	**(26)**	**9**	**12**	**(7)**	**(31)**	**(38)**	**7**	**7**
Provision for income taxes	(1)	(1)	(1)	–	–	–	(1)	(1)
Minority interest in (income) loss	–	–	–	–	–	–	–	–
Net (loss) income	**(27) %**	**8 %**	**11 %**	**(7) %**	**(31) %**	**(38) %**	**6 %**	**6 %**

(1) For the quarter ended March 31, 2002, Creative has adopted EITF Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." As a result, certain consideration paid to distributors and resellers of its products has been reclassified as a revenue offset rather than as selling, general and administrative expense. Prior quarters' financial data have been reclassified to conform to this presentation.

(2) Other charges for the quarter ended June 30, 2002 relates to the write-off of in-process technology arising from the acquisition of 3Dlabs. For the quarter ended March 31, 2001 includes $8.4 million in restructuring charges, fixed assets impairment write-downs of $3.2 million and write-off of other assets acquired from Aureal amounting to $11.2 million. See Notes 12 and 15 of "Notes to Consolidated Financial Statements."

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents at June 30, 2002 were $166.9 million, a decrease of $1.3 million compared to the balance of $168.2 million at June 30, 2001.

Operating Activities:
Net cash generated from operating activities during fiscal 2002 was $89.2 million compared with $76.9 million in fiscal 2001. The cash generated during fiscal 2002 primarily resulted from the net loss of $19.7 million offset by net adjustments of $105.7 million for non-cash items including depreciation and amortization of $29.9 million, write off of in-process technology acquired from 3Dlabs amounting to $26.1 million (see Note 15 of "Notes to Consolidated Financial Statements"), investments and other non-current asset write downs of $49.3 million, and net gain from investments of $5.3 million. Also contributing to the cash generated from operating activities were net decreases in accounts receivable of $18.2 million and inventory of $50.6 million which is in line with the management's decision to maintain a lower inventory level. However, the positive cash flow was offset partially by a net reduction in accounts payable, other accrued liabilities and income taxes payable of $69.2 million, resulting in the net cash generated of $89.2 million.

Net cash generated from operating activities during fiscal 2001 was $76.9 million compared with $160.2 million in fiscal 2000. The cash generated during fiscal 2001 primarily resulted from the net loss of $130.4 million being more than offset by net adjustments of $196.5 million for non-cash items including depreciation and amortization of $27.0 million, investments and other non-current asset write downs of $214.8 million, and net gain from investments of $49.9 million. Also contributing to the cash generated from operating activities were net decreases in marketable securities of $17.6 million, other assets and prepaids of $15.7 million, and inventory of $75.1 million which is in line with the management's decision to maintain a lower inventory level. However, the positive cash flow was offset partially by a net reduction in accounts payable, other accrued liabilities and income taxes payable of $101.9 million, resulting in the net cash generated of $76.9 million.

Investing Activities:
Net cash used for investing activities during fiscal 2002 was $49.8 million compared with $69.1 million in fiscal 2001. The amount used in fiscal 2002 comprises $25.8 million for the acquisition of 3Dlabs, net of cash acquired (see Note 15 of "Notes to Consolidated Financial Statements"), purchase of investments of $9.2 million, capital expenditures of $8.1 million, and the acquisition of other non current assets of $20.6 million. The cash used in investing activities was offset in part by the proceeds from sale of quoted investments amounting to $13.9 million.

Net cash used for investing activities during fiscal 2001 was $69.1 million compared with $104.3 million in fiscal 2000. The amount used in fiscal 2001 comprises the purchase of investments of $110.4 million, capital expenditures of $34.5 million, and the acquisition of other non current assets of $13.1 million, including assets from Aureal. The cash used in investing activities was offset in part by the proceeds from sale of quoted investments amounting to $88.9 million.

Financing Activities:
During fiscal 2002, $40.7 million was used for financing activities compared with $125.4 million in fiscal 2001. Cash used for financing included $18.0 million to purchase and retire 2.7 million Creative ordinary shares (See Note 6 of "Notes to Consolidated Financial Statements"), $18.0 million for dividends paid (See Note 7 of "Notes to Consolidated Financial Statements"), $10.0 million to buyout a subsidiary's preference shares issued to minority interests (See Note 11 of "Notes to Consolidated Financial Statements"), and $3.1 million to repay long-term obligations. The cash used in financing activities was offset partially by cash generated from exercises of stock options to purchase Creative ordinary shares amounting to $8.2 million.

During fiscal 2001, $125.4 million was used for financing activities compared with $89.1 million in fiscal 2000. Cash used for financing included $91.0 million to purchase and retire 7.7 million Creative ordinary shares (See Note 6 of "Notes to Consolidated Financial Statements"), $39.4 million for dividends paid (See Note 7 of "Notes to Consolidated Financial Statements"), and $4.5 million to repay long-term obligations. The cash used in financing activities was offset partially by cash generated from exercises of stock options to purchase Creative ordinary shares amounting to $9.3 million.

As of June 30, 2002, in addition to cash reserves and excluding long term loan, Creative had unutilized credit facilities totaling approximately $108.8 million for overdrafts, guarantees and letters of credit. Creative continually reviews and evaluates investment opportunities, including potential acquisitions of, and investments in, companies that can provide Creative with technologies, subsystems or complementary products that can be integrated into or offered with its existing product range. Creative generally satisfies its working capital needs from internally generated cash flows. Management believes that Creative has adequate resources to meet its projected working capital and other cash needs for at least the next twelve months. To date, inflation has not had a significant impact on Creative's operating results.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following table presents the contractual obligations and commercial commitments of Creative as of June 30, 2002:

	Payments Due by Period (US$'000)				
Contractual Obligations	Total	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years
Long Term Debt	$ 27,560	$ 19,228	$ 8,332	$ –	$ –
Short Term Debt	757	757	–	–	–
Capital Lease Obligations	7,919	3,556	4,269	94	–
Operating Leases	50,924	11,912	17,402	7,208	14,402
Unconditional Purchase Obligations	47,371	47,371	–	–	–
Other Long Term Obligations	2,754	2,452	302	–	–
Total Contractual Cash Obligations	**$ 137,285**	**$ 85,276**	**$ 30,305**	**$ 7,302**	**$ 14,402**

As of June 30, 2002, Creative has utilized approximately $6.5 million under guarantees, letters of credit, overdraft and short term loan facilities.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1 of "Notes to Consolidated Financial Statements" for the discussion of recently issued accounting pronouncements.

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE BOARD OF DIRECTORS AND
SHAREHOLDERS OF CREATIVE TECHNOLOGY LTD.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of cash flows and of shareholders' equity present fairly, in all material respects, the financial position of Creative Technology Ltd. and its subsidiaries at June 30, 2002 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2002 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of Creative's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers
Singapore
August 14, 2002

CREATIVE

CONSOLIDATED BALANCE SHEETS

(In US$'000, except per share data)

	June 30 2002	June 30 2001
ASSETS		
Current assets:		
Cash and cash equivalents	$ 166,917	$ 168,157
Marketable securities	1,388	3,581
Accounts receivable, less allowances of $22,159 and $25,221	85,193	94,445
Inventory	108,549	155,550
Other assets and prepaids	17,773	19,476
Total current assets	**379,820**	**441,209**
Property and equipment, net	104,748	110,535
Investments	66,688	118,330
Other non-current assets	115,122	3,906
Total Assets	**$ 666,378**	**$ 673,980**
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 64,809	$ 88,691
Accrued liabilities	77,831	98,135
Income taxes payable	43,794	47,601
Current portion of long term obligations and others	27,441	3,602
Total current liabilities	**213,875**	**238,029**
Long term obligations	16,782	22,560
Minority interest in subsidiaries	11,769	31,505
Shareholders' equity:		
Ordinary shares ('000); S$0.25 par value;		
Authorized: 200,000 shares		
Outstanding: 78,866 and 73,944 shares	7,592	6,914
Additional paid-in capital	311,445	209,555
Unrealized holding gains on quoted investments	20,636	22,249
Deferred share compensation	(8,836)	(5,711)
Retained earnings	93,115	148,879
Total shareholders' equity	**423,952**	**381,886**
Total Liabilities and Shareholders' Equity	**$ 666,378**	**$ 673,980**

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

CONSOLIDATED STATEMENTS OF OPERATIONS

(In US$'000, except per share data)

	Years ended June 30		
	2002	2001	2000
Sales, net	$ 805,905	$1,226,068	$1,342,192
Cost of goods sold	543,382	894,236	947,157
Gross profit	**262,523**	**331,832**	**395,035**
Operating expenses:			
Selling, general and administrative	170,122	230,417	252,321
Research and development	38,248	54,022	60,428
Other charges (Notes 12 and 15)	26,080	22,814	20,000
Operating income	**28,073**	**24,579**	**62,286**
(Loss) gain from investments, net	(45,414)	(148,490)	103,443
Interest income and other, net	5,155	2,416	5,287
(Loss) income before income taxes and minority interest	**(12,186)**	**(121,495)**	**171,016**
Provision for income taxes	(5,698)	(8,409)	(9,472)
Minority interest in income	(1,843)	(469)	(532)
Net (loss) income	**$ (19,727)**	**$ (130,373)**	**$ 161,012**
Basic (loss) earnings per share	$ (0.27)	$ (1.65)	$ 1.96
Weighted average ordinary shares outstanding ('000)	73,182	79,049	82,028
Diluted (loss) earnings per share	$ (0.27)	$ (1.65)	$ 1.86
Weighted average ordinary shares and equivalents outstanding ('000)	73,182	79,049	86,612

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

Increase (decrease) in cash and cash equivalents (in US$'000)

	Years ended June 30		
	2002	2001	2000
Cash flows from operating activities:			
Net (loss) income	$ (19,727)	$ (130,373)	$ 161,012
Adjustments to reconcile net (loss) income to net cash provided by operating activities:			
Depreciation and amortization	29,869	27,004	35,582
Deferred share compensation amortization	2,759	3,254	4,615
Write off of acquired in-process technology	26,080	–	–
Minority interest in income	1,843	469	532
Equity share in loss (income) of unconsolidated investments	1,220	927	(74)
Write off of investments and other non-current assets	49,303	214,754	9,793
Gain from investments, net	(5,341)	(49,934)	(94,712)
Changes in assets and liabilities, net:			
Accounts receivable	18,243	4,478	31,221
Inventory	50,589	75,066	(82,588)
Marketable securities	2,193	17,575	(21,156)
Other assets and prepaids	1,360	15,673	(15,252)
Accounts payable	(33,659)	(94,608)	81,633
Accrued and other liabilities	(29,431)	(6,588)	48,259
Income taxes payable	(6,076)	(749)	1,319
Net cash provided by operating activities	**89,225**	**76,948**	**160,184**
Cash flows from investing activities:			
Capital expenditures, net	(8,132)	(34,490)	(21,588)
Proceeds from sale of quoted investments	13,936	88,874	146,504
Purchase of new subsidiaries (net of cash acquired)	(25,806)	–	–
Purchase of investments	(9,152)	(110,397)	(228,273)
Increase in other non current assets, net	(20,629)	(13,106)	(994)
Net cash used in investing activities	**(49,783)**	**(69,119)**	**(104,351)**
Cash flows from financing activities:			
Increase (decrease) in minority shareholders' loan and equity balance	229	1,071	(114)
Net proceeds from issuance of preference shares to minority shareholders	–	(670)	22,459
Buyout of subsidiary's preference shares issued to minority interest	(10,019)	–	–
Proceeds from exercise of ordinary share options	8,195	9,265	16,953
Repurchase of ordinary shares	(18,013)	(91,029)	(102,189)
Repayments of long-term obligations, net	(3,050)	(4,497)	(5,618)
Dividends paid to ordinary shareholders	(18,024)	(39,414)	(20,557)
Dividends paid to minority interest	–	(155)	–
Net cash used in financing activities	**(40,682)**	**(125,429)**	**(89,066)**
Net decrease in cash and cash equivalents	**(1,240)**	**(117,600)**	**(33,233)**
Cash and cash equivalents at beginning of year	168,157	285,757	318,990
Cash and cash equivalents at end of year	**$ 166,917**	**$ 168,157**	**$ 285,757**
Supplemental disclosure of cash flow information:			
Interest paid	$ 752	$ 1,028	$ 1,069
Income taxes paid	$ 11,711	$ 9,158	$ 4,209
Non cash transaction:			
Buyout of a subsidiary's preference shares	$ 11,789	$ –	$ –

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

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In US$'000, except share data)

	Ordinary Shares ('000)	Ordinary Share Capital	Additional Paid In Capital	Unrealised Holding Gains (Losses) on Investments	Deferred Share Compensation	Retained Earnings	Total
Balance at June 30, 1999	**83,971**	**8,348**	**170,157**	**15,405**	**(5,078)**	**371,429**	**560,261**
Shares issued under employee options and share purchase plans	2,271	333	16,620	–	–	–	16,953
Repurchase of ordinary shares	(5,917)	(873)	873	–	–	(102,189)	(102,189)
Dividends paid	–	–	–	–	–	(20,557)	(20,557)
Deferred share compensation	–	–	15,461	–	(15,461)	–	–
Amortization of deferred share compensation	–	–	–	–	4,615	–	4,615
Comprehensive income	–	–	–	158,543	–	161,012	319,555
Balance at June 30, 2000	**80,325**	**7,808**	**203,111**	**173,948**	**(15,924)**	**409,695**	**778,638**
Shares issued under employee options and share purchase plans	1,153	165	9,100	–	–	–	9,265
Repurchase of ordinary shares	(7,742)	(1,089)	1,089	–	–	(91,029)	(91,029)
Shares issued for purchase of Aureal assets	208	30	3,214	–	–	–	3,244
Dividends paid	–	–	–	–	–	(39,414)	(39,414)
Reversal of unvested deferred share compensation, net	–	–	(6,959)	–	6,959	–	–
Amortization of deferred share compensation	–	–	–	–	3,254	–	3,254
Comprehensive loss	–	–	–	(151,699)	–	(130,373)	(282,072)
Balance at June 30, 2001	**73,944**	**6,914**	**209,555**	**22,249**	**(5,711)**	**148,879**	**381,886**
Shares issued under employee options and share purchase plans	1,319	180	8,015	–	–	–	8,195
Repurchase of ordinary shares	(2,722)	(381)	381	–	–	(18,013)	(18,013)
Dividends paid	–	–	–	–	–	(18,024)	(18,024)
Reversal of unvested deferred share compensation, net	–	–	(1,169)	–	1,169	–	–
Amortization of deferred share compensation	–	–	–	–	2,759	–	2,759
Comprehensive loss	–	–	–	(1,613)	–	(19,727)	(21,340)
Buyout of a subsidiary's preference shares	–	–	11,789	–	–	–	11,789
Shares and share options issued for acquisition of 3Dlabs	6,325	879	82,874	–	(7,053)	–	76,700
Balance at June 30, 2002	**78,866**	**$ 7,592**	**$ 311,445**	**$ 20,636**	**$ (8,836)**	**$ 93,115**	**$ 423,952**

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The consolidated financial statements include the financial statements of Creative Technology Ltd and Creative's subsidiaries under its effective control from their respective dates of acquisition, after elimination of intercompany transactions and balances. The consolidated financial statements are presented in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). The preparation of financial statements in accordance with US GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Creative conducts a substantial portion of its business in United States dollars ("US$" or "$"). All dollar amounts included in the financial statements and in the notes herein are United States dollars unless designated as Singapore dollars ("S$"). Creative's fiscal year-end is June 30. Creative generally operates on a thirteen week calendar closing on the Friday closest to the natural calendar quarter. For convenience, all quarters are described by their natural calendar dates.

Foreign exchange

The functional currency of Creative and its subsidiaries is predominantly US dollar and accordingly, gains and losses resulting from the translation of monetary assets and liabilities denominated in currencies other than the US dollar are reflected in the determination of net income (loss). Creative enters into forward exchange contracts to reduce its exposure to foreign exchange translation gains and losses. Forward exchange contracts are marked to market each period and the resulting gains and losses are included in the determination of net income or loss. No forward exchange contracts were outstanding at June 30, 2002. Included in interest and other expenses for fiscal years 2002, 2001 and 2000 are exchange gains of $3.9 million and exchange losses of $3.7 million and $7.0 million, respectively.

At June 30, 2002, monetary assets and liabilities of Creative are denominated in the following currencies:

	Approximate Percentage of $ Balance Denominated in:			
	US$	S$	EURO	Other Currencies
Cash and cash equivalents	83 %	3 %	5 %	9 %
Accounts receivable, less allowances	71 %	1 %	11 %	17 %
Total current liabilities	63 %	27 %	4 %	6 %
Long-term obligations	74 %	22 %	–	4 %

The exchange rates for the S$ and Euro utilized in translating the balance sheet at June 30, 2002, expressed in US$ per one S$ and Euro was 0.5673 and 0.9975, respectively.

Cash equivalents
Cash equivalents consist of highly liquid investment instruments with original maturities of three months or less. All deposits are in short term deposit and money market accounts with various banks. This diversification of risk is consistent with Creative's policy to maintain liquidity and ensure the safety of principal. Included in cash equivalents as of June 30, 2002 and 2001 are fixed rate deposits of $128.0 million and $132.7 million respectively. A total of $4.5 million in the fixed rate deposits was held as collateral for one of the subsidiary's bank overdraft and short term loan facilities (see Note 10).

Marketable Securities
Creative determines the appropriate classification of marketable securities at the time of acquisition and evaluates such designation at each balance sheet date. For all periods presented, Creative has classified marketable securities as trading securities, and accordingly such securities are stated at their market values based on the last transacted prices at each balance sheet date. The resulting net unrealized gains or losses on marketable securities are included in earnings in the period they are incurred.

Fair value of financial instruments
For certain of Creative's financial instruments, including cash equivalents, accounts receivable, accounts payable and accrued expenses, the carrying amounts approximate fair value due to their short maturities. The amounts shown for long term obligations also approximate fair value because current interest rates charged to Creative for debts of similar maturities are substantially the same.

Inventory
Inventory is stated at the lower of cost or market. Cost is determined using standard cost, appropriately adjusted at balance sheet date to approximate actual cost on a weighted average basis. In the case of finished products and work-in-progress, cost includes materials, direct labor and an appropriate proportion of production overheads.

Management performs a detailed assessment of inventory at each balance sheet date to establish provisions for excess and obsolete inventories. Evaluation includes a review of, among other factors, historical sales, current economic trends, forecasted sales, demand requirements, product lifecycle and product development plans, quality issues, and current inventory levels.

Property and equipment
Property and equipment are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the shorter of the remaining facility lease term or the estimated useful lives of the improvements. No depreciation is provided on freehold land and construction in progress.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Investments

Creative holds equity investments in various companies pursuant to which it has acquired anywhere from less than 1% to 100% of the issuer's outstanding capital stock. Investments in which Creative acquires more than 50% of the outstanding capital stock of an entity, or which are under the effective control of Creative, are treated as investments in subsidiaries, and the balance sheets and results of operations of these subsidiaries are fully consolidated after making allowance for any minority interests. Companies in which Creative's investment totals between 20% and 50% of such company's capital stock are treated as associated companies and recorded on an equity basis, whereby Creative adjusts its cost of investments to recognize its share of all post acquisition results of operations.

Non quoted investments of less than 20% in an entity are carried at cost, less provisions for permanent impairment where necessary.

In accordance with SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", quoted investments of less than 20% in an entity are classified as available-for-sale. Such investments are reported at fair value with the unrealized gains and losses included as a separate component of shareholders' equity. Unrealized losses are charged against income when a decline in fair value is determined to be other than temporary. Realized gains and losses upon the sale or disposition of such investments are based on the average cost of the specific investments sold.

The investment portfolio is monitored on a periodic basis for impairment. Creative's investments in these companies are inherently risky because the markets for the technologies or products they have under development are typically in the early stages and may never develop. In the event that the carrying value of an investment exceeds its fair value and the decline in value is determined to be other-than-temporary, an impairment charge is recorded and a new cost basis for the investment is established. Fair values for investments in public companies are determined using quoted market prices. Fair values for investments in privately-held companies are estimated based upon one or more of the following: pricing models using historical and forecasted financial information and current market rates, liquidation values, the values of recent rounds of financing, or quoted market prices of comparable public companies.

In order to determine whether a decline in value is other-than-temporary, Creative evaluates, among other factors: the duration and extent to which the fair value has been less than the carrying value; the financial condition of and business outlook for the company, including key operational and cash flow metrics, current market conditions and future trends in the company's industry, and the company's relative competitive position within the industry; and Creative's intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value.

A summary of investments is as follows (in US$'000):

	As of June 30	
	2002	2001
Non quoted investments	$ 15,924	$ 40,761
Quoted investments	50,764	77,569
Total investments	**$ 66,688**	**$ 118,330**

Acquisitions

Creative acquired 3Dlabs in fiscal 2002. The acquisition was accounted for under the purchase method of accounting, and accordingly, the estimated fair value of assets acquired and liabilities assumed and the results of operations were included in Creative's consolidated financial statements as of the effective date of the acquisition through the end of the period. There were no significant differences between the accounting policies of Creative and 3Dlabs.

Goodwill and other intangible assets
Goodwill and other intangible assets are stated at cost and relate principally to the acquisition of new subsidiaries accounted for under the purchase method. Under this method, the purchase price has been allocated to the assets acquired, liabilities assumed and in-process technology based on their estimated fair market values at the dates of acquisition. Amounts allocated to acquired in-process technology are expensed in the period in which the acquisition is consummated. The goodwill and identifiable intangible assets acquired in connection with the acquisition of 3Dlabs have been accounted for in accordance with SFAS 141 and SFAS 142, "Business Combinations" and "Goodwill and Other Intangible Assets." Intangible assets are amortized on a straight line basis over the estimated useful lives of the assets, ranging from one to seven years. Goodwill is not subject to amortization, but will be evaluated at least annually for impairment.

Creative reviews for impairment of goodwill and other intangible assets whenever events indicate that the carrying amount might not be recoverable. Factors that Creative may consider important which could trigger an impairment review include the followings:

- significant under performance relative to expected historical or projected future operating results;
- significant changes in the manner of use of the acquired assets or the strategy for Creative's overall business;
- significant negative industry or economic trends;
- significant decline in Creative's stock price for a sustained period; and
- Creative market capitalization relative to net book value.

When Creative determines that the carrying value of goodwill and other intangibles assets may not be recoverable based upon the existence of one or more of the above indicators, Creative measures any impairment based on a projected discounted cash flow method using a discount rate determined by the management to be commensurate with the risk inherent in Creative's current business model.

A summary of goodwill and other intangible assets are as follows (in US$'000):

	As of June 30	
	2002	2001
Gross carrying value:		
Goodwill	$ 91,976	$ –
Other intangible assets	33,682	45,461
Total gross carrying value	**125,658**	**45,461**
Accumulated amortization:		
Goodwill	–	–
Other intangible assets	(15,788)	(41,604)
Total accumulated amortization	**(15,788)**	**(41,604)**
Net goodwill and other intangible assets	**$ 109,870**	**$ 3,857**

Goodwill and other intangible assets fully amortized were excluded from above. Other intangible assets amortization expense was $5.2 million, $6.3 million and $12.8 million for fiscal year 2002, 2001 and 2000, respectively, and estimated to be $9.1 million in fiscal year 2003 and $1.8 million each in fiscal year 2004 to fiscal 2007.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Revenue recognition
Creative generally recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, price is fixed or determinable, and collectibility is probable. Allowances are provided for estimated returns, discounts and warranties, based on historical experience, current economic trends and changes in customer demand and acceptance of its products. Such allowances are adjusted periodically to reflect actual and anticipated experience. When recognizing revenue, Creative records estimated reductions to revenue for customer and distributor programs and incentive offerings, including price protection, promotions, other volume-based incentives and rebates.

Research and development
Research and development costs are charged to operations as incurred.

Restructuring costs and accruals for excess facilities
In accordance with the provisions of EITF Issue No. 94-3, "Accounting for Restructuring Charges," and Staff Accounting Bulletin No.100, "Restructuring and Impairment Charges," Creative records restructuring costs when it commits to an exit plan and significant changes to the exit plan are not likely. The estimated loss on facilities which Creative intends to sublease is based on estimates of the timing and amount of sublease income. Creative reassesses this liability quarterly based on market conditions.

Assessment of the probability of the outcome of current litigation
Creative record accruals for loss contingencies when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated.

Income taxes
Deferred tax assets and liabilities, net of valuation allowances, are established for the expected future tax consequences of events resulting from the differences between the financial reporting and income tax bases of Creative's assets and liabilities and from tax credit carry forwards. No provision has been made for the undistributed earnings of Creative's subsidiaries outside of Singapore since it is Creative's intention to reinvest these earnings in those subsidiaries. Reinvested earnings of such subsidiaries have been immaterial to date.

Concentrations of credit risk
Financial instruments that potentially subject Creative to significant concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. Creative limits the amount of credit exposure to any one financial institution. Creative sells its products to original equipment manufacturers, distributors and key retailers. Creative believes that the concentration of credit risk in its trade receivables is substantially mitigated due to performance of ongoing credit evaluations of its customers' financial condition, use of short collection terms, use of letters of credit in certain circumstances, procurement of credit insurance coverage and the geographical dispersion of sales. Creative establishes allowances for doubtful accounts, returns and discounts for specifically identified doubtful accounts, returns and discounts based on credit profiles of its customers, current economic trends, contractual terms and conditions and historical payment, return and discount experience.

Stock-based compensation
Creative accounts for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees", and related Interpretations. Accordingly, compensation expense for stock option is measured as the excess, if any, of the fair value of Creative's stock at the date of the grant over the stock option exercise price. In addition, Creative provides pro forma disclosures as required under SFAS 123, "Accounting for Stock-Based Compensation." See Note 8.

Reclassification
In fiscal 2002, Creative adopted EITF Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." EITF Issue No. 01-9 provides that consideration from a vendor to a reseller of the vendor's products is generally presumed to be an adjustment to the selling prices of the vendor's products and, therefore, should be classified as a reduction of revenue. As a result of the adoption, certain consideration paid to distributors and resellers of its products has been reclassified as a revenue offset rather than as selling, general and administrative expense. Prior years' financial statements have been reclassified to conform to this presentation.

Recently issued accounting pronouncements
In July 2002, the FASB issued SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS 146 addresses significant issues regarding the recognition, measurement, and reporting of costs that are associated with exit and disposal activities, including restructuring activities that are currently accounted for pursuant to the guidance that the EITF has set forth in EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)." The scope of SFAS 146 also includes (1) costs related to terminating a contract that is not a capital lease and (2) termination benefits that employees who are involuntarily terminated receive under the terms of a one-time benefit arrangement that is not an ongoing benefit arrangement or an individual deferred-compensation contract. SFAS 146 will be effective for exit or disposal activities that are initiated after December 31, 2002. Creative does not expect the adoption of this statement to have a material impact on Creative's financial statements.

In August 2001, the FASB issued SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS 144 supersedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", and the accounting and reporting provisions relating to the disposal of a segment of a business of Accounting Principles Board Opinion No. 30. Adoption of SFAS 144 is not expected to have a material impact on Creative's consolidated financial statements.

In August 2001, the FASB issued SFAS 143, "Accounting for Asset Retirement Obligations." SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. SFAS 143 will be adopted for Creative's fiscal year beginning July 1, 2002. Adoption of SFAS 143 is not expected to have a material impact on the consolidated financial statements.

In July 2001, the FASB issued SFAS 142, "Goodwill and Other Intangible Assets." It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Under SFAS 142, goodwill will be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. Creative will adopt SFAS 142 effective July 1, 2002 for business combinations completed prior to June 30, 2001. Upon adoption, amortization of goodwill recorded for business combinations consummated prior to July 1, 2001 will cease, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS 141 will be reclassified to goodwill. In connection with the adoption of SFAS 142, the Company will be required to perform a transitional goodwill impairment assessment. Adoption of these statements is not expected to have a material impact on the consolidated financial statements.

NOTE 2 – NET (LOSS) INCOME PER SHARE

In accordance with SFAS 128, "Earnings per Share", Creative reports both basic earnings per share and diluted earnings per share. Basic earnings per share is computed using the weighted average number of ordinary shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of ordinary and potentially dilutive ordinary equivalent shares outstanding during the period. Ordinary equivalent shares are excluded from the computation if their effect is anti-dilutive. In computing the diluted earnings per share, the treasury stock method is used to determine, based on average stock prices for the respective periods, the ordinary equivalent shares to be purchased using proceeds received from the exercise of such equivalent shares. Other than the dilutive effect of stock options, there are no other financial instruments that would impact the weighted average number of ordinary shares outstanding used for computing diluted earnings per share. The potentially dilutive ordinary equivalent shares outstanding under the employee share purchase plan were not material.

Following is a reconciliation between the average number of ordinary shares outstanding and equivalent shares outstanding (in '000):

	As of June 30		
	2002	2001	2000
Weighted average ordinary shares outstanding	73,182	79,049	82,028
Weighted average dilutive stock options outstanding	–	–	4,584
Weighted average ordinary shares and equivalents outstanding	**73,182**	**79,049**	**86,612**

For the fiscal year 2002 and 2001, approximately 2.4 million and 2.0 million potentially dilutive shares were excluded from the determination of diluted net loss per share, as the effect of including such shares is anti-dilutive.

NOTE 3 – BALANCE SHEET DETAIL (in US$'000)

	As of June 30	
	2002	2001
Inventory:		
Raw materials	$ 33,826	$ 66,509
Work in progress	5,658	6,882
Finished products	69,065	82,159
Total inventory	**$ 108,549**	**$ 155,550**

	Estimated Useful Life	As of June 30	
		2002	2001
Property and equipment:			
Land and buildings	25 years	$ 83,698	$ 83,203
Construction in progress	–	1,013	96
Machinery and equipment	3 - 6 years	50,880	54,539
Furniture, fixtures and office equipments	2 - 8 years	82,690	62,430
Leasehold improvements	Term of lease	11,981	12,879
		230,262	**213,147**
Accumulated depreciation		(125,514)	(102,612)
Net property and equipment		**$ 104,748**	**$ 110,535**

Included in property and equipment are assets purchased under capital lease obligations with a cost and accumulated depreciation of approximately $10.4 million and $2.4 million for fiscal year 2002 and $0.3 million and $0.04 million for fiscal 2001, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 – BALANCE SHEET DETAIL (in US$'000) (Cont'd)

	As of June 30	
	2002	2001
Other non-current assets:		
Goodwill	$ 91,976	$ –
Other intangible assets	17,894	3,857
Other non-current assets	5,252	49
Total other non-current assets	**$ 115,122**	**$ 3,906**

	As of June 30	
	2002	2001
Other accrued liabilities:		
Marketing accruals	$ 20,764	$ 27,104
Payroll accruals	19,188	18,365
Royalty accruals	5,092	7,483
Restructuring accruals	596	4,452
Other accruals	32,191	40,731
Total other accrued liabilities	**$ 77,831**	**$ 98,135**

NOTE 4 – LEASES AND COMMITMENTS

Creative leases the use of land and certain of its facilities and equipment under non-cancelable operating lease arrangements. The land and facility leases expire at various dates through 2024 and provide for fixed rental rates during the terms of the leases.

Minimum future lease payments for non-cancelable leases as of June 30, 2002, were as follows (in US$'000):

	Operating Leases
Fiscal years ended June 30,	
2003	$ 11,912
2004	9,680
2005	7,722
2006	5,282
2007	1,926
Thereafter	14,402
Total minimum lease payments	**$ 50,924**

Rental expense under all operating leases was $11.0 million, $11.8 million and $12.2 million for fiscal 2002, 2001 and 2000, respectively.

Future minimum lease obligations, which are secured by the underlying assets, as of June 30, 2002, under capital leases are as follows (in US$'000):

	Capital Leases
Fiscal years ended June 30,	
2003	$ 3,654
2004	3,018
2005	1,323
2006	68
2007	47
Thereafter	–
Total minimum lease commitments	$ 8,110
Less: Amount representing interest	(191)
Total capital lease obligations	**$ 7,919**

NOTE 5 – COMPREHENSIVE INCOME

The components of total comprehensive income are as follows (in US$'000):

	Years ended June 30		
	2002	2001	2000
Net (loss) income	$ (19,727)	$ (130,373)	$ 161,012
Movement in unrealized holding gains (losses)	15,042	(26,899)	169,357
Reclassification adjustments:			
– Gains (losses) included in net (loss) income	(16,655)	(124,800)	(10,814)
	(1,613)	(151,699)	158,543
Total comprehensive (loss) income	**$ (21,340)**	**$ (282,072)**	**$ 319,555**

NOTE 6 – SHARE REPURCHASES

Details of Share repurchases by Creative during the fiscal years since the commencement of the program on November 6, 1998 are set out below:

Years ended June 30,	Number of Shares Repurchased (in millions)	Average Price (US$)
1999	10.0	$ 14
2000	5.9	$ 17
2001	7.7	$ 12
2002	2.7	$ 7
Total	**26.3**	**$ 13**

At the 2001 Annual General Meeting ("AGM") held on October 31, 2001, the shareholders approved the share repurchase mandate allowing Creative to buy up to 10% of the issued share capital of Creative as at the date of the AGM. This amounts to approximately 7.2 million shares. This authority to repurchase shares shall continue in force unless revoked or revised by the shareholders in a general meeting, or until the date that the next AGM of Creative is held or is required to be held, whichever is the earlier.

In accordance with Singapore statutes, such repurchases are recorded as a reduction in retained earnings.

NOTE 7 – DIVIDENDS

At the Annual General Meeting held on October 31, 2001, Creative's shareholders approved an ordinary dividend of $0.25 for each outstanding ordinary share of Creative for the fiscal year ending June 30, 2002. Dividends of $18.0 million were paid on December 4, 2001 to all shareholders of record as of November 20, 2001. Creative paid an ordinary dividend of $0.25 and a special dividend of $0.25 amounting to $39.4 million in the previous fiscal year.

NOTE 8 – EMPLOYEE SHARE PURCHASE AND STOCK OPTION PLANS

Creative Employee Share Purchase Plan

As approved by the shareholders in November 1999, Creative has adopted the 1999 Employee Share Purchase Plan that permits substantially all employees to purchase ordinary shares of Creative. Participating employees may purchase ordinary shares through regular payroll deductions accumulated during each offering period at a purchase price of 85% of the lower of the fair market value on the offering date or on the purchase date. Each offering period consists of four six months purchase periods, except for the first purchase period in the first offering period, which was four months. A total of 1.0 million ordinary shares were reserved for issuance under this plan. In addition, on each July 1, the aggregate number of ordinary shares reserved for issuance under the plan shall be increased automatically by 1% of the total number of outstanding ordinary shares of Creative on the immediately preceding June 30; provided that the aggregate shares reserved under this plan shall not exceed 5.0 million shares.

In fiscal 2002, 2001 and 2000, 248,000, 225,000 and 57,000 shares were issued at a weighted average exercise price of $5.19, $10.80 and $15.25 per share under Creative's Employee Share Purchase Plan respectively.

Creative Employee Stock Option Plans

In December 1994, Creative adopted the new Creative Technology Employees' Share Option Scheme (the "New Plan"). Options granted under this plan were in accordance with Section 422(a) of the US Internal Revenue Code of 1986, as amended. On November 13, 1996, at a special meeting, shareholders approved certain changes to the New Plan to make it less restrictive. Under the amended New Plan, the total number of shares that could be granted was increased to an overall maximum of 15% of the issued share capital of Creative. The amended New Plan also provided for incentive stock options to be granted to employees of Creative on a quarterly basis, at the average market price established on the five days closing immediately prior to the date of grant. The options vested at the rate of 25% at the end of each anniversary of the grant date and were exercisable over a period not exceeding five years from the date of grant.

As of October 6, 1998, Creative is no longer subject to the listing rules of the Singapore Exchange but is required only to comply with the listing rules of NASDAQ, including rules governing stock option plans. Since many of Creative employees and shareholders are located in the United States of America, Creative has obtained shareholders' approval on December 30, 1998 to replace the New Plan with the Creative Technology (1999) Share Option Scheme ("1999 Scheme"), which is more in accordance with US practice. The 1999 Scheme allows options to be granted to full-time employees as well as consultants and non-executive directors. The total number of shares that may be granted as options is 7.5 million provided that such amount shall be automatically increased on the first day (July 1) of each of the five fiscal years ending June 30, 2001, 2002, 2003, 2004 and 2005 by four percent of the issued share capital of Creative as at the last day of the immediate preceding fiscal year. The Option Committee has the discretion to decide the vesting schedule in the letter of offer. If it is not specifically stated in the letter of offer, 1/4 of the total amount of the grant vest on the first anniversary of the grant date and 1/48 of the total amount of the grant on the last day of each calendar month thereafter. The exercise price of options granted under the 1999 Scheme may be less than the fair market value of the shares as of the date of grant and the options expire after the tenth anniversary of the date of grant, except in the case of options granted to participants other than employees, options expire not later than the fifth anniversary of the date of grant.

In fiscal 1999, Creative granted 2.9 million options under the 1999 Scheme at a weighted average exercise price of $10.14, which was below fair market value, resulting in deferred share compensation of $5.1 million which is being amortized over the vesting period of the underlying options.

In fiscal 2000, Creative granted 4.3 million options under the 1999 Scheme at a weighted average exercise price of $9.14, which was below fair market value, resulting in deferred share compensation of $6.3 million which is being amortized over the vesting period of the underlying options.

No options were granted under the 1999 Scheme in fiscal 2001.

NOTE 8 – EMPLOYEE SHARE PURCHASE AND STOCK OPTION PLANS (Cont'd)

Effective April 2000, unvested stock options to purchase 0.2 million shares of Creative's ordinary stock granted under the New Plan and 1999 Scheme to employees of a subsidiary were canceled in exchange for the right to receive options granted by the subsidiary. The employees are allowed to retain outstanding options vested on March 31, 2000 until March 31, 2001 at which time unexercised options were canceled. In May 2000, the subsidiary adopted a separate stock option plan and employees were then granted options under this plan. See "Subsidiary Stock Option Plan" below for additional information.

In fiscal 2002, Creative granted 7.1 million options under the 1999 Scheme at a weighted average exercise price of $4.57. 2.9 million options granted in fiscal 2002 are below fair market value, resulting in a deferred share compensation of $0.8 million being amortized over the vesting period of the underlying options. The 7.1 million options that were granted in fiscal 2002 included 1.6 million Creative's options that were granted to assume 3Dlabs' outstanding employee stock options. (See Note 15)

Creative Employee Stock Option Plans
A summary of options granted to employees and non-employee directors under Creative's stock option plans is presented below:

	Options Outstanding	
	Number of Shares ('000)	Weighted Average Exercise Price ($)
Balance as of June 30, 1999	**7,117**	**9.14**
Granted – at fair market value	697	11.81
– below fair market value	4,346	9.14
Exercised	(2,214)	7.17
Canceled	(1,052)	12.54
Balance as of June 30, 2000	**8,894**	**9.44**
Granted – at fair market value	–	–
– below fair market value	–	–
Exercised	(928)	7.31
Canceled	(1,185)	13.49
Balance as of June 30, 2001	**6,781**	**9.01**
Granted – at fair market value	2,509	4.72
– below fair market value	2,931	4.80
– pursuant to the acquisition of 3Dlabs (see Note 15)	1,641	3.93
Exercised	(1,070)	6.45
Canceled	(913)	9.18
Balance as of June 30, 2002	**11,879**	**6.56**

The total number of options exercisable at June 30, 2002, 2001 and 2000 under the New Plan and 1999 Scheme were 4,031,000, 3,843,000 and 2,594,000, respectively.

Summary of outstanding options under Creative's employee stock option plans

The following table summarizes option information for Creative's employee stock option plans (New Plan and 1999 Scheme) as at June 30, 2002.

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding ('000)	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price ($)	Number Exercisable ('000)	Weighted Average Exercise Price ($)
$1.00 to $2.99	556	8.85	2.85	36	2.85
$3.00 to $4.99	5,401	9.28	4.45	32	4.08
$5.00 to $7.99	994	8.37	6.10	353	5.18
$8.00 to $10.99	4,808	6.83	9.13	3,498	9.16
$11.00 to $14.99	–	–	–	–	–
$15.00 to $22.00	120	1.68	19.73	112	19.83
	11,879	8.11	6.56	4,031	9.01

Subsidiary Stock Option Plan

During fiscal 2000, a consolidated subsidiary of Creative established a stock option plan, which allows for subsidiary employees and others to be granted options to purchase shares of stock in the subsidiary. The total number of shares that may be granted as options under the subsidiary 2000 Stock Option Plan ("2000 Plan") is 8 million shares provided that such amounts shall be automatically increased on the first day (July 1) of each of the five fiscal years ending June 30, 2001, 2002, 2003, 2004 and 2005 by the lesser of (i) three hundred thousand shares or (ii) one percent of the issued share capital of the Company as at the last day of the immediately preceding fiscal year. The exercise price of options granted under the 2000 Plan may be less than the fair market value of the shares as of the date of grant and the options expire after the tenth anniversary of the date of grant.

In December 1999, the subsidiary agreed to issue options to certain key executives to acquire 1.2 million shares at an exercise price of $1.00 per share. The options were granted in May 2000, vest over four years and are exercisable for 10 years.

In May 2000, the subsidiary granted options to its employees to acquire 2.1 million shares at an exercise price of $2.50 per share. These options vest over four years and are exercisable for 10 years. In May 2000, the subsidiary also granted options to certain employees of Creative to acquire 0.47 million shares at an exercise price of $2.50 per share and 0.06 million shares at $1.00 per share. The options vest over four years effective from April 1, 2000 and are exercisable for 5 years.

NOTE 8 – EMPLOYEE SHARE PURCHASE AND STOCK OPTION PLANS (Cont'd)

Because the exercise prices for the aforementioned grants are below the deemed fair value per ordinary share of $4.50, the grants give rise to a deferred share compensation expense of approximately $9.2 million. The compensation expense is being amortized over the four-year vesting period of the underlying options and amortization of deferred share compensation expense is subject to changes due to the impact of future grants and cancellation of options, if any.

In fiscal 2001, the subsidiary granted 0.9 million options under the 2000 Plan at a weighted average exercise price of $2.45. Included in the options granted during the fiscal year were replacement options granted to certain employees of Creative Technology Ltd to acquire 235,000 and 30,000 of the subsidiary company's shares at an exercise price of $2.50 and $1.00 per share respectively. These options were granted in lieu of the cancellation of 470,000 shares at an exercise price of $2.50 per share and 60,000 shares at $1.00 per share. The replacement options vested immediately on grant date and the share compensation expense arising from replacement of options amounted to $0.7 million which was expensed in fiscal 2001.

The subsidiary did not grant options in fiscal 2002.

A summary of options granted to employees, consultants and directors under the subsidiary's stock option plan is presented below:

	Options Outstanding	
	Number of Shares ('000)	Weighted Average Exercise Price ($)
Balance as of June 30, 2000	**3,841**	**1.98**
Options granted	899	2.45
Options canceled	(2,540)	1.80
Balance as of June 30, 2001	**2,200**	**2.39**
Options granted	–	–
Options canceled	(2,195)	2.39
Balance as of June 30, 2002	**5**	**2.50**

The following table summarizes option information for the subsidiary employee stock option plan as at June 30, 2002:

Range of Exercise Price	Number Outstanding ('000)	Weighted Average Remaining Contractual Life (years)	Number Exercisable ('000)
$2.50	5	8.05	2

Creative and Subsidiary Pro Forma Disclosures

The fair value of the purchase rights under the Creative employee share purchase plan and stock option plan is estimated using the Black-Scholes model based on the following assumptions:

	Fiscal 2002	Fiscal 2001	Fiscal 2000
Volatility	60%	50%	60%
Risk-free interest rates			
Share purchase plan	2.18% to 5.16%	3.78% to 6.09%	6.22% to 6.81%
Stock options	2.16% to 5.16%	–	5.20% to 6.65%
Dividend yield	2.5%	–	1.0%
Expected lives:			
Share purchase plan	6 months	6 months	6 months
Stock options	0.01 years after vest date	–	0.01 years after vest date

	Years ended June 30		
	2002	2001	2000
Weighted average fair value of stock options granted:			
Stock options:			
At market	$ 1.53	$ –	$ 5.02
Below market	$ 3.74	$ –	$ 4.71

The fair value of the purchase rights under the subsidiary stock option plan is estimated using the Black-Scholes model based on the following assumptions:

	Fiscal 2002	Fiscal 2001	Fiscal 2000
Volatility	–	–	–
Risk-free interest rates	–	3.78% to 6.34%	5.99% to 6.40%
Dividend yield	–	–	–
Expected lives	–	0.01 years after vest date	0.01 years after vest date

NOTE 8 – EMPLOYEE SHARE PURCHASE AND STOCK OPTION PLANS (Cont'd)

Had compensation cost for Creative's employee share purchase and stock option plans, and the subsidiary's stock option plan been determined based on the fair value at the grant dates using the Black-Scholes model, Creative's net income (loss) and net income (loss) per share would have been as follows:

In US$'000, except for per share data

	Years ended June 30		
	2002	2001	2000
Net (loss) income:			
As reported	$ (19,727)	$ (130,373)	$ 161,012
Pro forma	$ (23,463)	$ (134,868)	$ 151,450
Diluted (loss) earnings per share:			
As reported	$ (0.27)	$ (1.65)	$ 1.86
Pro forma	$ (0.32)	$ (1.71)	$ 1.78

NOTE 9 – INCOME TAXES

Creative was granted a Pioneer Certificate in 1990 under the Singapore Economic Expansion Incentives (Relief from Income Tax) Act, Cap. 86 for the design and manufacture of digital computer video, audio and multimedia products, including personal computers and related components, chipsets and software but not including interest income. The Pioneer Certificate exempted income derived from such activities ("Pioneer Income") from tax in Singapore, subject to certain conditions. The Pioneer Certificate expired in March 2000. Such status had the effect of reducing Creative's provision for income taxes by approximately $15.4 million, $26.4 million and $43.3 million, or $0.18, $0.29 and $0.46 per share, for fiscal 2000, 1999 and 1998 respectively. The corporate income tax rate in Singapore, which would otherwise be applicable, would have been 25.5% for fiscal year 2000, and 26% for fiscal years 1998 to 1999.

Creative has applied for a separate and new Pioneer Certificate. If Creative is awarded this new Pioneer Certificate, profits under the new Pioneer Certificate will be exempted from tax in Singapore. For fiscal 2000 (covering period from April 1, 2000 to June 30, 2000), 2001 and 2002, corporate tax was provided for in full based on the standard tax rates of 25.5%, 24.5% and 22% respectively as the terms and agreements of the new Pioneer Certificate is currently still under negotiation as at to-date. The new Pioneer Certificate will result in the reduction of Creative's provision for income taxes, subject to the terms and agreement by the Singapore Comptroller of Income Tax. The corporate income tax rate in Singapore, which would otherwise be applicable, would be 22.0% for fiscal 2002, 24.5% for fiscal 2001 and 25.5% for fiscal 2000.

The Singapore and other components of (loss) income before income taxes are as follows (in US$'000):

	Years ended June 30		
	2002	2001	2000
Singapore	$ 45,738	$ 25,193	$ 96,577
Other countries	(57,924)	(146,688)	74,439
(Loss) income before income taxes and minority interest	**$ (12,186)**	**$ (121,495)**	**$ 171,016**

The provision for income taxes consists of (in US$'000):

	Years ended June 30		
	2002	2001	2000
Singapore	$ 4,780	$ 7,971	$ 7,376
Other countries	918	438	2,096
Provision for income taxes	**$ 5,698**	**$ 8,409**	**$ 9,472**

Creative's effective tax provision for fiscal 2002, 2001 and 2000 reconciles to the amount computed by applying the Singapore statutory rate of 22.0% for 2002, 24.5% for 2001, and 25.5% for 2000 to income before income taxes and minority interest, as follows (in US$'000):

	Years ended June 30		
	2002	2001	2000
Income tax (benefit) at Singapore statutory rate	$ (2,681)	$ (29,766)	$ 43,609
Tax exempt income			
Singapore	(13)	(834)	(18,316)
Others	–	–	–
Non-deductible expenses and write-offs	3,013	5,486	3,245
Change in valuation allowances	(657)	8,699	5,135
Rate differences and others	6,036	24,824	(24,201)
Provision for income taxes	**$ 5,698**	**$ 8,409**	**$ 9,472**

Deferred tax assets at June 30, 2002 and 2001 consisted of the following (in US$'000):

	As of June 30	
	2002	2001
Non-deductible reserves	$ 33,778	$ 26,388
Net operating loss carryforwards	20,099	22,518
Other	1,765	2,558
Total deferred tax assets	**55,642**	**51,464**
Valuation allowance for deferred tax assets	(55,642)	(51,464)
	$ –	$ –

Included in fiscal 2002 and 2001 are deferred tax assets comprising net operating losses of $0.2 million and $1.9 million and non-deductible reserves of $4.6 million and $5.5 million respectively mainly for the United States previously not identified and new subsidiary acquired.

NOTE 9 – INCOME TAXES (Cont'd)

Creative had Irish net operating loss carryforward of approximately $1.9 million and $23.7 million and US net operating loss carryforward of approximately $47.8 million and $41.9 million, as at June 30, 2002 and June 30, 2001, respectively. The Irish net operating losses have an indefinite carryforward period while the US net operating losses expire between 2005 to 2021. The utilization of these net operating losses by Creative is subject to certain conditions.

A full valuation allowance has been recorded for Creative's deferred tax assets at June 30, 2002 and 2001, as management believes substantial uncertainty exists regarding the realizability of these assets.

Creative has United States tax deductions not included in the net operating loss carryforward described above aggregating approximately $53.6 million at June 30, 2002 and June 30, 2001, as a result of the exercise of employee stock options, the tax benefit of which has not been realized. The tax benefit of the deductions, when realized will be accounted for as a credit to additional paid-in capital rather than a reduction of the income tax provision.

NOTE 10 – CREDIT FACILITIES AND SHORT TERM OBLIGATIONS

On March 13, 1996, Creative Technology Centre Pte Ltd ("CTC"), a Singapore subsidiary of Creative, entered into an agreement with two banks for an eight year term loan facility for up to S$60.0 million ($34.0 million) to finance the construction of Creative's headquarters building in Singapore. The loan is repayable in nineteen quarterly installments comprising eighteen installments of S$1.5 million ($0.9 million) and a final installment for the remaining S$30.9 million ($17.6 million). The repayment commenced on July 5, 1998. The interest on the outstanding loan balance is payable at the banks' cost of funds plus 1.25%. The interest rate charged for fiscal 2002 was at 2.19%. The loan is secured by a first mortgage on the building and by way of a fixed and floating charge over all assets of CTC. At June 30, 2002, S$33.9 million ($19.2 million) was outstanding and repayable by fiscal year 2003.

A portion of the construction of the headquarters building is also being financed in equal parts by Creative and Bukit Frontiers Pte Ltd. ("BFPL"), a company owned by Creative's Chairman and CEO, Sim Wong Hoo. At June 30, 2002, loans extended and equity contributed by Bukit Frontiers Pte Ltd. totaled S$12.5 million ($7.1 million) and S$0.5 million ($0.4 million), respectively.

Creative's newly acquired subsidiary, 3Dlabs, has an overdraft facility for 2.0 million Pounds Sterling expiring on December 31, 2002 and the outstanding balance was $3.7 million as at June 30, 2002. The facility charges interest at a rate of 1.0% above the bank's currency base rate if the overdraft balance is less than 2.0 million Pounds Sterling and 4.0% above the bank's currency base rate on any amount exceeding 2.0 million Pounds Sterling. The bank's currency base rate was 4.0% at June 30, 2002. A $3.5 million restricted investment with a Bermuda financial institution is held as collateral for this facility in the form of a certificate of deposit (see Note 1).

In August 2000, 3Dlabs entered into a $1.0 million credit facility to finance certain software purchases. The facility requires equal quarterly installments of $0.25 million and expired December 31, 2001. The repayments under the credit facility were revised in 2001, resulting in equal monthly repayments of $0.08 million commencing January 2002. The advances under the facility accrue interest at a per annum rate of the bank's currency base rate of 4.0% plus 1%. At June 30, 2002, $0.75 million was outstanding. A $1.0 million restricted investment with a Bermuda financial institution was held as collateral for this facility in the form of a certificate of deposit (see Note 1).

3Dlabs has also entered into a Loan and Security Agreement with a financial institution in an amount up to $20.0 million or 85% of the qualified accounts receivable of 3Dlabs' U.S. companies, whichever is less. The Agreement expires in July 2004 and is secured by all tangible and intangible assets of 3Dlabs. Borrowings under the Agreement bear interest at 1.25% above the institution's prime rate. The Agreement contains certain covenants, including that 3Dlabs meet certain agreed-upon financial covenants. Borrowings under the Agreement at June 30, 2002 was $1.4 million.

Creative has various other credit facilities relating to overdrafts, letters of credit, bank guarantees and short term loans with several banks totaling approximately $115.3 million at June 30, 2002. Within these credit facilities, sub-limits have been set on how Creative may utilize the overall credit facilities. At June 30, 2002, $3.7 million and $0.75 million in overdraft and short term loans (as mentioned above), $0.6 million in letters of credit and $1.5 million in bank guarantees were drawn under these facilities. Facilities under letters of credit and bank guarantees bear interest at approximately the banks' prime rates, and for interest rates on overdraft and short term loan facilities, please see above comments.

NOTE 11 – MINORITY INTEREST

In May 2000, a wholly owned subsidiary issued 5.0 million convertible preference shares at $4.50 per share, resulting in net proceeds to the subsidiary of $22.5 million. In November 2001, Creative entered into agreements with the holders of these 5.0 million convertible preference shares to repurchase all such shares for $10.0 million cash. The repurchase was completed during the quarter ended March 31, 2002 and the excess of carrying value over the repurchase price paid of $11.8 million was credited to additional paid in capital.

NOTE 12 – OTHER CHARGES

In fiscal 2002, Creative wrote off $26.1 million of in-process technology arising from the acquisition of 3Dlabs (see Note 15).

In March 2001, Creative announced a series of cost-cutting measures which included a worldwide workforce reduction of approximately 10%, closure of Creative's manufacturing location in Pennsylvania and transferring these manufacturing activities to Creative's other facilities, and sharp cutbacks in selected non-revenue generating Internet initiatives. As a result of these measures and other market changes, Creative in fiscal year 2001 recorded restructuring and other charges of $22.8 million which was included in operating expenses and an inventory charge of $8.2 million to cost of goods sold. The $22.8 million restructuring and other charges comprised $5.1 million in employee separation costs, $3.3 million in facility exit costs, fixed asset impairment write-downs of $3.2 million and write off of other assets acquired from Aureal amounting to $11.2 million.

Employee separation costs represent the costs of involuntary severance benefits for approximately 400 positions. As of June 30, 2002, all the affected employees had separated from the Company. Facility exit costs primarily include lease termination and unutilized capacity costs. The accruals for employee separation costs and exit costs are included in accrued liabilities in the consolidated balance sheet.

NOTE 12 – OTHER CHARGES (Cont'd)

The following table displays the movements of the accruals established for employee separation and facility exit costs for the fiscal year 2002 (in US$'000):

	As of June 30, 2001	Amounts Paid	Adjustments for Over Accruals	As of June 30, 2002
Employee separation costs	$ 1,877	$ (1,848)	$ (29)	$ -
Facility exit costs	2,575	(1,918)	(61)	596
Total	**$ 4,452**	**$ (3,766)**	**$ (90)**	**$ 596**

The adjustments for over accruals of $90,000 were reversed to the selling, general and administrative expenses.

Fixed and other asset impairment write-downs are attributed to manufacturing and other equipment associated with the facilities being closed as well as certain other intangible assets which have been impaired as a result of recent changes in market conditions.

The $8.2 million inventory charge primarily relates to digital video recorders and graphics which were written down to their estimated sales values as a result of management's decision to exit from these businesses.

Included in the results of operations for fiscal 2000 were US$20.0 million for the settlement of all outstanding litigation claims between Aureal and Creative.

NOTE 13 – LITIGATION

During the course of its normal business operations, Creative and its subsidiaries are involved from time to time in a variety of intellectual property and other disputes, including claims against Creative alleging copyright infringement, patent infringement, contract claims, employment claims and business torts. Currently such disputes exist with, among other entities, Sunonwealth Electric Machine Industry Co. (a patent infringement action pending in the Northern District of California), under which Creative has a contractual right of indemnity from Adda Corporation, and the Lemelson Foundation (an action that involved patent claims by Lemelson against over 500 entities, including Creative, which action has been stayed pending resolution of issues in third party litigation). Creative and 3Dlabs have also been named as defendants in a class action lawsuit by a purported class of 3Dlabs shareholders, alleging breach of fiduciary duty in connection with the 3Dlabs merger. Based upon the information currently available, Creative believes that there are strong defenses and the lawsuits are without merit. Creative also from time to time receives licensing inquiries and/or threats of potential future patent claims from a variety of entities, including IBM and Lucent. Creative believes it has valid defenses to the various claims and counterclaims asserted against it. However, should any of these plaintiffs prevail in their claims or counterclaims, Creative does not expect there to be any consequent material adverse effect on its financial position or results of operations.

NOTE 14 – INVESTMENTS

Due to a continued downturn in global equity markets, Creative experienced a decline in its investment portfolio in fiscal 2002 and 2001, resulting in net investment losses of $45.4 million and $148.5 million, respectively. Net investment losses of $45.4 million in fiscal 2002 include permanent write-downs of quoted and unquoted investments by $49.3 million and net gains from quoted investments of $3.9 million. Included in the results of operations for fiscal 2001 are net gains from quoted investments of $51.8 million and permanent write-downs of quoted and unquoted investments by $200.3 million.

NOTE 15 – BUSINESS COMBINATION

In May 2002, Creative completed the acquisition of 3Dlabs, a graphics vendor, supplying graphics accelerator solutions for professionals in Computer Aided Design ("CAD"), Digital Content Creation ("DCC"), and visual simulation markets. Creative believes that the acquisition will provide Creative a significant competitive advantage in the graphics space and allow Creative to re-emphasize graphics products.

To acquire the remaining outstanding capital stock of 3Dlabs, Creative paid $37.0 million in cash, issued approximately 6.3 million shares of Creative's ordinary shares valued at approximately $71.7 million at the time of closing, and assumed 3Dlabs' outstanding options exercisable into approximately 1.6 million shares of Creative ordinary shares valued at approximately $12.0 million at the time of closing. As a result of the acquisition, Creative also assumed 3Dlabs net liabilities of $21.1 million. In addition, Creative incurred approximately $1.3 million in transaction fees, including legal, valuation and accounting fees. The ordinary shares issued were valued in accordance with EITF Issue No. 99-12, "Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination," using the average for the Creative closing prices ordinary shares during the two days before and two days after (and including) the day on which the total number of Creative shares issuable to holders of 3Dlabs common shares were fixed and determinable. The assumed stock options were valued using the Black-Scholes valuation model, with a volatility rate of 60%, a risk-free interest rate of 2.20% to 4.93%, expected dividend yield of 2.5%, and an estimated vest term of 0.01 years after vest date.

Of the total assumed stock options of 3Dlabs, approximately 1.3 million stock options with an intrinsic value of $7.0 million were unvested. In accordance with FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation," these unvested options were accounted for as deferred stock-based compensation and are being recognized as compensation expense over their related vesting periods. Total stock-based compensation expense with respect to the unvested options totaled $0.3 million in fiscal 2002.

Creative accounted for the acquisition using the purchase method of accounting and has included the results of 3Dlabs from the acquisition date of May 15, 2002. The allocation of the purchase price to in-process technology and identifiable intangible assets acquired was based on independent appraisals. The income approach, which includes an analysis of the markets, cash flows and risks associated with achieving such cash flows, was the primary technique utilized in valuing the existing technology, in-process technology and non-competition agreements. The estimated net free cash flows generated by the existing technology, in-process technology and non-competition agreements were discounted at rates ranging from 16% to 40%. In estimating the fair value of the patents/core technology and trade name/trademarks, royalty savings approach was used, whereby the value of an asset was estimated by capitalizing the royalties saved, with discount rates ranging from 18% to 28%.

The following table summarizes the estimated fair values of the tangible assets acquired and the liabilities assumed at the date of acquisition (in US$'000):

Cash	$ 11,285
Other current assets	13,899
Property and equipment	10,717
Total assets acquired	35,901
Total liabilities assumed	(56,963)
Net liabilities assumed	$ (21,062)

NOTE 15 – BUSINESS COMBINATION (Cont'd)

The following table summarizes the allocation of the purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed (in US$'000):

Net liabilities assumed	$ (21,062)
Goodwill	91,976
Acquired in-process technologies	26,080
Other intangible assets consisting of:	
Existing technology	7,580
Patent/core technology	6,910
Non-competition agreement	620
Trade name/trademarks	4,160
Total purchase price excluding deferred share compensation	$ 116,264
Total deferred share compensation	7,053
Total purchase price including deferred share compensation	$ 123,317

The intangible assets are being amortized over their respective benefit periods, which range from one to six years. In accordance with SFAS 142, "Goodwill and Other Intangible Assets," Creative will not amortize the goodwill, but will evaluate it at least annually for impairment.

In accordance with the prevailing accounting standards, the amount of $26.1 million allocated to acquired in-process technology was written off as other charges in fiscal 2002. It is reasonably possible that the development of this technology could fail because of either prohibitive cost, inability to perform the required efforts to complete the technology or other factors outside of Creative's control such as a change in the market for the resulting developed products. In addition, at such time that the project is completed it is reasonably possible that the completed products do not receive market acceptance or that Creative is unable to produce and market the product cost effectively.

The following unaudited pro forma information has been prepared assuming that the above acquisitions had taken place at the beginning of the earliest periods presented. The amount of the aggregate purchase price allocated to in-process technology has been excluded from the pro forma information as it is a non-recurring item. The pro forma financial information is not necessarily indicative of the combined results that would have occurred had the acquisitions taken place at the beginning of the earliest period, nor is it necessarily indicative of results that may occur in the future.

In US$'000	Unaudited Pro Forma for the years ended June 30	
	2002	2001
Sales, net	$ 859,096	$ 1,317,147
Net loss	(31,778)	(160,611)
Basic loss per share	(0.43)	(2.03)
Diluted loss per share	(0.43)	(2.03)

NOTE 16—LONG TERM OBLIGATIONS

In December 1999, prior to its acquisition by Creative, 3Dlabs issued a subordinated convertible note to an investor in the principal amount of $7.5 million which matures in December 2004. The outstanding unpaid principal balance under the note bears interest at a rate of 4.5% per annum, payable upon conversion, prepayment or at maturity. The holder of the note has the option to convert all or a portion of the outstanding unpaid principal balance under the note plus interest into shares of 3Dlabs' common stock at a conversion price of $5.563 per share or to transfer the note to a third party. At any time after June 2002, 3Dlabs has the option to require the noteholder to convert all or a portion of the outstanding unpaid principal balance under the note plus interest, so long as the weighted average closing share price of 3Dlabs' common stock is equal to or greater than the conversion price of $5.563 for twenty trading days prior to the conversion date. In August 2002, after the closing of the acquisition of 3Dlabs by Creative, 3Dlabs, the noteholder and Creative entered into an amendment of the convertible subordinated note agreement and convertible subordinated note to allow the outstanding unpaid principal balance under the note plus interest to be convertible into ordinary shares of Creative, at the conversion price equal to $18.05. To-date, no conversion has been made. 3Dlabs may prepay the outstanding unpaid principal balance plus interest due upon thirty days' prior written notice to the noteholder.

NOTE 17—SUBSEQUENT EVENT

Subsequent to the financial year end, a Creative subsidiary, CTC declared dividend of approximately $4 million to its shareholders, namely BFPL and Creative. BFPL and Creative each received net dividend of $2 million.

In accordance with the joint venture agreement with BFPL as approved by Creative's shareholders, Creative acquired from BFPL the remaining 50% interest that it does not currently own in its building located in the International Business Park in Singapore. The consideration paid by Creative for the 50% interest in CTC amounted to approximately $4 million. Additionally, the Company will also repay the outstanding building-related loans of US$7.1 million to BFPL. The financial consideration for the purchase of Creative Technology Centre Pte Ltd ("CTC") shares was set at CTC's audited net asset value at 4 July 2002, based on the value of the building as determined by an independent property valuer. The acquisition will be accounted for by the purchase method. The payment will be allocated to land and buildings, deferred tax liability and against minority interest.

NOTE 18 – SEGMENT REPORTING

Creative operates primarily in one industry segment and provides advanced multimedia solutions for personal computers. Creative has manufacturing plants in Singapore and Malaysia with the European distribution center located in Dublin, Ireland and the Americas distribution center located in Milpitas, California. Creative focuses its worldwide sales and marketing efforts predominantly through sales offices in North America, Europe and the Asia Pacific region.

The following is a summary of operations by geographical regions (in US$'000):

	Years ended June 30		
	2002	2001	2000
External net sales:			
Asia Pacific	$ 141,966	$ 227,146	$ 274,101
The Americas	390,861	596,295	597,544
Europe	273,078	402,627	470,547
Consolidated	**$ 805,905**	**$ 1,226,068**	**$ 1,342,192**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Years ended June 30		
	2002	2001	2000
Operating income (loss):			
Asia Pacific	$ 11,126	$ 26,913	$ 85,621
The Americas	(5,290)	(18,954)	(45,654)
Europe	22,237	16,620	22,319
Consolidated	**$ 28,073**	**$ 24,579**	**$ 62,286**

	As of June 30	
	2002	2001
Identifiable assets:		
Asia Pacific	$ 468,227	$ 442,000
The Americas	122,651	151,501
Europe	75,500	80,479
Consolidated	**$ 666,378**	**$ 673,980**

Long-lived assets are based on the physical location of the assets at the end of each of the fiscal years. Geographic revenue information for the three years ended June 30, 2002 is based on the location of the selling entity.

	As of June 30	
	2002	2001
Identifiable assets:		
Singapore	$ 233,316	$ 275,103
United States of America	122,651	151,501
Ireland	61,268	77,743
Rest of the world	249,143	169,633
Consolidated	**$ 666,378**	**$ 673,980**

	Years ended June 30		
	2002	2001	2000
Revenue by geographic region:			
Singapore	$ 89,458	$ 149,228	$ 202,917
United States of America	390,861	596,295	597,544
Ireland	272,824	402,627	470,547
Rest of the world	52,762	77,918	71,184
Consolidated	**$ 805,905**	**$ 1,226,068**	**$ 1,342,192**

Major customers: In fiscal 2002, 2001 and 2000, no customer accounted for more than 10% of net revenues. As of June 30, 2002 and 2000, no customer accounted for more than 10% of net accounts receivable and as of June 30, 2001, one customer accounted for 11.7% of net accounts receivable.

STOCK MARKET INFORMATION

Creative's ordinary shares have been traded on the NASDAQ National Market ("NASDAQ") since August 3, 1992, under the symbol "CREAF". Creative's ordinary shares have been traded on the Singapore Exchange ("SGX-ST") since June 15, 1994. The following table presents, for the registered shares on the NASDAQ and SGX-ST:

(i) the annual high and low market prices for the five most recent full fiscal years;

(ii) the high and low market prices for each full fiscal quarter for the two most recent full fiscal years; and

(iii) the high and low market prices for each month for the most recent six months.

These prices do not include retail markups, markdowns, or commissions.

	NASDAQ (Price in US$/Share)		SGX-ST (Price in Singapore $/Share)	
	High	Low	High	Low
Annual High and Low				
Fiscal 1998	29.38	11.00	46.50	17.90
Fiscal 1999	18.56	8.12	30.30	14.10
Fiscal 2000	38.00	9.69	64.00	16.60
Fiscal 2001	23.81	8.10	41.00	14.90
Fiscal 2002	15.05	4.20	27.90	8.15
Quarterly High and Low				
Fiscal 2001				
First Quarter	23.81	19.63	41.00	34.00
Second Quarter	19.88	10.00	35.70	18.20
Third Quarter	13.88	9.03	24.10	16.50
Fourth Quarter	9.90	8.10	18.00	14.90
Fiscal 2002				
First Quarter	9.00	4.20	16.90	8.15
Second Quarter	8.30	4.24	15.10	8.25
Third Quarter	15.05	8.16	27.90	14.80
Fourth Quarter	12.20	8.40	22.90	15.10
Monthly High and Low				
February 2002	15.05	11.72	27.90	21.70
March 2002	13.10	11.54	23.80	21.60
April 2002	12.20	10.50	22.90	19.70
May 2002	11.60	10.51	21.40	19.20
June 2002	10.30	8.40	18.70	15.10
July 2002	10.50	8.70	18.90	15.70

As of August 16, 2002, there were approximately 15,298 shareholders of record of the ordinary shares, of which approximately 301 were registered in the US, and approximately 14,997 in Singapore. Because many of the US shares are held by brokers and other institutions on behalf of shareholders, Creative is unable to estimate the total number of shareholders represented by these US record holders.

On August 16, 2002, the closing price of Creative's ordinary shares on the NASDAQ National Market was $8.92 and on the SGX-ST was S$15.50.

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Tan Lip-Bu,	Director
Tang Chun Choy,	Director
Lee Kheng Nam,	Director

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Creative's Family of

LifeStyle

Digital Entertainment Gadgets.

Sound Blaster Audigy 2

Sound Blaster Extigy

NOMAD Jukebox Zen

Creative Prodikeys

Creative CardCam

Creative Inspire 6.1 6600

Creative NOMAD MuVo

Creative PC-CAM 750

Creative TravelSound MP3

Network Blaster Wireless Access Point Router

NOMAD Jukebox 2

Creative CardCam Value

Creative Inspire 5.1 Digital 5500

NOMAD DXT 200 MP3 English Learning Device

Creative PC-CAM 350

Creative Inspire 2.0 1300

Creative Slix Barebone

Broadband Blaster BritePort Router 8100C

MegaWorks 2.1 250D

NOMAD Jukebox 3

Creative WebCam Mobile

CD-MP3 Slim 600

Creative WebCam

CDRW Blaster 1394 External

Creative WebCam Pro

Network Blaster Wireless Access Point

Storage Blaster

NOMAD II MG

Creative NOMAD MuVo

Awards & Accolades

Editor's Choice
CNET (USA)
Jul, 2002

Editor's Choice
ZDNET (USA)
Jul, 2002

Top Music Gadget
Newsweek Online
Aug 6, 2002

Gadget of The Month
PC Magazine
Sep 17, 2002

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