GRAND TOYS INTERNATIONAL INC
Form 10-Q
May 15, 2002

FORM 10-Q

Securities and Exchange Commission

Washington, D.C. 20549

(Mark One)

[**X**] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: **March 31, 2002**

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the transition period from _______________ to _______________.

Commission File No. 0-22372.

GRAND TOYS INTERNATIONAL, INC.

(Exact Name of Registrant as Specified in its Charter)

Nevada

98-0163743

(State or other jurisdiction of (I.R.S. Employer

incorporation or organization Identification No.)

1710 Route Transcanadienne, Dorval, Quebec, Canada, H9P 1H7

(Address of principal executive offices)

(514) 685-2180

(Registrant's telephone number, including Area Code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes **X** No _____

Indicate the number of shares outstanding of each of the Issuer's classes of common equity, as of May 14, 2002: 1,527,413.

GRAND TOYS INTERNATIONAL, INC.

Index to Quarterly Report on Form 10 - Q

Filed with the Securities and Exchange Commission

Period ended March 31, 2002

GRAND TOYS INTERNATIONAL, INC.

Part I. - Financial Information

Item 1. Financial Statements

Consolidated Balance Sheets

	March 31, 2002	December 31, 2001
	(Unaudited)	

Assets		
Current assets:		
Short-term deposit (note 12(c))	$ 250,000	$ 250,000
Accounts receivable (net of allowance for		
doubtful accounts of $20,526; 2001 - $12,556)	1,502,495	1,386,333
Current portion of loan receivable (note 2)	198,903	194,494
Due from employees and affiliated company	1,850	2,034
Income taxes recoverable	-	143,668
Inventory	1,929,629	1,838,770
Prepaid expenses	766,113	781,867
Total current assets	4,648,990	4,597,166
Loan receivable, (note 2)	497,311	548,721
Other assets (note 3)	64,950	236,436
Equipment and leasehold improvements, net (note 4)	350,174	360,275
Total assets	$ 5,561,425	$ 5,742,598

GRAND TOYS INTERNATIONAL, INC.

Consolidated Balance Sheets

	March 31, 2002	December 31, 2001
	(Unaudited)	
Liabilities and Stockholders' Equity		
Current liabilities:		
Bank indebtedness (note 5)	$ 955,985	$ 602,577
Trade accounts payable	1,840,833	1,974,030
Other accounts payable and accrued liabilities	313,677	307,974
Shortfall on share conversions (note 6)	-	581,310
Income taxes payable	5,667	-
Royalties payable	55,344	20,104
Total current liabilities	3,171,506	3,485,995
Minority interest	100	100
Stockholders' equity:		
Capital stock (note 7):		
Voting common stock, $0.001 par value:		

12,500,000 shares authorized,		
1,527,332 shares issued and outstanding		
(2001 - 1,285,119 shares)	1,527	1,285
Series B preferred stock, $0.001 par value:		
915,000 shares authorized,		
915,000 shares issued and outstanding		
(2001 - 915,000)	915	800
	2,442	2,085
Additional paid-in capital	22,200,961	21,496,788
Deficit	(18,824,372)	(18,253,908)
Accumulated other comprehensive income-		
cumulative currency translation adjustment	(989,212)	(988,462)
	2,389,819	2,256,503
Commitments and contingencies (notes 11 and 12)		
Total liabilities and stockholders' equity	$ 5,561,425	$ 5,742,598

See accompanying notes to consolidated financial statements.

grand toys international, inc.

Consolidated Statements of Operations, (Unaudited)

For the three months ended March 31,

2002

2001

Net sales		$2,561,685	$2,216,816
Cost of goods sold		1,579,830	1,514,601
Gross profit		981,855	702,215
Operating expenses:			
Selling, general and administrative		1,473,467	1,210,713
Bad debt expense		16,745	17,791
Depreciation and amortization		23,313	31,833
Foreign exchange loss		14,984	29,345
Interest expense		24,818	-
Interest revenue		(17,158)	(32,986)
		1,536,169	1,256,696
Loss before income taxes		(554,314)	(554,481)
Income taxes (expense):		(16,150)	(30,636)
Net loss		$(570,464)	$(585,117)
Earnings per share (note 9):			
Basic		(0.42)	(0.72)
Diluted		(0.42)	(0.72)

See accompanying notes to consolidated financial statements.

GRAND TOYS INTERNATIONAL, INC.

Consolidated Statements of Stockholders' Equity and Comprehensive Income (Unaudited)

	Capital Stock	Additional Paid in Capital	Deficit	Accumulated other comprehensive income	Total
January 1, 2002	$ J,085	$ 21,496,788	$(18,253,908)	$ (988,462)	$ 2,256,503
Net loss for the period			(570,464)		(570,464)
Foreign currency adjustment				(750)	(750)
Total comprehensive income					(571,214)
Share issuance in settlement of shortfall on share					
Conversions (note 6)	242	581,068			581,310

Private sale of preferred stock (note 7 (c))	115	114,885			115,000
Compensation expense		8,220			8,220
March 31, 2002	$ 2,442	$ 22,200,961	$ (18,824,372)	$ (989,212)	$ 2,389,819

See accompanying notes to consolidated financial statements.

GRAND TOYS INTERNATIONAL, INC.

Consolidated Statements of Cash Flows, (Unaudited)

For the three months ended March 31,

		2002	2001
Cash flows from operating activities:			
Net loss		(570,464)	(585,117)
Adjustments for:			
Depreciation and amortization		23,313	31,833
Compensation expense		(6,183)	
Net change in operating working capital			
items (note 10)		(120,845)	203,988
Net cash used for operating activities		(674,179)	(349,296)
Cash flows from financing activities:			

Increase in bank indebtedness		353,871	-
Share issuance proceeds (note 7 (c))		115,000	331,000
Other		306	(18,018)
Net cash provided by financing activities		469,177	312,982
Cash flows from investing activities:			
Loan receivable		47,001	-
Increase in other assets		171,481	-
Additions to equipment and leasehold improvements		(13,480)	(5,508)
Net cash used for (provided by) investing activities		205,002	(5,508)
Net decrease in cash		-	(41,822)
Cash, beginning of period		-	211,515
Cash, end of period		$ -	$ 169,693
Supplemental disclosure of cash flow information:			
Cash paid during the period for:			
Interest		$ J4,818	$ -
Income taxes		16,150	18,582
Private placement proceeds included in accounts receivable		-	169,000

Non-cash transactions:			
Share conversions		-	250,000
Shortfall on share conversions		-	232,810
Reduction in shortfall on share conversions through the issuance of common stock (note 7(c))		581,310	-

See accompanying notes to consolidated financial statements

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

Grand Toys International, Inc., a Nasdaq SmallCap listed Company, is organized under the laws of the State of Nevada. Its principal business activity, through its wholly-owned Canadian and US operating subsidiaries, is the distribution of toys and related items.

1. Significant accounting policies:

a. Basis of presentation:

The accompanying financial statements have been prepared on a going concern basis which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business and do not reflect adjustments that might result if the Company cannot continue as a going concern. The Company incurred a significant operating loss in fiscal 2000 primarily as a result of the loss of one of its major product lines and the reduced market demand for certain other products. The Company again incurred an operating loss for the year ended December 31, 2001 and for the three months ended March 31, 2002.

In 2001, the Company secured a line of credit to finance its inventory and accounts receivable and also realized net proceeds from the sale of capital stock and warrants. This financing however is not sufficient and the Company will require additional financing before the end of the 2002 fiscal year.

The above matters raise substantial doubt about the Company's ability to continue as a going concern. The Company's ability to continue as a going concern will depend on its obtaining additional financing and its return to profitable operations.

b. Principles of consolidation:

These consolidated financial statements, presented in US dollars and in accordance with accounting principles generally accepted in the United States, include the accounts of the Company and its subsidiaries. All significant intercompany balances and transactions have been eliminated.

c. Revenue recognition:

Sales are recognized at the time of shipment of products. The Company estimates liabilities and records provisions for customer allowances as a reduction of revenue, when such revenue is recognized.

d. Inventory:

Inventory is valued at the lower of cost, determined by the first in, first out method, and net realizable value. The only significant class of inventory is finished goods.

e. Prepaid expenses:

Prepaid expenses primarily include insurance, advances on inventory purchases and current portion of royalties and product development costs.

f. Other assets:

Prepaid royalties are capitalized and written off over the term of the related agreements.

Product development costs for proprietary product lines are capitalized and written off over a period of twenty four months.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

1. Significant accounting policies (continued

):

g. Equipment and leasehold improvements:

Equipment and leasehold improvements are stated at cost less accumulated depreciation. Depreciation methods and annual rates adopted by the Company are as follows:

Asset	Method	Rate
Computer equipment	Declining balance	30%
Machinery and equipment	Declining balance	20%
Furniture and fixtures	Declining balance	20%
Trucks and automobiles	Declining balance	30%
Telephone equipment	Declining balance	30%
Leasehold improvements	Straight-line	Term of
		lease plus one
		renewal term

a. Impairment of long-lived assets and long-lived assets to be disposed of:

Management reviews long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows, undiscounted and without interest charges, expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

b. Foreign currency translation:

8. Grand Toys Ltd. and Grand Concepts Inc., which ceased operations on January 29, 2002, wholly-owned Canadian subsidiaries, use the Canadian dollar as their functional currency and translate their assets and liabilities into US dollars at the exchange rates prevailing at the balance sheet date and sales, expenses and cash flows are translated at the average exchange rate for the year. The resulting currency translation adjustments are accumulated and reported in other comprehensive income.

ii. Other monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates prevailing at the balance sheet date. Revenues and expenses denominated in foreign currencies are translated at the rates of exchange prevailing at the transaction dates. All exchange gains and losses are included in income.

j. Earnings per share:

i. On September 4, 2001, the Company completed a one-for-four reverse stock split. For purposes of earnings per share calculations and all share amounts, the comparative numbers of shares have been restated to reflect the reverse split.

ii. Basic earnings per share are determined by dividing the weighted average number of common shares outstanding during the period into net earnings (loss).

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

1. Significant accounting policies (continued

):

j. Earning per share, continued:

iii. Diluted earnings per share give effect to all potentially dilutive common shares that existed at March 31, 2002.

k. Advertising and promotion:

All costs associated with advertising and promoting products are expensed in the period incurred. Total expense for the period ended March 31, 2002 and 2001 amounted to approximately $210,990 and $103,422.

l. Employee stock option plan:

The Company accounts for its employee stock option plan in accordance with the provisions of Accounting Principles Board ("APB") Opinion No. 25, Accounting for Stock Issued to Employees. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. Financial Accounting Standards Board ("FASB") Statement No. 123, Accounting for Stock-Based Compensation, allows entities to continue to apply the provisions of APB Opinion No. 25 and requires pro-forma net earnings and pro-forma earnings per share disclosures for employee stock option grants as if the fair-value-based method defined in FASB Statement No. 123 had been applied. This disclosure is included in the notes to these statements.

m. Comprehensive income:

Comprehensive income consists of net income and cumulative currency translation adjustments and is presented in the consolidated statements of stockholders' equity and comprehensive income. The statement requires only additional disclosures in the consolidated financial statements; it does not affect the Company's financial position or results of operations.

n. Use of estimates:

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

2. Loan receivable:

The loan receivable is due from Limited Treasures Inc. ("Limited Treasures"), a company which was an acquisition target in 1999. The loan is secured by accounts receivable and inventory and personal guarantees of the shareholders of Limited Treasures. In 2000, the Company recorded a 50% provision or $434,371 against the loan because of difficulty in recovering the amount due.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

2. Loan receivable (continued):

In June 2001, the Company was successful in obtaining judgment against Limited Treasures for $775,000 repayable over 42 months commencing June 30, 2001, and accordingly the provision was reduced to $146,269. Interest is charged at a rate of 9%.

Details are as follows:

Amount due repayable in monthly payments of principal and	
interest of $21,124 per month	$ 696,214
Less current portion	198,903
	$ 497,311

- **Other assets:**

Prepaid royalties	360,894
Product development costs	165,233
	526,127
Less current portion, included in prepaid expenses	461,177
	$ 64,950

- Equipment and leasehold improvements:

	March 31, 2002		December 31, 2001	
	Cost	Accumulated depreciation	Cost	Accumulated depreciation
Computer equipment	$1,218,671	$1,001,688	$1,213,935	$985,304
Machinery and equipment	445,455	408,476	445,821	406,881
Furniture and fixtures	484,204	436,590	482,598	434,492
Trucks and automobiles	76,654	75,965	76,722	75,977

Telephone equipment	48,149	37,982	42,486	37,499
Leasehold improvements	321,198	283,456	321,479	282,613
	$2,594,331	$J,244,157	$2,583,041	$2,222,766
Net book value		$350,174		$360,275

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GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

5. Bank indebtedness:

   In 2001, the Company secured a line of credit to finance its inventory and accounts receivable providing for advances of up to $1,500,000 (Cdn$2,425,000). An additional amount of $47,000 (Cdn$75,000) was advanced to the Company based on the value of certain of its equipment. The receivable loan has a discount fee of 2% and both the inventory loan and the equipment loan bear interest at Canadian prime plus 7.5%. The latter is being repaid through monthly capital repayments of $1,100 (Cdn$1,875). The agreement is for a period of one year and is renewed automatically, unless prior notice is given by either party.

   The loan is secured by a first ranking movable hypothec in the principal amount of $2,500,000 (Cdn$4,000,000) on the universality of all present and future assets of the Company and the assignment of insurance.

   The Company has approximately $459,000 of credit available as at March 31, 2002.

6. Shortfall on share conversions:

   In connection with the acquisition of the assets of Ark Foundation LLC, on January 1999, the Company created and issued a class of 200,000 shares of non-voting Series A Convertible Redeemable Preferred Shares ("Series A shares") with a stated value of $5.00 per share. The Series A shares rank senior to the common stock. The Series A shares have a cumulative preferred quarterly dividend of 5% per annum of the par value, payable in cash, contingent upon company declaration. The Series A shares were redeemable and convertible at determinable prices on determinable dates. The Series A shares were convertible into shares of the Company's common stock on a one-for-one basis. If upon conversion, the market value of the common stock of the Company was less than $5.00 per share, the Company was obligated to make up the difference between the market price on the conversion date and $5.00 in cash.

All of the shares were converted into common stock between January 2000 and August 2001. Because the market price of the common stock was below $5.00 per share on certain of the conversion dates, the Company recorded shortfalls of $118,000 in 2000 and $463,310 in 2001.

On February 26, 2002, the Company entered into a settlement agreement with the seller of the assets of Ark Foundation LLC and certain other parties, which settled all outstanding matters resulting from the purchase of the assets. Pursuant to the settlement agreement, the Company issued 242,213 shares of its common stock in settlement of the outstanding shortfalls noted above. The Company agreed to remove the legend on the shares which had previously been pledged to secure Ark Creations' $1,500,000 note payable and granted the seller an option to purchase the remaining assets of Art Creations

7. Capital stock

The number of common shares has been adjusted for transactions that occurred prior to September 4, 2001, to give effect to the one-for-four reverse stock split, which reduced the number of outstanding common shares to 1,284,619 at that date and the number of authorized shares from 50,000,000 to 12,500,000.

a. Authorized capital also includes 5,000,000, $0.001 par value preferred shares, issuable in series with such designation, rights and preferences as may be determined from time to time by the Board of Directors. There are no shares issued and outstanding at March 31, 2002.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

5. Capital stock, continued:

6. Each Series B Preferred share will automatically be converted, upon approval by the stockholders, into one share of the Company's common stock at an exercise price of $1.00 per share and a warrant to purchase three shares of the Company's common stock at an exercise price of $0.01 per share. In the event the stockholders approve the conversion, a total of 3,660,000 common shares would be issued.

7. Share transactions:

- January 2001:

50,000 Series A preferred shares converted to 12,500 common shares, increasing capital stock by $50.

- February 2001:

In satisfaction of the full payment of the long-term debt of its US subsidiary, Ark Creations, which ceased operations in 2002, 93,750 common shares were issued, increasing capital stock by $375.

- March 2001:

As a result of a private sale of common stock by the Company, 357,143 common shares and 357,143 warrants were issued, increasing capital stock by $1,428.

- August 2001:

50,000 Series A preferred shares converted to 12,500 common shares, increasing capital stock by $50.

- November 2001:

500 options exercised for total proceeds of $683, increasing the number of common shares outstanding by 500 and capital stock by $1.

♦ December 2001:

As a result of a private sale of Series B convertible redeemable preferred stock by the Company, 915,000 convertible preferred shares were issued for a total consideration of $915,000, of which $115,000 is unpaid at year-end. This transaction increased capital stock by $800.

♦ January 2002:

115,000 shares of Series B convertible redeemable preferred stock were issued pursuant to the December 2001 private sale of convertible preferred stock for a total consideration of $115,000, increasing capital stock by $115.

♦ February 2002:

As a result of the settlement of the outstanding shortfall on share conversions, 242,213 common shares were issued, increasing capital stock by $242.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

7. Capital stock (continued):

- Summary of common stock outstanding:

A summary of the number of shares of common stock outstanding and share transactions since January 1, 2001 is as follows:

January 1, 2001	808,726
Share issuance in settlement of long-term debt (note 7(c))	93,750
Share conversions (note 7(c))	25,000
Private sale (note 7(c))	357,143
Stock options (note 7(c))	500
December 31, 2001	1,285,119
Share issuance on settlement of shortfall on share conversion (note 7(c))	242,213
March 31, 2002	1,527,332

- Stock options and warrants:

The Company's amended and restated employee stock option plan (the "Option Plan") provides for the issuance of up to 150,000 options to acquire common stock of the Company. Stock options granted under the Option Plan may be Incentive Stock Options under the requirements of the Internal Revenue Code, or may be Non-statutory Stock Options which do not meet such requirements. Options may be granted under the Option Plan to, in the case of Incentive Stock Options, all employees (including officers) of the Company, or, in the case of Non-statutory Stock Options, all employees (including officers) or non-employee directors of the Company.

Under the option plan, the exercise price of each option granted has been equal to the market price of the Company's stock on the grant date, and an option's maximum term is ten years.

Changes in options and warrants are as follows:

	Option	Other			Weighted-average

	Plan	stock options	Warrants	Total	exercise price per share
January 1, 2002	134,093	236,875	412,143	783,111	$ 3.72
Granted	12,000	-	-	12,000	
Expired	(18,533)	-	-	(18,533)	
March 31, 2002	127,560	236,875	412,143	776,578	$3.74

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

- **Earnings per share:**

	Income (numerator)	Shares (denominator)	Per Share Amount
Quarter ended March 31, 2002			
Basic EPS			
Earnings available to			
common stockholders	$ (570,464)	1,373,930	$(0.42)

Diluted EPS			
Earnings available to			
common stockholders			
and assumed conversions	$ (570,464)	1,373,930	$ (0.42)

	Income (numerator)	Shares (denominator)	Per Share Amount
Quarter ended March 31, 2001			
Basic EPS			
Earnings available to			
common stockholders	$ (585,117)		$ (0.72) 833,131
Diluted EPS			
Earnings available to			
common stockholders			
and assumed conversions	$ (585,117)	833,131	$ (0.72)

Options and warrants to purchase 776,578 shares (2001 - 783,111) of the Company's common stock were not included in the diluted earnings per share calculation as their effect is anti-dilutive.

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Notes to Consolidated Financial Statements

• Changes in operating working capital items:

For the three months ended March 31,

2002 J001

(Increase) decrease in accounts receivable		$ (117,158)	$I57,905
Decrease in due from employees and affiliated company		182	17,137
(Increase) decrease in inventory		(91,769)	286,919
Decrease in income taxes recoverable		146,644	15,632
Decrease in prepaid expenses		29,894	89,997
(Decrease) in trade accounts payable		(132,253)	(414,466)
Increase in other accounts payable and accrued liabilities		5,882	59,699
Increase (decrease) in royalties payable		35,241	(8,835)
Increase in income taxes payable		2,492	-
		$ (120,845)	$ 203,988

• Commitments:

The Company has entered into long-term leases with minimum annual rental payments approximately as follows:

2002	$267,000
2003	349,000

2004	233,000
2005	8,000
2006	8,000
	865,000

Rent expense for the period ended March 31, 2002, and 2001 amounted to approximately $40,980, and $52,582 respectively.

- Contingencies

:

- Lawsuits for alleged breach of contract have been filed against the Canadian subsidiary by two former sales representatives. In the opinion of management, these actions have no merit. At this point in time it is difficult to ascertain or estimate the value of a settlement, if any.

- The Company was named in a lawsuit for breach of contract in a licensing dispute, for recovery totaling in excess of $600,000. A defense was filed against the plaintiff, and management had reserved, at December 31, 2000, $550,000 in the event the results were unfavorable. In March 2001, the Company received a favorable court judgment, and reversed the accrual, in full, by the third quarter of 2001.

- The Company's Canadian subsidiary is also contingently liable for an outstanding letter of credit of $250,000 as at March 31, 2002. the short-term deposit has been pledged as collateral fort this letter of credit.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

7. Segment information:

- Operating and geographic information:

The Company operates primarily in one segment which includes the distribution of toys and related items. Approximately 87% of total sales are to Canadian customers. The majority of long-lived assets are located in Canada.

b. Other information:

Sales of toys purchased from the Company's two largest manufacturers and suppliers of toys in aggregate accounted for 66% of gross sales for the quarter ended March 31, 2002. The Company's two largest suppliers accounted for 57% of gross sales for the quarter ended March 31, 2001.

- Financial instruments:

- Foreign currency risk management:

The Company enters into forward foreign exchange contracts to minimize its foreign currency exposure on purchases. The contracts oblige the Company to buy US dollars in the future at predetermined exchange rates. The contracts are not used for trading purposes. The Company's policy is to enter into forward foreign exchange contracts on a portion of its purchases anticipated in the next selling season. Gains and losses on forward exchange contracts are recorded in income and generally offset transaction gains or losses on the foreign currency cash flows which they are intended to hedge.

At March 31, 2002, the Company had no contracts to purchase US dollars.

a. Fair values:

Fair value estimates are made as of a specific point in time, using available information about the financial instruments. These estimates are subjective in nature and often cannot be determined with precision.

The fair value of the Company's accounts receivable, due from affiliated companies, bank indebtedness, trade and other payables approximate their carrying value due to the immediate or short-term maturity of these financial instruments.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

14. Financial instruments, continued:

• Credit risk and economic dependence:

For the period ended March 31, 2002, approximately 57% (March 2001 - 57%) of the Company's sales were made to two unrelated companies, as detailed below.

	March 2002		March 2001	
	Net Sales	%	Net Sales	%
Customer A	1,153,000	45	998,000	45
B	307,000	12	266,000	12

The Company regularly monitors its credit risk exposure to these and other customers and takes steps to mitigate the risk of loss.

d. Interest rate risk:

The company's principal exposure to interest rate risk is with respect to its short-term financing which bears interest at a floating rate.

15. Comparative Figures:

Certain of the 2001 comparative figures have been reclassified to conform with the basis of presentation adopted in the current year.

GRAND TOYS INTERNATIONAL, INC.

Notes to Consolidated Financial Statements

Item 2. Management's Discussion and Analysis:

The following should be read in conjunction with the consolidated financial statements included in this 10-Q and the December 31, 2001 Annual Report.

Overview

Forward-looking statements

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This Form 10-Q contains forward-looking statements about events and circumstances that have not yet occurred. For example, statements including terms such as the Company "expects" or "anticipates" are forward-looking statements. Investors should be aware that the Company's actual results may differ materially from the Company's expressed expectations because of risks and uncertainties about the future. The Company will not necessarily update the information in this Form 10-Q if and when any forward-looking statement later turns out to be inaccurate. Risks and uncertainties that may affect the Company's future results and performance include, but are not limited to, the following: intense competition and pricing pressures in the toy industry; the general consolidation in the toy industry; whether the Company's general strategy with respect to the toy industry and the Company's implementation of that strategy will correctly anticipate key trends in the toy industry; the Company's ability to retain its product lines; the Company's relationships with retailers and other issues with respect to the Company's distribution channels. Additional information about factors that could affect future results and events is included elsewhere in this Form 10-Q, in the Company's fiscal 2001 Form 10-K and in other reports filed with the Securities and Exchange Commission.

In our audited financial statements for the years ended December 31, 2001 and 2000 we recognized that we had certain issues which raised substantial doubt about the Company's ability to continue as a going concern. The reasons cited were our recurring losses and the cancellation of our line of credit in 2000. This was noted in KPMG's audit report on those financial statements. In 2001, we implemented a plan to stem our losses and return to profitability and secured lines of credit. However, these lines of credit are not sufficient to meet all of our financial needs and we might not be able to successfully implement our new operational plan. If doubts about our ability to continue as a going concern persist, it may have an adverse impact on investors' willingness to invest in our stock which would negatively impact the price and liquidity of our shares.

We incurred net losses of $1,371,492 for the year ended December 31, 2001, $10,156,713 for the year ended December 31, 2000. We have not reported an annual profit since December 31, 1997. We have recently begun to implement a plan to return to profitability. Over the course of 2001 we have focused on products with higher profit margins and have reduced expenses. This has resulted in improved performance but we have not achieved profitability for the year ending December 31, 2001 and, in spite of these efforts, there can be no assurance that we will become profitable on an annual basis.

Net sales consist of sales of products to customers after deduction of customer cash discounts, freight and warehouse allowances, and volume rebate allowances. Sales are recorded when the merchandise is shipped.

The cost of goods sold for products imported as finished goods includes the cost of the product in the appropriate domestic currency, duty and other taxes, and freight and brokerage charges. Royalties to Grand Canada suppliers not contingent upon the subsequent sales of the suppliers' products are included in the price paid for such products.

Major components of selling, general and administrative expenses include: payroll and fringe benefits; advertising expense, which includes the cost of production of television commercials and the cost of air time; advertising allowances paid to customers for cooperative advertising programs; and royalty expense. Royalties include payments by Grand Canada to licensors of character properties and to manufacturers of toy products if such payments are contingent upon subsequent sales of the products. Royalties are usually a percentage of the price at which the product is sold and are payable once a sale is made.

GRAND TOYS INTERNATIONAL, INC

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Accounts receivable are receivables net of an allowance for doubtful accounts. The allowance is adjusted periodically to reflect the current status of receivables. Management believes that current reserves for doubtful accounts are adequate. Sales of products to retailers and distributors are on an irrevocable basis. Consistent with industry practices, Grand Canada may make exceptions to this policy on a case-by-case negotiated basis. Inventory is comprised of finished goods at landed cost.

All amounts are in US Dollars ($) unless otherwise noted.

Results of Operations

The following table sets forth consolidated operations data as a percentage of net sales for the periods indicated:

For the Three Months

Ended March 31,

	2002	2001
	%	%

Net sales	100.00	100.00
Cost of goods sold	61.67	68.32
Gross profit	38.33	31.68
Operating expenses:		
Selling, general and administrative	57.52	54.61
Foreign exchange loss	0.58	1.33
Interest revenue	(0.67)	(1.49)
Interest expense	0.97	-
Bad debt expense	0.65	.80
Depreciation and amortization	0.91	1.44
Total operating expenses	59.96	56.69
Loss before income taxes	(21.63)	(25.01)
Net loss	(22.27)	(26.39)

On a quarterly basis management reviews its inventory of products and makes an assessment of its realizable value. The factors considered include current market prices, the demand for and the seasonality of its products. If circumstances change (i.e. unexpected shift in market demand, pricing, trends etc.) there could be a material impact on the net realizable value of inventory.

Comparison of the three months ended March 31, 2002 to the three month ended March 31, 2001

Net Loss:

Net loss for the first quarter 2002 was $570,464 or $0.42 per share as compared to a net loss of $585,117 or $0.72 per share for the first quarter of 2001.

Despite the increases in net sales and gross profit, net loss improved marginally by 4.12% as a percentage of sales over the same quarter of last year. An increase in total operating expenses offset the increased gross profit.

Net Sales:

Net sales increased for the first three months of 2002 by $344,869 or by 15.56% to $2,561,685 from $2,216,816 for the first quarter of 2001. During the quarter, gross profit also increased as a result of the Company's emphasis on profitable sales and tighter inventory control.

Net Sales, continued:

The increase in the current quarter is due to the Spider-Man, Lord of the Rings, Disney/Universal product lines and Uno product lines.

Spider-Man the evergreen, perennially popular line of action adventure figures from the classis comic book hero has been dramatically enhanced by the release of Spider-Man the movie and additional lines of product based on the movie characters.

Similarly, Lord of the Rings action figure toys based on the characters for the wildly successful movie adaptation of J.R. Tolkien's classic novel line captured the imagination of children.

The line of records and audiotapes is a new distribution opportunity acquired early in January 2002.

Uno specialty game product line, produced by our Sababa subsidiary, is a new introduction generated from the recently acquired Mattel license for these products.

Gross Profit:

Gross profit for the Company increased during the first three months of 2002 by $279,640 compared to the prior period. As a percentage of sales, gross profit increased from 31.68% in the first quarter of 2001 to 38.33% in the first quarter of 2002. Gross profit increased as a result of the sales and product mix in the first quarter 2002. In addition the increased gross profit in the first quarter of 2002 resulted from the Company's continued emphasis on higher margin sales and minimized sales of discontinued products by tighter inventory control.

Selling, General and Administrative Expenses:

The increase in selling, general and administrative expenses of $262,754 to $1,473,467, in the first quarter of 2002, from $1,210,713 in the first quarter, of 2001, was due to an increase in advertising and co-operative advertising, royalty and insurance expenses.

Other material expenses in the quarter were:

Bank financing	$71,103
Legal expenses	52,173
Recruiting	33,000
Consulting	11,051
	$167,327

Of the above expenses, $81,051 are of a non-recurring nature.

Selling, general and administrative expenses as a percentage of sales, were higher in 2002, a 2.91% increase, as compared to 2001. The Company continues to conduct reviews of all aspects of its operations to reduce costs and improve profitability.

Interest Expense:

During the quarter the Company incurred interest on the following:

Legal settlement	$ 15,317
Financing interest	9,501
	$ 24,818

The legal settlement interest is of a non-recurring nature.

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Comparison of the three months ended March 31, 2001 to the three months ended March 31, 2000:

Net Loss:

Net loss was $585,117 for the first quarter of 2001 compared to a net loss of $823,094 for the first quarter of 2000. The decrease in loss was primarily due to the increase in gross profit and a reduction in selling, general and administrative, depreciation and interest expenses.

Net Sales:

Net sales decreased by $1,275,051 or by 36% over net sales of the first quarter of 2000. The lower net sales volume in 2001 was attributed to the loss in 2000, of the Tiger Electronics product line, which was purchased by Hasbro in 1999. In 2000, the product mix consisted primarily of electronics, which were at a higher sales dollar value.

Gross Profit:

Gross profit for the Company increased by $223,668, and as a percentage of sales, gross profit increased from 13.70% to 31.68%. Despite the decrease in net sales, gross profit increased as a result of the sales mix in the product line.

The increased gross profit in 2001 results from the Company's emphasis on higher margin sales. In addition commissions on FOB sales increased as compared to the same quarter of 2000. In 2000, the lower gross profit percentage was associated with the clearance of the Tiger Electronics product line.

Selling, General and Administrative Expenses:

The decrease in selling, general and administrative expenses of $377,886 compared to those of the first quarter of 2000 was mainly due to decreases in advertising and salary expenses and aggregate decreases in other expenses, as a result of the cost cutting measures implemented. The Company is currently conducting an intensive review of all aspects of its operations to reduce costs and improve profitability.

Depreciation and Amortization:

As a result of the complete write off of deferred financing and intangibles in 2000, depreciation and amortization expense decreased significantly in the first quarter of 2001.

Liquidity and Capital Resources

The Company generally finances its operations through borrowings from Montcap Financial Inc., by cash flow from operations, and sales of equity securities. The inflow of funds in 1999, due to options and warrants being exercised resulted in virtually all short-term bank debt being eliminated by December 31, 1999 and a cash position maintained through June 30, 2001, as a result of a private sale of common stock and the receipt of income taxes recoverable.

In March 2001, the Company received gross proceeds of $500,000 from a private sale of its Common Stock and warrants.

In June 2001, the Company secured a line of credit up to $627,825 with drawdowns based upon specified percentages of its accounts receivable. The line of credit was secured by the accounts receivable of the Company.

In October 2001, the Company increased its credit facility up to $1,569,563 with drawdowns based upon specified percentages of accounts receivable and inventory and the value of its equipment. All the assets of the Company secure the line of credit.

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In December 2001, the Company issued Series B Convertible Redeemable Preferred Stock for a total of $915,000 of which $800,000 was received in December 2001, and the balance in January 2002.

During 2001, we secured a new line of credit to finance our inventory and accounts receivable and we also realized net proceeds from the sale of our common stock and warrants. This source of financing, however, will not be sufficient to fully implement our business plan. To the extent that we will be required to fund operating losses, our financial position will deteriorate. There can be no assurance that we will be able to find significant additional financing at all or on terms favorable to us. If equity securities are issued in connection with a financing, dilution to our stockholders may result, and if additional funds are raised through the incurrence of debt, we may be subject to restrictions on our operations and finances. Furthermore, if we do incur additional debt, we may be limiting our ability to repurchase capital stock, engage in mergers, consolidations, acquisitions and asset sales, or alter our lines of business or accounting methods, even though these actions would otherwise benefit our business

Accounts receivable at March 31, 2002 were $1,502,495 compared to $1,386,333 at December 31, 2001. The sales were mainly to mass retailers. Inventory at March 31, 2002 increased to $1,929,679 from $1,838,770 at December 31, 2001.

Working capital increased from $1,111,171 at December 31, 2001 to $1,477,484 at March 31, 2002. Net cash used for operating activities was $674,179 in 2002 compared to net cash used by operating activities of $349,296 in 2001. Cash for additions to equipment and leasehold improvements was $13,480 in 2002 compared to $5,508 for 2001.

The Company's accounts receivable level is subject to significant seasonal variations due to the seasonality of sales. As a result, the Company's working capital requirements are greatest during its third and fourth quarters. In addition, to the extent accounts receivable, inventories, guarantees and advance payments increase as a result of growth of the Company's business, the Company could require additional working capital to fund its operations.

Sources of such funding include cash flow from operations, drawings on the financing facilities, or sales of additional equity or debt securities by the Company.

If the funds available to the Company for current cash and cash equivalents are not sufficient to meet the Company's cash needs, the Company may from time to time seek to raise capital from additional sources, including project-specific financing, additional public or private debt or equity financing.

We believe that in order to achieve our long-term expansion objectives and to enhance our competitive position in the U.S. market, we will need additional financial resources over the next several years. The precise amount and timing of our future financing needs cannot be determined at this time and will depend upon a number of factors, including the demand for our products and the management of our working capital. We may not be able to obtain additional financing on acceptable terms or at all. If we are unable to obtain sufficient capital, we could be required to curtail our expansion.

Certain Business Relationships and Related Transactions

In March 2001, David Mars and Stephen Altro, directors of the Company, purchased Common Stock in the private sale of the

Company's stock. David Mars invested $131,000 and received 93,571 shares at $0.35 each and 93,571 warrants to purchase Common Stock at an exercise price of $0.53 each. Stephen Altro invested $106,000 and received 75,714 shares at $0.35 each and 75,714 warrants to purchase Common Stock at an exercise price of $0.53 each.

In December 2001, David Mars and Stephen Altro, directors of the Company, purchased shares of Series B Convertible Redeemable Preferred Stock. David Mars invested $195,000 and received 195,000 shares at $1.00 each and 585,000 warrants to purchase Common Stock at an exercise price of $0.01 each. In March 2002, Mr. Mars invested an additional $200,000 and received 200,000 shares at $1.00 each and 600,000 warrants to purchase Common Stock at an exercise price of $0.01 each. Stephen Altro invested $200,000 and received 200,000 shares at $1.00 each and 600,000 warrants to purchase Common Stock at an exercise price of $0.01 each. The conversion of these shares is subject to shareholder approval.

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Effects Of Inflation

The Company does not believe that inflation has had a significant impact on its financial position or results of operations in the past three years

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New Accounting Pronouncements

The Company has determined that the new pronouncements that will come into effect in the year 2002 will not have an impact on the financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company is exposed to certain market risks, which arise from transactions entered into the normal course of business. The Company's primary exposures are changes in interest rates with respect to its debt and foreign currency exchange fluctuations.

INTEREST RATE RISK The interest payable on the Company's revolving lines-of-credit are variable based on the prime rate, and therefore, affected by changes in market interest rates. The Company does not use derivative financial instruments.

FOREIGN CURRENCY RISK While the Company's product purchases are transacted in United States dollars; most transactions among the suppliers and subcontractors are effected in HK dollars. Accordingly, fluctuations in Hong Kong monetary rates may have an impact on the Company's cost of goods. Furthermore, appreciation of Chinese currency values relative to the Hong Kong dollar could increase the cost to the Company of the products manufactured in the People's Republic of China, and thereby have a negative impact on the Company. As well since the majority of the Company's sales are in Canadian dollars, the Company is at risk with regards to the conversion of Canadian dollars to US dollars to pay its suppliers. Therefore, fluctuations in the conversion rate may have an impact on the Company. The Company may use derivative financial instruments solely to hedge the effects of such currency fluctuations.

Part II: Other Information

Item 1. Legal proceedings

During the quarter ended March 31, 2002, there were no other material developments to any legal proceedings which have been previously reported by the Company.

Other than discussed above or in Note 16 to the Company's December 31, 2001 Consolidated Financial Statements, the Company is not a party to, nor is it aware of, any other pending litigation of a material nature.

Item 2. Changes in Securities and Use of Proceeds

On February 26, 2002, the Company issued 242,213 shares of Common Stock in the settlement of a liability. Refer to note 7 of the Financial Statements included herein, for additional information.

Item 3. Defaults Upon Senior Securities

None

GRAND TOYS INTERNATIONAL, INC.

Item 4. Submission of Matters to a Vote of Security Holders

Submission of Matters to a Vote of Security Holders:

On March 14, 2002, the Company held its 2001 annual meeting of stockholders. At the meeting, the following actions took place:

1. The stockholders re-elected Stephen Altro, David Mars, Elliot Bier and James Rybakoff as directors of the Company. The number of votes for and against each of them was as follows:

Director Name	For	Against	Withheld	Abstain
Elliot Bier	741,194	52	n/a	2,710
James Rybakoff	741,194	52	n/a	2,710
Stephen Altro	741,194	102	n/a	2,710
David Mars	741,144	852	n/a	2,710

- The Stockholders ratified the approval of KPMG LLP to serve as the Company auditors for the fiscal year ending December 31, 2001. 740,570 shares were voted for the appointment, 2,326 shares were voted against the appointment, no shares were withheld and 1,060 shares abstained.

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

No exhibits or reports on Form 8-K were filed during the quarter ended March 31, 2002.

GRAND TOYS INTERNATIONAL, INC.

Signatures

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

Dated: May 15, 2002 **GRAND TOYS INTERNATIONAL, INC.**

By: /s/ R. Ian Bradley

R. Ian Bradley

President and CEO

By: /s/ Tania M. Clarke

Tania M. Clarke

Executive Vice President and CFO

(Principal Financial and Accounting Officer)

GRAND TOYS INTERNATIONAL, INC.

Signatures

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

Dated: May 15, 2002 **GRAND TOYS INTERNATIONAL, INC.**

By: ______ R. Ian Bradley

President and CEO

By: ______

Tania M. Clarke

Executive Vice President and CFO

(Principal Financial and Accounting Officer)