



To Our Employees, Clients and Fellow Shareholders:

2008 was a challenging yet ultimately rewarding year for EMAK.

We have made significant progress toward our overall corporate priorities, which I published in last year's letter. These include: containing costs and achieving profitability across business units and geographies, driving new business development and organic growth, investing in our people and the highest growth segments of the industry, exceeding our clients' needs and expectations, and being recognized in the industry as consumer engagement experts.

EMAK's 2008 financial results reflect the growth of our services business revenues, up 10% for the year. We made huge strides in cost containment with operating expenses before charges lower by 20%, or \$9.0 million, well ahead of our \$6.0 million goal for annualized expense reduction. Before charges, we broke even for the first time since 2004, and I congratulate everyone at EMAK for getting us back in the black. Our balance sheet is in good shape with ample cash, zero debt and an untapped credit facility.

We have worked diligently with an agenda of: a) nurturing and growing our services-based agencies, while b) restructuring our collection of promotional products agencies into a coherent, rolled-up, efficient group offering the highest quality in customer service and product integrity, and c) revamping our corporate structure to better serve the needs of our agencies and to be as transparent as possible to all stakeholders.

**I am pleased that EMAK's transformational actions have been implemented successfully, and we are now better positioned to return to meaningful profitability and sustained growth. I still see much work ahead for the leadership team and all employees at EMAK, but we're on the right path to build a truly great family of marketing agencies.**

EMAK's "Transformation" Agenda
<b>A. Build Services</b> Investments made in services agencies fueling growth Neighbor Agency launched to deliver better-for-all marketing
<b>B. Rebuild Promotional Products</b> Five promotional agencies fully-integrated to be highest quality and profitable Unprofitable European agencies closed
<b>C. Right-Size Business Model</b> Reduced public-company costs Redundant facilities closed Cash generation the priority Healthy balance sheet
<b>Next: Actively Pursuing Recapitalization</b>

EMAK's business model is now supporting growth across all the agencies. Let me highlight the three main themes that comprise our agenda for 2009.

**1. Continue to Transform EMAK**

EMAK is now in a new era of opportunity and growth following its multi-stage transformation that began three years ago with a new management team and an exhaustive redesign of operations. We have successfully consolidated the promotional products acquisitions into one agency team in order to tap into the efficiencies embedded in their operations, and to go-to-market with enough scale and reach to be attractive to global clients. The consolidation process was completed in 2008 as remaining units Equity Marketing and Logistix were unified under a single leadership team with shared operations. Throughout this hard work, our core teams stayed engaged, with voluntary turnover in 2008 at 14%, its lowest in EMAK's recent history. (To learn more about our promotional products agencies, visit [www.equity-marketing.com](http://www.equity-marketing.com) and [www.logistixmarketing.com](http://www.logistixmarketing.com).)

As part of the promotional products move to reliability and profitability, we liquidated our unprofitable European operations.

Our agency services businesses now represent EMAK's growth engine. Upshot continues to experience very positive business momentum with increasing revenues from current clients as well as the addition of major new clients. For the second year in a row, the agency has been recognized by Crain's Chicago Business as one of the Best Places to Work in Chicago. (For more information, visit Upshot at [www.upshot.net](http://www.upshot.net).)

Further, the Neighbor agency was born from a strategic corporate initiative to capitalize on the healthy-living marketing segment, and staffed initially by existing employees who are passionate about better-for-all marketing. Launched from the ground up less than one year ago and profitable from day one, today Neighbor has roughly \$3 million in revenues, 16 employees and several blue chip clients. (To learn more about Neighbor, visit [www.neighboragency.com](http://www.neighboragency.com).)

Our agencies are now well-positioned, each one profitable, each one growing and each one staffed by incredible people who go the extra mile to deliver for our clients.

## 2. Focus

During the heavy lifting and tough calls we've had to make during our transformation, our focus has been and continues to be on profitable growth and cash generation via delivering the highest-quality work and superior service to our clients.

The table below illustrates our focus on cash generation. EMAK's historical operations can be segmented into three distinct periods. The first period is EMAK's IPO through 2000, and during this period, EMAK serviced one client profitably, went public, and raised \$25 million in investment capital from Crown Capital. The second period is EMAK's acquisition period during which EMAK made a series of acquisitions and executed its share buyback, in effect using up nearly all the cash generated in the prior period. During the third period, beginning July 2005 and ending December 31, 2008, our focus on cash generation and preservation and overall EMAK transformation is apparent.

	IPO (1994) - December 31, 2000	January 1, 2001 - June 30, 2005	July 1, 2005 - December 31, 2008
Beginning Cash (a)	\$ 3,944	\$ 37,505	\$ 4,887
<b>Sources of Funds:</b>			
Cash flow from Operations	\$ 42,348	\$ 23,346	\$ 9,720 (b)
IPO, net	6,032	-	-
Preferred stock issuance (dividends)	23,702	(6,750)	(1,282)
Bank financing (payments)	-	875 (c)	(875)
Proceeds from stock option exercise	4,377	3,814	(248)
Net cash received	<u>76,459</u>	<u>21,285</u>	<u>7,315</u>
<b>Uses of Funds:</b>			
Capital expenditures	(9,768)	(5,830) (c)	(4,667) (d)
Acquisitions (net of cash)	(28,790)	(36,181)	(1,380)
Stock buyback	(4,340)	(11,892)	-
Net cash used	<u>(42,898)</u>	<u>(53,903)</u>	<u>(6,047)</u>
Total Cash Received (Used)	\$ <u>33,561</u>	\$ <u>(32,618)</u>	\$ <u>1,268</u>
Ending Cash (a)	\$ <u>37,505</u>	\$ <u>4,887</u>	\$ <u>6,155</u>
(a) Includes Cash, Restricted Cash and Marketable Securities.			
(b) The \$9.7 million of Cash Flow from Operations for the period July 1, 2005 through December 21, 2008 is presented net of (i) \$5.2 million of cash paid related to the restructurings and reorganizations, which occurred during 2005 and through 2008 and (ii) approximately \$1.3 million of severance paid to the former CEO, who left the Company during the second quarter of 2005.			
(c) Amounts presented net of approximately \$1.3 million of mortgage loan repayment and related proceeds from the sale of a building.			
(d) Amounts presented net of approximately \$0.5 million, received from a landlord for tenant improvements.			

Further, we deregistered our common stock due to the limited trading volume and the high costs associated with preparing and filing periodic reports and other filings with the SEC in comparison to the size of the company. To continue to support the over-the-counter trading of our common stock, we have and will remain current in the flow of information by continuing to issue press releases and make news announcements of important events and posting them on our website, including quarterly and annual financials in accordance with our normal reporting schedule. Summary financial information accompanies this letter at pages 6 and 7. Our complete audited financial statements for the fiscal year ended December 31, 2008 are posted at [www.emak.com](http://www.emak.com) on the Investor Info page under Financial Reports.

Operationally, the team has been focused and pragmatic. As one example, we launched Neighbor with the caveat that it needed to make money from day one. We also took the step to freeze salaries and are holding open positions until the economic picture becomes clearer. We have reduced capital expenditures by renegotiating with suppliers and by finding more efficient solutions, without jeopardizing our systems integrity. And finally we are exiting Europe as efficiently as possible. The management team is leading EMAK's transformation, with clear focus on growth and on cash preservation and generation.

### 3. Take the Right Path

The marketing industry continues to evolve rapidly, and we are serving our clients with effective marketing programs and products. We know that conventional tactics, such as broadcast advertising, “push” marketing, one-way communication, and broad-based image-building without activation are all fading. Savvy clients are turning to EMAK’s agencies for smarter, more effective business-building marketing initiatives.

EMAK’s corporate structure is now set to fuel future growth. Our highly-productive shared services group serves the company efficiently, and with trimmed public company costs we have significant leverage in our business model. We are projecting positive EBITDA before charges in 2009, approximately flat when compared to 2008, and we should have positive net cash flow for 2009 and no debt.

In spite of this, EMAK’s market cap of late ranges from approximately \$2 million to \$4 million, which is below the cash we have on hand, indicative of the illiquid market for our stock, and not uncommon in today’s market. Including the preferred stock, EMAK’s total market value is below \$30 million and well below my estimate for our fair enterprise value. Our growing services agency, Upshot, should be valued at a premium to net sales. And our combined products businesses are of the highest quality, with losses purged. We are not in the specialty advertising (“ASI”) business, which is suffering in this economy, but in the higher-end, value-added customized promotional products business. This business demands a higher level of service, quality and total supply chain management, and our agencies are among a select group that can do this work, and should also be valued above net sales. Add to these our significant tax assets to offset future earnings, and together, EMAK should have an enterprise value far in excess of the current market value.

While I continue to believe that delivering improved financial results is the best way to increase shareholder value, I also realize that we must consider all strategic alternatives. To this end, we have engaged Barrington Associates, a division of Wells Fargo, to assist us. This work is ongoing.

Finally, let me say that EMAK has a great team working hard to meet the future head on. We are committed to the success of our clients and EMAK. Many thanks to my fellow board members, my outstanding management team and dedicated employees, as well as our clients and shareholders, for remaining committed to EMAK.

I’m proud of what we have achieved in 2008 and look forward to the future success of EMAK.



Jim Holbrook  
Chief Executive Officer

Recent Accomplishments Timeline			
		Upgraded its technology and R&D systems	
		Implemented enterprise improvement system	Exiting remaining unprofitable operations based in Europe
		Established Neighbor agency	Serving global clients' needs from offices in Los Angeles and Asia
Integrated five promotional agencies into one		Engaged Barrington Associates to explore strategic initiatives following an unsolicited takeover bid	Revenue growth
Changed focus; clients first, agencies second, corporate last	Began restructuring to bring costs in line with revenues	Reduced size of Board of Directors	Path to profitability
Exited redundant facilities	Extended contract with largest client through 2010	Reduced public-company costs by deregistering common stock and engaging new auditors	Good cash generation
Streamlined management structure	Integrated products business under single unified leadership team	Closed London-based office	Improved shareholder returns
<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009 and beyond</b>

## 2008 FINANCIAL HIGHLIGHTS

- With net income before charges at breakeven, the fiscal year 2008 represented EMAK's first profitable year since 2004 and a substantial improvement over the \$3.7 million comparable net loss reported in 2007
- EMAK's U.S. operations posted their second consecutive year of profitability
- EBITDA before charges and non-cash expenses was \$2.9 million in 2008, surpassing management's original projection of \$2.0 million set forth in January 2008
- Operating expenses before charges were reduced by 20 percent, or \$9.0 million, for the twelve-month period ended December 31, 2008, far exceeding EMAK's original cost reduction target of \$6.0 million
- EMAK generated \$4.7 million of cash from operations during 2008, versus \$5.0 million of cash used in fiscal year 2007. Cash generated in 2008 includes \$0.6 million provided by a landlord in Chicago to build out new lease space
- Reported \$6.2 million in cash and cash equivalents; ended the year debt-free

<b>RECENT FINANCIAL RESULTS</b>			
EMAK Worldwide, Inc.			
Condensed Results of Operations - Selected Data			
<i>(In thousands, except share and per share data)</i>			
	Twelve Months Ended December 31,		
	<u>2007</u>	<u>2008</u>	
Revenue	\$ 164,174	\$	150,378
Gross profit	41,324		36,086
Loss from operations	(7,754)		(2,202)
Net loss	(7,616)		(2,011)
Basic loss per share	\$ (1.30)	\$	(0.32)
Diluted loss per share	\$ (1.30)	\$	(0.32)
EBITDA, before charges and non-cash expenses, is calculated as follows:			
	Twelve Months Ended December 31,		
	<u>2007</u>	<u>2008</u>	
Net loss	\$ (7,616)	\$	(2,011)
Interest expense (income), net	(75)		84
Provision for income taxes	212		294
Depreciation	1,536		1,696
Amortization	60		2
EBITDA	<u>(5,883)</u>		<u>65</u>
Charges:			
Restructuring charges	584		2,010
Impairment of assets	3,298		68
Non-cash expenses:			
Amortization of share-based awards*	1,441		755
EBITDA, before charges and non-cash expenses	<u>\$ (560)</u>	<u>\$</u>	<u>2,898</u>
Note: (*) Reflects the impact of forfeitures in the fourth quarter of 2008			
Net income (loss), before charges, is calculated as follows:			
	Twelve Months Ended December 31,		
	<u>2007</u>	<u>2008</u>	
Net loss	\$ (7,616)	\$	(2,011)
Charges:			
Restructuring charges	584		2,010
Impairment of assets	3,298		68
Net income (loss) before charges	<u>\$ (3,734)</u>	<u>\$</u>	<u>67</u>
<b>Consolidated Balance Sheet - Selected Data</b>			
<i>(In thousands)</i>			
	December 31,		December 31,
	<u>2007</u>	<u>2008</u>	
Cash, cash equivalents and restricted cash	\$ 3,378	\$	6,155
Working capital	6,408		6,604
Total assets	51,443		48,385
Total liabilities	31,967		30,120
Redeemable preferred stock recorded in mezzanine (a)	19,041		-
Total stockholders' equity (a)	\$ 435	\$	18,265
(a) Redeemable preferred stock was reclassified in 2008 from "mezzanine" to stockholders' equity			

Certain expectations and projections regarding the future performance of EMAK Worldwide, Inc. discussed in this letter are forward-looking and are made under the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. These expectations and projections are based on currently available competitive, financial and economic data along with the Company's operating plans and are subject to future events and uncertainties. Management cautions the reader that the following factors, among others, could cause the Company's actual consolidated results of operations and financial position in 2009 and thereafter to differ significantly from those expressed in forward-looking statements: the Company's dependence on a single customer; the significant quarter-to-quarter variability in the Company's revenues and net income; the Company's dependence on the popularity of licensed entertainment properties and the ability to license, develop and market new products; the Company's dependence on foreign manufacturers; the Company's need for additional working capital; the negative results of litigation, governmental proceedings or environmental matters; and the potential negative impact of past or future acquisitions. The Company undertakes no obligation to publicly release the results of any revisions to forward-looking statements, which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. The risks highlighted herein should not be assumed to be the only items that could affect the future performance of the Company.