CMGI INC
Form 10-K
October 16, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended July 31, 2006

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

For the Transition Period From to

Commission File 000-23262

CMGI, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**04-2921333**
(State or other jurisdiction	**(I.R.S. Employer**
of incorporation or organization)	**Identification No.)**
1100 Winter Street	
Waltham, Massachusetts	**02451**
(Address of principal executive offices)	**(zip code)**

(781) 663-5001

Registrant s telephone number, including area code

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:	**Name of each Exchange on which registered:**
Common Stock, $0.01 par value	**The NASDAQ Stock Market LLC**

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or 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 by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The approximate aggregate market value of registrant s Common Stock held by non-affiliates of the Registrant on January 31, 2006, based upon the closing price of a share of the Registrant s Common Stock on such date as reported by the Nasdaq Global Market (formerly the Nasdaq National Market): $683,193,579.

On October 9, 2006, the Registrant had outstanding 486,937,596 shares of Common Stock, $0.01 par value.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement (the Definitive Proxy Statement) to be filed with the Securities and Exchange Commission relative to the Company s 2006 Annual Meeting of Stockholders are incorporated by reference into Part III of this Report.

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ANNUAL REPORT ON FORM 10-K

FISCAL YEAR ENDED JULY 31, 2006

CMGI, INC.

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes, anticipates, plans, expects and similar expressions are intended to identify forward-looking statements. The important factors discussed under the caption Risk Factors in Item 1A of this report, among others, could cause actual results to differ materially from those indicated by forward-looking statements made herein and presented elsewhere by management. Such forward-looking statements represent management s current expectations and are inherently uncertain. Investors are warned that actual results may differ from management s expectations. CMGI does not undertake any obligation to update forward-looking statements.

PART I

ITEM 1. BUSINESS

General

CMGI, Inc. (together with its consolidated subsidiaries, CMGI or the Company), through its subsidiary, ModusLink Corporation (ModusLink), provides industry-leading global supply chain management services that help businesses market, sell and distribute their products and services. In addition, CMGI s venture capital business, @Ventures, invests in a variety of technology ventures. The Company previously operated under the name CMG Information Services, Inc. and was incorporated in Delaware in 1986. CMGI s address is 1100 Winter Street, Suite 4600, Waltham, Massachusetts 02451.

CMGI s business strategy in recent years has led to the development, acquisition and operation of majority-owned subsidiaries focused on supply chain management services, as well as the strategic investment in other companies. A further description of the Company s recent developments is set forth in Notes 4 and 6 of the Notes to Consolidated Financial Statements included in Item 8 below and is incorporated herein by reference.

On August 2, 2004, CMGI completed its acquisition of Modus Media, Inc., a privately held provider of supply chain management solutions (Modus), which conducted business through its wholly owned subsidiary, Modus Media International, Inc. CMGI acquired Modus in order to expand the geographic presence of its supply chain management offerings, diversify its client base, broaden its product and service offerings and bolster its management team.

Prior to the Modus acquisition, CMGI s supply chain management business was operated by SalesLink LLC (formerly SalesLink Corporation) and its subsidiary, SL Supply Chain Services International Corp. SalesLink LLC was contributed by CMGI to ModusLink on August 2, 2004. Thereafter, ModusLink succeeded to SalesLink s supply chain management business and SalesLink continued to operate a marketing distribution services business focused on financial services companies. On June 28, 2006, SalesLink s marketing distribution services business was sold to Automatic Data Processing, Inc. (ADP).

Upon closing of the acquisition, Modus Media International, Inc. was renamed ModusLink Corporation. Through the formation of ModusLink, CMGI has created a supply chain management market leader with fiscal 2006 revenue of $1.1 billion, 41 locations in 13 countries (including four locations in Japan operated by an entity in which the Company has a 40% interest), including a significant presence in Asia and Europe. ModusLink has a widely diversified client base that includes leaders in the hardware, software, consumer electronics, telecommunications and storage markets. As a result of the Modus acquisition, the Company modified its organizational structure to closely resemble the operating model historically used by Modus. This operating structure is aligned along the Americas, Asia and Europe regions. Each of these regions has designated management teams with direct responsibility over the operations of the respective regions. As a result, the Company now reports three operating segments, Americas, Asia and Europe.

As used herein, references to SalesLink for periods prior to August 2, 2004 refer to SalesLink Corporation and SL Supply Chain Services International Corp., which was contributed by CMGI to SalesLink on July 31, 2003 and together comprised the Company s supply chain management business prior to the Modus acquisition. References to SalesLink for periods including and after August 2, 2004 refer to CMGI s marketing distribution services business. All references to ModusLink include both the supply chain management and marketing distribution services businesses.

Products and Services

Supply Chain Management Services and Solutions

Through ModusLink, we provide end-to-end supply chain management services and solutions to the technology industry on a global scale. The services and solutions are designed to optimize the supply chain, helping companies improve time to market, inventory management, customer service and distribution. Our clients include hardware manufacturers, software publishers, storage and consumer electronic device manufacturers, telecommunication carriers, broadband and wireless service providers and other companies that engage us to manage and perform the multiple business processes throughout the end-to-end supply chain. Our core execution services include consulting and demand planning, sourcing and supply base management, manufacturing and product configuration, logistics management, marketing distribution and print-on-demand, e-commerce, sales support and the complete range of after market services, from testing and repair to asset disposition. We are also a Microsoft Authorized Replicator, further enhancing our position as a valued supply chain services provider to leading technology hardware original equipment manufacturers (OEMs).

We have many years of experience servicing the supply chain management needs of companies in the technology market. We offer a complete line of customized, vertical market solutions designed and configured to address the supply chain needs and challenges specific to the computing, software, consumer electronics, storage and communications industries.

We also offer go-to-market solutions designed to help companies quickly, efficiently and cost-effectively enter new geographic markets, where we have established operations and local market expertise. These solutions leverage a set of pre-configured, end-to-end services and processes designed to help companies manufacture and/or distribute their products in regions where they currently have no supply chain infrastructure or local market operating knowledge.

Additionally, using our information technology (IT) systems and infrastructure, we manage the flow and use of information throughout the supply chain. ModusLink s robust technology infrastructure serves as the backbone of a client s fully-integrated global supply chain solution. We offer a secure and redundant network environment to ensure our clients data and information is secure and accurate. We work with clients to integrate data, tools and applications to create a technology solution that meets our clients business needs and improves management of the global supply chain.

We are in the process of upgrading and further integrating our Enterprise Resource Planning (ERP) system. Our infrastructure spans critical aspects of supply chain processes from beginning to end and serves as the foundation for the design, integration and ongoing management of a client s global supply chain. Our new ERP system is designed to provide the visibility and control needed for better decision making, more rapid response to global market dynamics and effective asset utilization across services and geographies. Our new operating infrastructure is expected to leverage an integrated global systems platform, standardized process execution, strategic global management, industry expertise and local market knowledge to provide clients with more effective global operations management.

Our global operational footprint consists of an integrated network of 41 strategically located facilities (including four locations in Japan operated by an entity in which the Company has a 40% interest) in 13 countries, including numerous sites throughout North America, Europe and Asia. ModusLink s regionally-optimized and highly-scalable solution centers are designed to provide the flexibility to deliver and configure products in-region, close to the customer or in low-cost regions, such as China, Eastern Europe and Mexico for maximum efficiency and cost-effectiveness.

Sales and Marketing

ModusLink s sales and marketing staffs are strategically, and globally, aligned to support the development, marketing and sale of our supply chain management services and solutions worldwide.

Our marketing efforts are focused on developing greater awareness and brand recognition among our target client base, with an emphasis on companies within our key vertical markets of computing, software, storage, consumer electronics and communications. We market our services and solutions through our website, public relations, advertising and tradeshow campaigns and are developing a wide range of collateral materials and sales tools to support these efforts. Additionally, our global product marketing staff is focused on the ongoing development, positioning and marketing of new services and solutions, including customized, vertical market solutions; high-value core execution services; and geographic go-to-market solutions. This marketing staff also identifies and generates new opportunities and leads within these markets.

ModusLink sells its services and solutions on a global scale, through the direct sales channel. Our strategically aligned, global sales staff creates new opportunities and cultivates leads in all of our key regions throughout North America, Europe and Asia as well as within our target vertical markets around the world. Our sales staff helps us to further diversify our client base.

Competition

The markets for the supply chain management and marketing distribution service offerings provided by ModusLink are very competitive. As an end-to-end solutions provider with services offerings covering a range of supply chain operations and activities across the globe, ModusLink competes with a number of different vendors, both global and regional, in a number of different service areas. We expect the intensity of competition to continue to increase from both global and regional competitors. A failure to maintain and enhance our competitive position, including the expansion into geographical areas where we currently have no presence, will limit our ability to maintain and increase market share, which could result in serious harm to our business. Increased competition may also result in price reductions, reduced gross margins and loss of market share. We compete in the supply chain management market on the basis of quality, performance, service levels, global capabilities, technology, operational efficiency and price.

Some of our competitors have substantially greater financial, infrastructure, personnel, and other resources than we do. Furthermore, some of our competitors have well established, large and experienced marketing and sales capabilities and greater name recognition, including well established relationships with our current and potential clients. As a result, our competitors may be in a stronger position to respond quickly to new or emerging technologies and changes in client requirements. They may also develop and promote their services more effectively than us and may have more strategic geographical locations in low cost production areas of the world. Also, we may lose potential clients to competitors for various reasons, including the ability or

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willingness of competitors to offer lower prices and other incentives or concessions that we cannot or will not match. There can be no assurance that our competitors will not develop products and services that are superior to ours or that achieve greater market acceptance than our offerings.

Venture Capital

The Company maintains interests in several venture capital funds: CMG@Ventures I, LLC (CMG@Ventures I), which was dissolved on July 31, 2006; CMG@Ventures II, LLC (CMG@Ventures II); CMG@Ventures III, LLC (CMG@Ventures III); CMG@Ventures Expansion, LLC (CMG@Ventures Expansion); CMGI@Ventures IV, LLC (CMGI@Ventures IV); and @Ventures V, LLC (@Ventures V). These venture capital funds invest in emerging, innovative and promising technology companies.

The Company owned 100% of the capital and was entitled to approximately 77.5% of the cumulative net profits of CMG@Ventures I. The Company owns 100% of the capital and is entitled to approximately 80% of the cumulative net profits of CMG@Ventures II.

The @Ventures III venture capital funds (@Ventures III Fund) were formed in August 1998. The @Ventures III Fund secured capital commitments from outside investors and CMGI, to be invested in emerging Internet and technology companies. The @Ventures III Fund consists of four entities, which co-invest in each investment made by the @Ventures III Fund. Approximately 78% of each investment made by the @Ventures III Fund is made by two entities, @Ventures III, L.P. and @Ventures Foreign Fund III, L.P. CMGI does not have a direct ownership interest in either of these entities, but CMGI is entitled to approximately 0.1% of the capital of each entity as a result of its ownership of an approximately 10% interest in the general partner of each of such entities, @Ventures Partners, III, LLC (@Ventures Partners III). CMG@Ventures III co-invests approximately 20% of the total amount invested in each @Ventures III Fund portfolio company investment. CMGI owns 100% of the capital and is entitled to approximately 80% of the cumulative net capital gains realized by CMG@Ventures III. @Ventures Partners III is entitled to the remaining 20% of the net capital gains realized by CMG@Ventures III. The remaining 2% invested in each @Ventures III Fund investment is provided by a fourth entity, @Ventures Investors, LLC, in which CMGI has no interest. During fiscal year 2000, CMGI formed additional venture capital fund entities to provide follow-on financing to @Ventures III Fund portfolio companies. These expansion funds have a structure that is substantially identical to the @Ventures III Fund, and CMGI s interests in such funds are comparable to its interests in the @Ventures III Fund.

CMGI owns 100% of the capital and is entitled to a percentage (ranging from approximately 80% to approximately 92.5%) of the net profits realized by CMGI@Ventures IV on each of its investments.

During fiscal year 2004, CMGI formed @Ventures V. CMGI owns 100% of the capital and is entitled to approximately 92% of the net profits realized by @Ventures V.

An aggregate of approximately $6.8 million was invested by CMGI s venture capital business, @Ventures, during the fiscal year ended July 31, 2006. In addition, in three separate transactions, the Company received distributions of approximately $36.5 million from the acquisition by third parties of certain of its venture capital portfolio companies during fiscal 2006.

As of July 31, 2006, the Company, through @Ventures, held investments in 15 portfolio companies. From time to time, the Company may make new and follow-on venture capital investments and will from time to time receive distributions from the @Ventures entities as a result of previous investments made in the portfolio. As of July 31, 2006, the Company was not obligated to fund any new or follow-on investments.

Other

In recent years, a limited number of clients accounted for substantially all of the Company s consolidated net revenue. For the fiscal year ended July 31, 2004, sales to one client, Hewlett-Packard, accounted for 74% of our consolidated revenue. Through the Modus acquisition, the Company addressed its client concentration and for fiscal year 2005, Hewlett-Packard accounted for 36% of the Company s consolidated net revenue. For fiscal year 2006, two clients, Hewlett-Packard and Kodak, accounted for 30% and 11%, respectively, of the Company s consolidated net revenue. During fiscal year 2006, five clients, accounted for approximately 60% of the Company s net revenues. The Company currently does not have any agreements that obligate any client to buy a minimum amount of products or services from CMGI or any subsidiary, or to designate CMGI or any subsidiary as its sole supplier of any particular products or services. The loss of a significant amount of business with any key client, could have a material adverse effect on CMGI. The Company believes that it will continue to derive the vast majority of its consolidated operating revenue from sales to a small number of clients. There can be no assurance that revenue from key clients will not decline in future periods.

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The Company relies upon a combination of patent, trade secret, copyright and trademark laws to protect its intellectual property. New trade secrets and other intellectual property are from time to time developed by the Company or obtained through the Company s acquisition activities. The Company s business is not substantially dependent on any single or group of related patents, trademarks, copyrights or licenses.

At July 31, 2006, the Company employed approximately 3,729 persons on a full-time basis. The Company s subsidiaries in Mexico are parties to collective bargaining agreements covering approximately 48 employees. The Company s subsidiaries in France and The Netherlands are parties to collective bargaining agreements covering approximately 518 employees pursuant to and in accordance with applicable law that provide representation for all employees of those subsidiaries. Approximately 274 of the employees of the Company s Irish subsidiaries are members of labor unions. The Company considers its employee relations to be good.

Certain segment information, including revenue, profit and asset information, is set forth in Note 3 of the Notes to Consolidated Financial Statements included in Item 8 below and in Management s Discussion and Analysis of Financial Condition and Results of Operations included in Item 7 below, and is incorporated herein by reference.

Significant clients information is set forth under the heading Diversification of Risk in Note 2 of the Notes to Consolidated Financial Statements included in Item 8 below and is incorporated herein by reference.

As of July 31, 2006, approximately 47%, 36% and 17% of the Company s long-lived assets were located in the Americas, Asia and Europe, respectively. As of July 31, 2005, approximately 48%, 36% and 16% of the Company s long-lived assets were located in the Americas, Asia and Europe, respectively. As of July 31, 2004 approximately 99% of the Company s long-lived assets were located in the Americas. Approximately 60%, 60% and 47% of the Company s consolidated revenue was generated outside the United States during fiscal years 2006, 2005 and 2004, respectively.

We sell our products and services to our clients primarily on a purchase order basis rather than pursuant to contracts with minimum purchase requirements. Consequently, sales are subject to demand variability by such clients and the Company purchases and maintains adequate levels of inventory in order to meet client needs rapidly and on a timely basis. The Company has no guaranteed price, quantity or delivery agreements with its suppliers. Because of the diversity of the Company s products and services, as well as the wide geographic dispersion of its facilities, the Company uses numerous sources for the wide variety of raw materials needed for its operations. The Company has not been adversely affected by an inability to obtain raw materials.

Available Information

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports available through our website, free of charge, as soon as reasonably practicable after we file such material with, or furnish it to the Securities and Exchange Commission. Our internet address is http://www.cmgi.com. The contents of our website are not part of this annual report on Form 10-K, and our internet address is included in this document as an inactive textual reference only.

ITEM 1A. RISK FACTORS

We operate in a rapidly changing environment that involves a number of risks, some of which are beyond our control. Forward-looking statements in this document and those we make from time to time through our senior management are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements concerning the expected future revenues or earnings or concerning projected plans, performance, or development of products and services, as well as other estimates related to future operations are necessarily only estimates of future results. We cannot assure you that actual results will not materially differ from expectations. Forward-looking statements represent our current expectations and are inherently uncertain. We do not undertake any obligation to update forward-looking statements. Factors that could cause actual results to differ materially from results anticipated in forward-looking statements include, but are not limited to, the following:

We may have difficulty achieving and sustaining operating profitability, and if we deplete our working capital balances, our business will be materially and adversely affected.

During the fiscal year ended July 31, 2006, we reported operating income of approximately $0.6 million. While we have reported operating profitability in recent past periods, as a result of a variety of factors discussed in this report, our revenue for a particular quarter is difficult to predict and may fluctuate significantly. We anticipate that we will continue to incur significant operating expenses in the future, including significant costs of revenue and general and administrative expenses. We also have

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significant commitments and contingencies, including borrowings under a revolving line of credit, real estate leases, continuing stadium sponsorship obligations, and inventory purchase obligations. Therefore, we cannot assure you that we will sustain operating profitability in the future. We may also use significant amounts of cash to grow and expand our operations, including through additional acquisitions. At July 31, 2006, we had a consolidated cash, cash equivalents, marketable securities and short-term investment balance of approximately $228.7 million and fixed contractual obligations of $217.7 million. If we are unable to sustain operating profitability, we risk depleting our working capital balances and our business will be materially adversely affected.

We derive a substantial portion of our revenue from a small number of clients and adverse industry trends or the loss of any of those clients could significantly damage our business.

We derive a substantial portion of our revenue by providing supply chain management services to a small number of clients. Our business and future growth will continue to depend in large part on the industry trend towards outsourcing supply chain management and other business processes. If this trend does not continue or declines, demand for our supply chain management services would decline and our financial results could suffer.

In addition, the loss of any one or more of our key clients would cause our revenues to decline. For the fiscal year ended July 31, 2006, sales to one client, Hewlett-Packard, accounted for approximately 30% of our consolidated net revenue. During the fiscal year ended July 31, 2006, five clients accounted for approximately 60% of our net revenues. We do not have any agreements which obligate any client to buy a minimum amount of products or services. We do not have any agreements which designate us as the sole supplier of any particular products or services. The loss of a significant amount of business with Hewlett-Packard or any other key clients, or a decision by any one of our key clients to significantly change or reduce the services we provide, could have a material adverse effect on our business. We cannot assure you that our revenue from key clients will not decline in future periods.

In addition, ModusLink has been designated as an authorized replicator for Microsoft. This designation provides a license to replicate Microsoft software products and documentation for clients who want to bundle licensed software with their hardware products. This designation is annually renewable at Microsoft s discretion. A failure to maintain authorized replicator status could result in a reduction in our business and our revenues.

Our quarterly results may fluctuate significantly.

Our operating results have fluctuated widely on a quarterly basis during the last several years. We expect that we may experience significant fluctuations in future quarterly operating results. Many factors, some of which are beyond our control, have contributed to these quarterly fluctuations in the past and may continue to contribute to fluctuations. Therefore, operating results for future periods are difficult to predict, and prior results are not necessarily indicative of results to be expected in future periods. These factors include:

- how well we execute on our strategy and operating plans;
- implementation of our strategic initiatives and achievement of expected results of these initiatives;
- demand for our products and services;
- timing of new product introductions or software releases by our clients or their competitors;
- payment of costs associated with our acquisitions, sales of assets and investments;
- timing of sales of assets and marketable securities;

market acceptance of new products and services;

seasonality;

temporary shortages in supply from vendors;

charges for impairment of long-lived assets and/or restructuring in future periods;

political instability or natural disasters in the countries in which we operate;

specific economic conditions in the industries in which we compete;

general economic conditions;

actual events, circumstances, outcomes, and amounts differing from judgments, assumptions, and estimates reflected in our Consolidated Financial Statements; and

changes in accounting rules.

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We believe that period-to-period comparisons of our results of operations will not necessarily be meaningful or indicative of our future performance. In some fiscal quarters our operating results may be below the expectations of securities analysts and investors, which may cause the price of our common stock to decline.

We may encounter problems in our efforts to increase operational efficiencies.

Following our acquisition of Modus in August 2004, we continue to identify ways to increase efficiencies and productivity and effect cost savings. We have undertaken and implemented projects designed to increase our operational efficiencies, including the standardization to a global business solutions platform through the investment of approximately $29.8 million in an Enterprise Resource Planning system. We have also begun the implementation of a shared services model utilizing centralized hub locations to service multiple spoke locations across the Americas, Asia and Europe regions. We cannot assure you that the completion of these projects will result in the realization of the expected benefits that we anticipate in a timely manner or at all. We may encounter problems with these projects that will divert the attention of management and/or result in additional costs. If we are unable to complete these projects in a timely manner and without significant problems, or do not achieve expected results, our business, financial position and operating results may be adversely affected.

We are subject to risks of operating internationally.

We maintain significant operations outside of the United States, and we will likely continue to expand these operations. Our success depends, in part, on our ability to manage and expand our international operations. This international expansion requires significant management attention and financial resources. Our operations will continue to be subject to numerous and varied regulations worldwide, some of which may have an adverse effect on our ability to develop our international operations in accordance with our business plans or on a timely basis.

We currently conduct business in Mexico, China, Taiwan, Singapore, Malaysia, the United Kingdom, Hungary, Ireland, the Czech Republic, France, The Netherlands and other foreign locations, in addition to our United States operations. International sales accounted for 60% of our total revenue for the fiscal year ended July 31, 2006. A portion of our international revenue, cost of revenue and operating expenses are denominated in foreign currencies. Changes in exchange rates between foreign currencies and the U.S. dollar may adversely affect our operating margins. There is also additional risk if the currency is not freely traded. Some currencies, such as the Chinese Renminbi, are subject to limitations on conversion into other currencies, which can limit or delay our ability to repatriate funds or engage in hedging activities. While we often enter into forward currency exchange contracts to manage a portion of our exposure to foreign currencies, future exchange rate fluctuations may have a material adverse effect on our business and operating results.

There are other risks inherent in conducting international operations, including:

- added fulfillment complexities in operations, including multiple languages, currencies, bills of materials and stock keeping units;
- the complexity of ensuring compliance with multiple U.S. and foreign laws, particularly differing laws on intellectual property rights, export control, taxation and duties; and
- labor practices, difficulties in staffing and managing foreign operations, political and social instability, health crises or similar issues, and potentially adverse tax consequences.

In addition, a substantial portion of our business is now conducted in China, where we face additional risks, including the following:

- the challenge of navigating a complex set of licensing and tax requirements and restrictions affecting the conduct of business in China by foreign companies;
- difficulties and limitations on the repatriation of cash;

- currency fluctuation and exchange rate risks;
- protection of intellectual property, both for us and our clients;
- evolving regulatory systems and standards; and
- difficulty retaining management personnel and skilled employees.

Our international operations increase our exposure to international laws and regulations. Noncompliance with foreign laws and regulations, which are often complex and subject to variation and unexpected changes, could result in unexpected costs and

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potential litigation. For example, the governments of foreign countries might attempt to regulate our products and services or levy sales or other taxes relating to our activities; foreign countries may impose tariffs, duties, price controls or other restrictions on foreign currencies or trade barriers; or a governmental authority could make an unfavorable determination regarding our operations, any of which could make it more difficult to conduct our business and have a material adverse effect on our business and operating results.

If we are unable to manage these risks, we may face significant liability, our international sales may decline and our financial results may be adversely affected.

We may have problems raising capital we need in the future.

Historically, we have financed our operations and met our capital requirements primarily through funds generated from operations, the issuance of common stock, the sale of our interests in subsidiaries, returns generated by our venture capital business and borrowings from lending institutions. Market and other conditions largely beyond our control may affect our ability to engage in future sales of our securities, the timing of any sales, and the amount of proceeds we receive from sales of our securities. Even if we are able to sell our securities in the future, we may not be able to sell at favorable prices or on favorable terms. In addition, this funding source may not be sufficient in the future, and we may need to obtain funding from outside sources. However, we may not be able to obtain funding from outside sources. In addition, even if we find outside funding sources, we may be required to issue to those outside sources securities with greater rights than those currently possessed by holders of our common stock. We may also be required to take other actions, which may lessen the value of our common stock or dilute our common stockholders, including borrowing money on terms that are not favorable to us or issuing additional shares of common stock. If we experience difficulties raising capital in the future, our business could be materially adversely affected.

A decline in the technology sector could reduce our revenues.

A large portion of our revenue comes from clients in the technology sector, which is intensely competitive and very volatile. Declines in the overall performance of the technology sector have in the past and could in the future adversely affect the demand for supply chain management services and reduce our revenues and profitability from these clients.

The gross margins in the supply chain management business are low, which magnifies the impact of variations in revenue and operating costs on our financial results.

As a result of intense price competition in the technology products marketplace, the gross margins in our supply chain management business are low, and we expect them to continue to be low in the future. These low gross margins magnify the impact of variations in revenue and operating costs on our financial results. Although we have identified initiatives designed to increase our gross margins, increased competition arising from industry consolidation and/or low demand for products may hinder our ability to maintain or improve our gross margins. Portions of our operating expenses are relatively fixed, and planned expenditures are based in part on anticipated orders. Our current ability to forecast the amount and timing of future order volumes is low, and we expect this to continue because we are highly dependent upon the business needs of our clients, which are highly variable. As a result, we may not be able to reduce our operating expenses as a percentage of revenue to mitigate any further reductions in gross margins. We may also be required to spend money to restructure our operations should future demand fall significantly in any one facility. If we cannot proportionately decrease our cost structure in response to competitive price pressures, our business and operating results could suffer.

We will continue to be subject to intense competition.

The markets for our products and services are highly competitive and often lack significant barriers to entry, enabling new businesses to enter these markets relatively easily. Numerous well-established companies and smaller entrepreneurial companies are focusing significant resources on developing and marketing products and services that will compete with our products and services. The market for supply chain management products and services is very competitive, and the intensity of the competition is expected to continue to increase. Any failure to maintain and enhance our competitive position would limit our ability to maintain and increase market share, which would result in serious harm to our business. Increased competition may also result in price reductions, reduced gross margins and loss of market share. In addition, many of our current and potential competitors will continue to have greater financial, technical, operational and marketing resources. We may not be able to compete successfully against these competitors. Competitive pressures may also force prices for supply chain management products and services down and these price reductions may reduce our revenues.

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Because our contracts do not contain minimum purchase requirements and we sell primarily on a purchase order basis, we are subject to uncertainties and variability in demand by clients, which could decrease revenue and adversely affect our financial results.

Our contracts do not contain minimum purchase requirements and we sell primarily on a purchase order basis. Therefore, our sales are subject to demand variability by our supply chain management clients, which is difficult to predict and may fluctuate significantly. The level and timing of orders placed by these clients vary for a variety of reasons, including seasonal buying by end-users, the introduction of new technologies and general economic conditions. If we are unable to anticipate and respond to the demands of our supply chain management clients, we may lose clients because we have an inadequate supply of products, or we may have excess inventory, either of which may harm our business, financial position and operating results.

We must maintain adequate levels of inventory in our supply chain management business in order to meet client needs, which presents risks to our financial position and operating results.

We often purchase and maintain adequate levels of inventory in our supply chain management business in order to meet client needs rapidly and on a timely basis. The markets, including the technology sector served by many of our clients are subject to rapid technological change, new and enhanced product specification requirements, and evolving industry standards. These changes may cause inventory on hand to decline substantially in value or to rapidly become obsolete. Our clients offer limited protection, if any, from the loss in value of inventory. In addition, our clients may become unable or unwilling to fulfill their protection obligations. The inability of our clients to fulfill their protection obligations could lower our gross margins and cause us to record inventory write-downs. If we are unable to manage our inventory with our clients with a high degree of precision, we may have insufficient product supplies or we may have excess inventory, resulting in inventory write-downs, which may harm our business, financial position and operating results.

Our ability to obtain particular products or components in the quantities required to fulfill client orders on a timely basis is critical to our success. We have no guaranteed price or delivery agreements with our suppliers. We may occasionally experience a supply shortage of some products as a result of strong demand or problems experienced by our suppliers. If shortages or delays persist, the price of those products may increase, or the products may not be available at all. Accordingly, if we are not able to secure and maintain an adequate supply of products or components to fulfill our client orders on a timely basis, our business, financial position and operating results may be adversely affected.

Our failure to meet client demands could result in lost revenues, increased expenses and negative publicity.

Our supply chain management clients face significant uncertainties in forecasting the demand for their products. Limitations on the size of facilities, number of personnel and availability of materials could make it difficult to meet clients unforecasted demand for additional production. Any failure to meet clients specifications, capacity requirements or expectations could result in lost revenue, lower client satisfaction, negative perceptions in the marketplace and potential claims for damages.

If we are not able to establish client sites where requested, or if we fail to retain key clients at established sites, our client relationships, revenue and expenses could be seriously harmed.

Our supply chain management clients have, at times, requested that we add capacity or open a facility in locations near their sites. If we elect not to add required capacity at sites near existing clients or establish sites near existing or potential clients, clients may decide to seek alternate service providers. In addition, if we lose a significant client of a particular site or open or expand a site with the expectation of business that does not materialize, operations at that site could become unprofitable or significantly less efficient. Any of these events could have a material adverse effect on our business, revenues and expenses.

Venture capital investing is risky and highly speculative.

Through @Ventures we invest in privately held companies. We receive proceeds relating to our investments, if at all, only when a portfolio company engages in a liquidity event such as an initial public offering or the acquisition of a portfolio company by a third party. Liquidity events may take many years to materialize and the timing of liquidity events are difficult to predict. As a result there is much uncertainty as to the timing and impact of our venture capital portfolio on our financial results. Our ability to earn returns on our investment, or even recover our capital, is dependent upon factors outside of our control, including the success of our portfolio companies businesses, and the market for initial public offering and mergers and acquisitions. We typically own a minority position in our portfolio companies, which may afford us representation on the board of directors of a portfolio company but does not give us control over the entity. As a result we may have limited, if any, influence over our portfolio companies businesses and strategies. We cannot assure you that we will earn any returns or recover our invested capital.

We may be affected by strikes, work stoppages and slowdowns by our employees.

Some of our international employees are covered by collective bargaining agreements or represented by labor unions. We believe our relations with our employees are generally good; however, we may experience strikes, work stoppages or slowdowns by employees. A strike, work stoppage or slowdown may affect our ability to meet our clients needs, which may result in the loss of business and clients and have a material adverse effect on our financial condition and results of operations. The terms of future collective bargaining agreements also may affect our competitive position and results of operations.

The intellectual property of our supply chain management clients may be damaged, misappropriated, stolen or lost while in our possession, subjecting us to litigation and other adverse consequences.

In the course of providing supply chain management services to our clients, we have possession of or access to their intellectual property, including databases, software masters, certificates of authenticity and similar valuable intellectual property. If our clients intellectual property is damaged, misappropriated, stolen or lost, we could suffer:

- claims under client agreements or applicable law, or other liability for damages;
- delayed or lost revenue due to adverse client reaction;
- negative publicity; and
- litigation that could be costly and time consuming.

We may be liable if third parties misappropriate personal information of our clients customers.

We often handle personal information as part of our e-commerce offering. Any security breach could expose us to risks of loss, litigation and liability and could seriously disrupt our operations. If third parties are able to penetrate our network or telecommunications security or otherwise misappropriate the personal information or credit card information of our clients customers or if we give third parties improper access to such information, we could be subject to liability. This liability could include claims for unauthorized purchases with credit card information, impersonation or other similar fraud claims. They could also include claims for other misuses of personal information, including unauthorized marketing purposes. These claims could result in litigation. Liability for misappropriation of this information could be significant. Further, any resulting adverse publicity arising from investigations could have a material adverse impact on our business.

We depend on third-party software, systems and services.

Our business and operations rely on third parties to provide products and services, including IT products and services, and shipping and transportation services. We may experience operational problems attributable to the installation, implementation, integration, performance, features or functionality of third-party software, systems and services. Any interruption in the availability or usage of the products and services provided by third parties could have a material adverse effect on our business or operations.

We depend on important employees, and the loss of any of those employees may harm our business.

Our performance is substantially dependent on the performance of our executive officers and other key employees, as well as management of our subsidiaries. The familiarity of these individuals with technology and service-related industries makes them especially critical to our success. Our success is also dependent on our ability to attract, train, retain and motivate high quality personnel, especially for our subsidiaries management teams. Competition for personnel is intense. The loss of the services of any of our executive officers or key employees may harm our business.

Our strategy of expanding our business through acquisitions of other businesses and technologies presents special risks.

We may expand our business in certain areas through the acquisition of businesses, technologies, products and services from other businesses, as we have in the past. Acquisitions involve a number of special problems, including:

- the need to incur additional indebtedness, issue stock or use cash in order to complete the acquisition;
- difficulty integrating acquired technologies, operations and personnel with the existing businesses;
- diversion of management attention in connection with both negotiating the acquisitions and integrating the assets;
- strain on managerial and operational resources as management tries to oversee larger operations;
- the funding requirements for acquired companies may be significant;

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- exposure to unforeseen liabilities of acquired companies;
- increased risk of costly and time-consuming litigation, including stockholder lawsuits; and
- potential issuance of securities in connection with an acquisition with rights that are superior to the rights of our common stockholders, or which may have a dilutive effect on our common stockholders.

We may not be able to successfully address these problems. Our future operating results will depend to a significant degree on our ability to successfully integrate acquisitions and manage operations while also controlling expenses and cash burn.

The price of our common stock has been volatile and may fluctuate, in part, based on the value of our assets.

The market price of our common stock has been and is likely to continue to be volatile. In recent years, the stock market has experienced significant price and volume fluctuations, which have particularly impacted the market prices of equity securities of many companies providing technology-related products and services. Some of these fluctuations appear to be unrelated or disproportionate to the operating performance of these companies. Future market movements may adversely affect the market price of our common stock. In addition, should the market price of our common stock be below $1.00 per share for an extended period, we risk NASDAQ delisting, which would have an adverse effect on our business and on the trading of our common stock. In order to maintain compliance with NASDAQ listing standards, we may consider several strategies, such as a reverse stock split.

In addition, a portion of our assets includes the equity securities of both publicly traded and privately held companies. The market price and valuations of the securities that we hold may fluctuate due to market conditions and other conditions over which we have no control. Fluctuations in the market price and valuations of the securities that we hold in other companies may result in fluctuations of the market price of our common stock and may reduce the amount of working capital available to us.

We could be subject to infringement claims and other liabilities.

From time to time, we have been, and will continue to be, subject to third-party claims in the ordinary course of business, including claims of alleged infringement of intellectual property rights. These claims may damage our business by:

- subjecting us to significant liability for damages;
- resulting in invalidation of our proprietary rights;
- resulting in costly license fees in order to settle the claims;
- being time-consuming and expensive to defend even if the claims are not meritorious; and
- resulting in the diversion of our management s time and attention.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

At September 30, 2006, the Company s various properties in the Americas, Asia and Europe utilized for office, storage, warehouse, production and assembly, sales and marketing, and operations facilities include the following locations:

Location	**Approximate Sq. Ft.**
California(1)	580,000
Florida	34,000
Illinois	151,000
Indiana	96,000
Massachusetts	198,000
North Carolina	163,000
Oregon	16,000
Tennessee	250,000
Texas	187,000
Utah	513,000
China	332,000
Czech Republic	77,000

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Location	Approximate Sq. Ft.
France	84,000
Hungary	38,000
Ireland(2)	172,000
Mexico	109,000
The Netherlands(3)	369,000
Singapore	132,000
Taiwan	94,000
Total Square Feet	3,595,000

(1) Includes approximately 209,000 square feet not currently being utilized by the Company.

(2) Includes approximately 135,000 square feet located in a building owned by the Company and approximately 36,000 square feet not currently being utilized by the Company.

(3) Includes approximately 1600 square feet not currently being utilized by the Company.

The Company s leases generally expire at varying dates through fiscal year 2025 and include renewals at our option. Certain facilities leased by the Company are subleased in whole or in part to subtenants and the Company is seeking to sublease additional office and warehouse space that is not currently being utilized by the Company. We believe that our existing facilities are suitable and adequate for our present purposes, and that new facilities will be available in the event we need additional or new space.

ITEM 3. LEGAL PROCEEDINGS

From time to time, the Company may become involved in litigation relating to claims arising out of operations in the normal course of business, which it considers routine and incidental to its business. The Company currently is not a party to any legal proceedings, the adverse outcome of which, in management s opinion, would have a material adverse effect on the Company s business, results of operation or financial condition.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matter was submitted to a vote of the Company s stockholders during the fourth quarter of fiscal 2006.

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PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company s Common Stock trades on the Nasdaq Global Market under the symbol CMGI. Other market price information is set forth in Note 14 of the Notes to Consolidated Financial Statements included in Item 8 below and is incorporated herein by reference.

On September 14, 2006, there were approximately 5,638 holders of record of Common Stock of the Company.

The Company has never declared or paid cash dividends on its Common Stock. The Company currently intends to retain earnings, if any, to support its growth strategy and does not anticipate paying cash dividends in the foreseeable future. Payment of future dividends, if any, will be at the discretion of the Company s Board of Directors after taking into account various factors, including the Company s financial condition, operating results, current and anticipated cash needs and plans for expansion.

Information regarding the Company s equity compensation plans and the securities authorized for issuance thereunder is set forth in Item 12 below.

The Company did not repurchase any shares of Common Stock during fiscal 2006.

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ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following table sets forth selected consolidated financial information of the Company for the five years ended July 31, 2006. The following selected consolidated financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and the Company s Consolidated Financial Statements and notes to those statements included elsewhere or incorporated by reference in this report. The following consolidated financial data includes the results of operations of ModusLink (from date of acquisition of Modus in August 2004) and the fiscal 2002 acquisition of the assets and operations of iLogistix. The following consolidated financial data also includes the results of operations of certain subsidiary companies that have been sold or ceased operations. In fiscal 2002, the operations of NaviPath and MyWay ceased and the Company sold its interest in Activate. In fiscal 2003, the operations of ProvisionSoft ceased, the Company s former operating companies AltaVista and uBid each sold substantially all of their assets, and the Company divested its interest in NaviSite, Engage, Equilibrium, Yesmail, Tallán and its remaining minority interest in Signatures Network. In fiscal 2006, the Company sold its marketing distribution services business, SalesLink. For all periods presented, the results of operations of NaviSite, Engage, AltaVista, Yesmail, uBid, Tallán, ProvisionSoft and the marketing distribution services business of SalesLink have been accounted for within discontinued operations. A description of the Company s recent discontinued operations and divestiture activities is set forth in Note 4 of the Notes to Consolidated Financial Statements. The historical results presented herein are not necessarily indicative of future results.

	Years Ended July 31,				
	2006	2005	2004	2003	2002
	(in thousands, except per share data)				
Consolidated Statement of Operations Data:					
Net revenue	$ 1,148,886	$ 1,053,507	$ 381,315	$ 419,102	$ 147,028
Cost of revenue	1,030,655	933,063	359,989	389,742	135,878
Research and development					4,732
Selling	20,068	21,578	4,458	5,930	27,547
General and administrative	83,233	80,613	36,470	61,263	53,246
Amortization of intangible assets	4,824	5,226			4,723
Impairment of long-lived assets				456	2,482
Restructuring, net	9,521	5,258	5,604	55,348	(3,118)
Operating income (loss)	585	7,769	(25,206)	(93,637)	(78,462)
Interest income (expense), net	3,405	1,762	1,837	3,717	36,416
Other gains (losses), net	28,518	2,614	44,982	(14,255)	(22,511)
Other income (expense), net	(49)	(1,396)	(4,415)	(28,517)	(60,880)
Income tax benefit (expense)	(3,780)	19,933	69,532	(3,249)	7,096
Earnings (loss) from continuing operations before extraordinary item	28,679	30,682	86,730	(135,941)	(118,341)
Income (loss) from discontinued operations, net of income taxes	(13,734)	(4,157)	245	(80,367)	(537,858)
Extraordinary gain on retirement of debt, net of income taxes					131,281
Net income (loss)	14,945	26,525	86,975	(216,308)	(524,918)
Preferred stock accretion and amortization of discount					(2,301)
Gain on repurchase of Series C convertible preferred stock					63,505
Net income (loss) available to common stockholders	$ 14,945	$ 26,525	$ 86,975	$ (216,308)	$ (463,714)
Basic and diluted earnings (loss) per share:					
Earnings (loss) from continuing operations before extraordinary item	$ 0.06	$ 0.06	$ 0.22	$ (0.34)	$ (0.15)
Loss from discontinued operations, net of income taxes	(0.03)	(0.00)		(0.21)	(1.42)
Extraordinary gain on retirement of debt, net of income taxes					0.35
Net earnings (loss)	$ 0.03	$ 0.06	$ 0.22	$ (0.55)	$ (1.22)
Shares used in computing basic earnings (loss) per share	482,837	475,294	399,153	393,455	379,800

Shares used in computing diluted earnings (loss) per share	486,170	483,570	404,246	393,455	379,800

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	2006	2005	As of July 31, 2004 (in thousands)	2003	2002
Consolidated Balance Sheet Data:					
Working capital	$ 282,222	$ 224,638	$ 261,106	$ 217,135	$ 203,879
Total assets	763,219	721,684	423,026	449,581	909,676
Long-term obligations	51,813	25,929	18,768	26,016	122,697
Stockholders equity	497,915	471,215	293,315	247,012	416,696

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The matters discussed in this report contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, that involve risks and uncertainties. All statements other than statements of historical information provided herein may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes , anticipates , plans , expects and similar expressions are intended to identify forward-looking statements. Factors that could cause actual results to differ materially from those reflected in the forward-looking statements include, but are not limited to, those discussed in Item 1A above and elsewhere in this report and the risks discussed in the Company s other filings with the SEC. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management s analysis, judgment, belief or expectation only as of the date hereof. The Company undertakes no obligation to publicly revise these forward-looking statements to reflect events or circumstances that arise after the date hereof.

Overview

CMGI, through its subsidiary, ModusLink, provides industry-leading global supply chain management services. ModusLink provides extended supply chain management services and solutions to the technology industry on a global basis. These services and solutions include consulting and demand planning, sourcing and supply base management, manufacturing and product configuration, logistics management, marketing distribution and print-on demand, e-commerce, sales support and the complete range of after market services, from testing and repair to asset disposition. We invest in emerging, innovative and promising technologies and industries through our venture capital business, @Ventures. An aggregate of $6.8 million was invested by @Ventures in fiscal 2006 and $36.5 million of proceeds were received from liquidity events from portfolio companies.

Management evaluates operating performance based on net revenue, operating income (loss), and net income (loss), and, across its segments, on the basis of non-GAAP operating income (loss), which is defined as the operating income (loss) excluding net charges related to depreciation, long-lived asset impairment, restructuring, amortization of intangible assets and stock-based compensation. See Note 3 of Notes to Consolidated Financial Statements for segment information, including a reconciliation of non-GAAP operating income (loss) to net income (loss).

In fiscal 2004, we articulated the following goals:

- Make strategic investments to expand globally;
- Narrow our losses;
- Preserve our cash; and
- Improve our operating efficiencies.

We believe our acquisition of Modus Media, Inc. (Modus) on August 2, 2004, our sales and marketing efforts, and our cost savings initiatives implemented throughout fiscal 2005 and 2006 allowed us to make substantial progress in achieving these goals. The Modus acquisition increased our global footprint significantly, including multiple facilities in China, which has become an increasingly important region of the world for providing supply chain management services in support of many of our global clients and prospects. The integration of Modus with our existing supply chain management business to form ModusLink also improved our operating efficiency by eliminating redundancies, primarily in the areas of facilities and personnel, and by reducing our overall material and freight costs. These operating synergies provided approximately $19.0 million of cost savings in fiscal 2005, and over $28.0 million of annualized cost savings. In addition, in fiscal 2005, we reported our first annual operating profit in nine years.

During the latter part of fiscal 2005, we developed a set of strategic initiatives and an operating plan focused on increasing both revenue and profitability. We view the continued development of our global operational infrastructure and footprint as a

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primary source of differentiation in the marketplace. We believe that by leveraging our global footprint we will be able to optimize our client s supply chains using multi-facility, multi-geographic solutions. In line with this focus, during fiscal 2005, we made our initial investment in the implementation of a new global systems infrastructure, the foundation of which will be run on SAP s ERP system. During fiscal 2006 and as we move into fiscal 2007, our focus is on executing against our strategic plan, including implementing the following initiatives to achieve our goals:

Drive sales growth through a combination of existing client penetration, and targeting new vertical markets; A significant portion of our revenues are currently generated from clients in the computing and software verticals. These verticals are mature and, as a result, gross margins in these verticals are low. To address this, we have expanded our sales focus to include three new markets, in addition to the computing and software verticals, that we believe can benefit from our supply chain expertise. We believe these verticals, communications, including broadband, storage devices, and consumer electronics, are experiencing faster growth than our historical markets, and represent opportunities to realize higher gross margins on our services. Companies in these markets often are early in their product life cycles and have significant need for a supply chain partner who will be an extension to their business models.

Increase the value delivered to clients through service expansion; In fiscal 2006, we focused on and invested in expanding our e-commerce and logistics management services offerings, which we believe will increase the overall value of the supply chain solutions we deliver to our existing clients and to new clients. We expect these solutions will enhance our gross margins and drive greater profitability. Further, we believe that the addition of new services to existing clients will strengthen our relationship with these clients, and further integrate us with their business.

Drive operational efficiencies throughout our organization; As a result of the Modus acquisition, the Company has been running multiple information technology systems at a significant cost. Our strategy is to offer an integrated supply chain system infrastructure that extends from front-end order management through distribution and returns management. This end-to-end solution will enable clients to link supply and demand in real time, improve visibility and performance throughout the supply chain, and provide real-time access to information for greater collaboration and making informed business decisions. We believe our clients will benefit greatly from a global integrated business solution while we too reduce our operating costs. In fiscal 2006, we invested $14.8 million in this initiative and we expect to invest a total of approximately $29.8 million in this initiative. Another program that we expect will drive further operational efficiencies in the future, is the implementation of a global shared services model utilizing centralized hub locations to service multiple spoke locations across the Americas, Asia and Europe regions. We believe this initiative will yield improved process standardization and operating efficiency gains, as well as lower our operating costs.

We believe that successful execution of these initiatives will enable the Company to increase its gross margin percentage to approximately 12% to 14%, compared to the fiscal 2006 gross margins of approximately 10%. We also believe that these initiatives will allow us to reduce our overall selling, general and administrative, restructuring and amortization costs to approximately 7% of revenue. These actions are expected to result in an operating margin between 5% and 7%. We expect to make steady progress toward these goals and to be operating at this level by the end of fiscal year 2008. Among the key external factors that will influence our performance against these goals are successful execution and implementation of our strategic initiatives, global economic conditions, especially in the technology sector, demand for our clients products, and demand for outsourcing services.

For the year ended July 31, 2006, CMGI reported net revenue of $1.1 billion, an operating profit of $0.6 million, income from continuing operations of $28.7 million and net income of $14.9 million. Included in both our operating income and net income for the fiscal year ended July 31, 2006 was incremental stock-based compensation of $4.8 million related to the implementation of SFAS 123(R). We currently conduct business in the United Kingdom, The Netherlands, Hungary, France, Singapore, Taiwan, China, Malaysia, Ireland, the Czech Republic, Mexico and other foreign locations, in addition to the Company s United States operations. At July 31, 2006, we had cash and cash equivalents, available for sale securities and short-term investments of $228.7 million, and working capital of $282.2 million. Our primary use of cash during the fiscal year ended July 31, 2006 was for working capital requirements in support of new client programs and our new ERP system.

As a large portion of our revenue comes from outsourcing services provided to clients such as hardware manufacturers, software publishers, telecommunications carriers, broadband and wireless service providers and consumer electronics companies, our operating performance could be adversely affected by declines in the overall performance of the technology sector. The market for our supply chain management products and services is very competitive. We also face pressure from our clients to continually realize efficiency gains in order to help our clients maintain their gross margins and profitability. Increased competition and client demands for efficiency improvements may result in price reductions, reduced gross margins and in some cases loss of market share. As a result of these competitive and client pressures, the gross margins in our business are low. Increased competition arising from industry consolidation and/or low demand for our clients products and services may hinder our ability to maintain or improve our gross margins, profitability and cash flows. We must continue to focus on margin improvement, through implementation of our strategic initiatives, cost reductions and asset and employee productivity gains in order to improve the profitability of our business and maintain our competitive position. We are reacting to margin and pricing pressures in several ways, including efforts to target new vertical markets, expand our service offerings and to lower our infrastructure costs. Our ERP and hub and spoke initiatives are key enablers to drive efficiencies and lower our operating costs. We also seek to lower our cost to service clients by moving work to lower-cost venues, establishing facilities closer to our clients to gain efficiencies, and other actions designed to improve the productivity of our operations.

Historically, a limited number of key clients have accounted for a significant percentage of our revenue. For the fiscal year ended July 31, 2006, sales to Hewlett-Packard and Kodak accounted for approximately 30% and 11%, respectively, of our consolidated net revenue. During fiscal year 2006, five clients, accounted for approximately 60% of the Company s net revenues. We expect to continue to derive the vast majority of our operating revenue from sales to a small number of key clients. We currently do not have any agreements which obligate any customer to buy a minimum amount of products or services from us or designate us as an exclusive service provider. Consequently, our sales are subject to demand variability by our clients. The level and timing of orders placed by our clients vary for a variety of reasons, including seasonal buying by end-users, the introduction of new technologies and general economic conditions. In fiscal 2007, we expect to realize lower annual revenues from Kodak as a result of changes to certain programs that we currently execute on their behalf.

Basis of Presentation

As a result of the Modus acquisition, the Company modified its organizational structure to closely resemble the operating model historically used by Modus. This operating structure is aligned along the Americas, Asia, and Europe regions. Each of these regions has designated management teams with direct responsibility over the operations of the respective regions. As a result, the Company now reports three operating segments, Americas, Asia, and Europe.

In addition to its three current operating segments, the Company reports an Other category. The Other category represents corporate expenses consisting primarily of directors and officers insurance costs, costs associated with maintaining certain of the Company s information technology systems and certain corporate administrative functions such as legal and finance, as well as certain administrative costs related to the Company s venture capital business. The Other category also consists of any residual results from operations that exist through the cessation of operations of Equilibrium, MyWay, iCast, NaviPath, ExchangePath, and Activate, each of which have been divested or substantially wound down, as these entities do not meet the aggregation criteria under SFAS No. 131 with respect to the Company s current reporting segments. The Other category s balance sheet information includes certain cash equivalents, available-for-sale securities, investments and other assets, which are not identifiable to the operations of the Company s operating business segments.

During the second quarter of fiscal 2006, CMGI s Board of Directors authorized the divestiture of the Company s marketing distribution services business, SalesLink. At that time, management determined that this divestiture met the criteria for discontinued operations accounting in accordance with the provisions of Statement of Financial Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets . As such, the operating results of SalesLink have been segregated from continuing operations and have been reported as discontinued operations in the accompanying balance sheets, statements of operations and cash flows for all periods presented. SalesLink s business was sold in June 2006. See note 4 to the Consolidated Financial Statements.

Also during fiscal year 2006, the Company revised its presentation of discontinued operations in its statement of cash flows to separately disclose the operating, investing and financing portions of the cash flows attributable to its discontinued operations, which in prior periods were reported on a combined basis as a single amount.

Certain prior year amounts in the Consolidated Financial Statements have been reclassified in accordance with US GAAP to conform to the current year presentation.

In accordance with accounting principles generally accepted in the United States of America, all significant intercompany transactions and balances have been eliminated in consolidation. Accordingly, segment results reported by the Company exclude the effect of transactions between the Company and its subsidiaries and between the Company s subsidiaries.

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Results of Operations

Fiscal 2006 compared to Fiscal 2005

Net Revenue:

	2006	As a % of Total Net Revenue	2005	As a % of Total Net Revenue	$ Change	% Change
			($ in thousands)			
eBusiness and Fulfillment						
Americas	$ 479,093	42%	$ 433,147	41%	$ 45,946	11%
Asia	245,624	21%	212,595	20%	33,029	16%
Europe	424,169	37%	407,681	39%	16,488	4%
Total eBusiness and Fulfillment	1,148,886	100%	1,053,423	100%	95,463	9%
Other			84		(84)	(100)%
Total	$ 1,148,886	100%	$ 1,053,507	100%	$ 95,379	9%

Net revenue increased by $95.4 million or 9% year over year. This increase in net revenues was primarily the result of approximately $152.3 million of net revenues from two new global client programs awarded during fiscal 2005 which generated approximately $80.3 million, $32.5 million and $39.5 million of incremental revenues in the Americas, Europe and Asia, respectively. This net revenue growth was partially offset by form factor changes and price reductions of approximately $71.4 million during fiscal 2006. We have experienced reduced revenues from certain customer programs, primarily in Asia, as a result of the continued dematerialization of components or form factor changes to certain accessory kits which we produce for our clients. The price reduction impact to our revenues was largely attributable to certain price concessions in connection with the signing of a new multi-year contract in the spring of 2005 related to a major customer and its programs in the Asia region. Form factor relates to the simplification or elimination of components from our clients final products, which in turn reduces the Company s revenue and margin potential.

Two clients, Hewlett-Packard and Kodak, accounted for approximately 30% and 11%, respectively, of CMGI s consolidated net revenue for the fiscal year ended July 31, 2006. A significant portion of our annual volume in fiscal 2006 with Kodak was concentrated within the first six months of our fiscal year in support of seasonality based demand for Kodak s consumer products during the holiday season. In fiscal 2007, we expect to realize lower annual revenues from Kodak as a result of changes to certain programs that we currently execute on their behalf.

The Company continues to see volatility in demand for our clients products and as such maintains a conservative view on order volumes and revenue. Our current ability to forecast the amount and timing of future order volumes is low, and we expect such condition to continue for the foreseeable future, as the Company is highly dependent upon the business needs of its clients, whose businesses, in turn, depend upon various factors related to the high tech and consumer electronics sector generally and demand for products and services in that industry. The Company sells pursuant to contracts without minimum purchase requirements and on a purchase order basis. These purchase orders are generally for quantities necessary to support near-term demand for our clients products. A significant portion of our client base operates in the technology sector, which is intensely competitive and very volatile. Our clients order volumes vary from quarter-to-quarter for a variety of reasons, including market acceptance of their new product introductions and overall demand for their products. This business environment, and our mode of transacting business with our clients, does not lend itself to precise measurement of the amount and timing of future order volumes, and as a result, future sales volumes and revenues could vary significantly from period to period.

Cost of Revenue:

	2006	As a % of Segment Net Revenue	2005	As a % of Segment Net Revenue	$ Change	% Change
			(in thousands)			
eBusiness and Fulfillment						
Americas	$ 430,570	90%	$ 397,225	92%	$ 33,345	8%
Asia	197,190	80%	161,184	76%	36,006	22%
Europe	402,895	95%	374,654	92%	28,241	8%
Total eBusiness and Fulfillment	1,030,655	90%	933,063	89%	97,592	10%
Total	$ 1,030,655	90%	$ 933,063	89%	$ 97,592	10%

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Cost of revenue consists primarily of expenses related to the cost of products purchased for sale or distribution as well as salaries and benefit expenses, consulting and contract labor costs, fulfillment and shipping costs, and applicable facilities costs. Cost of revenue increased for the fiscal year ended July 31, 2006 primarily as a result of the increase in revenues as compared to the prior fiscal year. Overall net revenue increased 9% while cost of revenue increased 10%, as compared to the prior year. As a result, gross margins for the fiscal year ended July 31, 2006 were 10% as compared to 11% in the prior year, a $2.2 million decline.

The Company s gross margin percentages within the Americas, Asia and Europe regions were 10%, 20% and 5%, as compared to 8%, 24% and 8%, respectively, for the same period of the prior year. Within the Americas region, the $12.6 million or two-percentage point increase in gross margin percentage was primarily attributable to higher sales and the benefit of cost reduction initiatives implemented to improve operational efficiencies. Within the Asia region, the $3.0 million or four-percentage point decline in gross margin percentage was attributable to $27.9 million of increased business volumes and cost savings offset by $30.9 million of form factor changes and price reductions. While volumes have been strong, we have also experienced reduced revenues from certain customer programs as a result of the continued dematerialization of components or form factor changes to certain accessory kits which we produce for our clients. The price reductions impact was largely attributable to certain price concessions in connection with the signing of a new multi-year contract in the spring of 2005. Within the Europe region, $11.8 million or the three-percentage point decline in gross margin percentage was primarily attributable to $5.1 million of additional costs incurred in the second quarter to support a larger than anticipated surge in demand for a significant client s products during the holiday season. These costs primarily included higher freight expediting fees, warehousing and assembly costs, and distribution costs. In addition, gross margins in Europe were negatively impacted by $7.9 million of form factor changes and price reductions versus the prior year, partially offset by approximately $1.3 million of cost savings and increased business volumes.

As a result of the lower overall cost of delivering the Company s products and services in the Asia region, particularly China, and the increasing demand for supply chain management services in that region, we expect gross margin levels in Asia to continue to exceed those earned in the Americas and Europe regions. However, we expect that there will continue to be pressure on gross margin levels in Asia as the market, particularly China, matures. Our gross margins are impacted by a number of factors, including competition, order volumes, pricing, client and product mix and configuration, and overall demand for our clients products. A significant portion of the costs required to deliver our products and services is fixed in nature.

As outlined in our strategic initiative discussion in the Overview section above, the Company remains focused on margin improvement through several revenue and operating efficiency initiatives designed to improve the profitability of our business and maintain our competitive position. We are reacting to margin and pricing pressures in several ways including efforts to target new vertical markets, expand our service offerings and lower our infrastructure costs. We believe our ERP and hub and spoke initiatives are key enablers to drive efficiencies and lower our operating costs. We also seek to lower our cost to service clients by moving work to lower-cost venues and establishing facilities closer to our clients to gain efficiencies.

Selling Expenses:

	2006	As a % of Segment Net Revenue	2005	As a % of Segment Net Revenue	$ Change	% Change
			(in thousands)			
eBusiness and Fulfillment						
Americas	$ 7,504	2%	$ 7,019	2%	$ 485	7%
Asia	5,310	2%	6,874	3%	(1,564)	(23)%
Europe	7,254	2%	7,688	2%	(434)	(6)%
Total eBusiness and Fulfillment	20,068	2%	21,581	2%	(1,513)	(7)%
Other			(3)	(4)%	3	100%

Total	$ 20,068	2%	$ 21,578	2%	$ (1,510)	(7)%

Selling expenses consist primarily of compensation and employee-related expenses, sales commissions, facilities costs, marketing expenses and travel costs. During the fiscal year ended July 31, 2006, travel and entertainment, stock-based compensation, facility costs and employee related costs decreased by approximately $0.8 million, $0.4 million, $0.3 million and $0.2 million, respectively. These decreases were partially offset by higher consulting fees of approximately $0.2 million. The $0.5 million increase in selling expenses within the Americas region is primarily the result of higher employee-related costs as a result of higher commissions related to new business awarded during the year. The $1.6 million decrease in selling expenses within the Asia region is primarily the result of lower employee-related costs of approximately $0.9 million as a result of lower headcount, lower stock-based compensation of approximately $0.3 million and lower travel and entertainment of $0.1 million. The

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$0.4 million decrease in selling expenses within the Europe region is primarily the result of lower employee-related costs as a result of lower headcount. This decrease was partially offset by higher commissions. Of the Company s total selling expenses for the fiscal year ended July 31, 2006 and 2005, employee-related costs represented approximately 66% and 62% of the total selling expense in each period. The Company expects its selling expenses to continue to approximate 2% of net revenue for the foreseeable future.

General and Administrative Expenses:

	2006	As a % of Segment Net Revenue	2005	As a % of Segment Net Revenue	$ Change	% Change
			(in thousands)			
eBusiness and Fulfillment						
Americas	$ 19,676	4%	$ 23,183	5%	$ (3,507)	(15)%
Asia	21,802	9%	18,532	9%	3,270	18%
Europe	25,318	6%	21,955	5%	3,363	15%
Total eBusiness and Fulfillment	66,796	6%	63,670	6%	3,126	5%
Other	16,437		16,943		(506)	(3)%
Total	$ 83,233	7%	$ 80,613	8%	$ 2,620	3%

General and administrative expenses within the Americas, Asia, and Europe operating segments consist primarily of compensation and other employee-related costs, facilities costs, depreciation expense and fees for professional services. The total general and administrative expenses for these operating segments increased during the fiscal year ended July 31, 2006, as compared to the prior fiscal year, primarily as a result of $7.7 million of higher costs associated with the Company s migration to a new Enterprise Resource Planning (ERP) platform, higher depreciation of approximately $1.6 million primarily as a result of the change to the new ERP platform and $1.1 million of higher consulting costs. These costs were partially offset by approximately $3.3 million of lower employee-related costs, $1.9 million of lower legal and accounting costs and $1.1 million of lower stock-based compensation. Within the Americas region, the $3.5 million decrease in general and administrative expenses was primarily associated with lower employee-related costs of $3.1 million. Within the Asia region, the $3.3 million increase in general and administrative expenses was primarily associated with ERP initiative costs of approximately $3.8 million. This increase was partially offset by lower software and hardware maintenance of $0.7 million. Within the Europe region, the $3.4 million increase in general and administrative expenses was primarily associated with the ERP initiative costs of approximately $1.8 million, higher employee related costs of $0.2 million, higher facility related costs of $0.2 million and higher professional and accounting fees of $0.2 million.

The general and administrative expenses within the Other category primarily reflect the cost of the Company s directors and officers insurance, costs associated with certain corporate administrative functions such as legal and finance which are not fully allocated to the Company s subsidiary companies, and administration costs related to the Company s venture capital business. General and administrative expenses within the Other category decreased by approximately $0.5 million from the prior fiscal year primarily as a result of lower legal fees of approximately $1.6 million, lower consulting, accounting and professional fees of $2.3 million and lower insurance costs of $0.7 million. These decreases were partially offset by higher stock based compensation expense recorded in connection with the Company s adoption of SFAS No. 123(R) of approximately $2.9 million and higher employee related costs of $0.9 million. The Company expects its total general and administrative costs to approximate 8% of net revenue in fiscal 2007 due primarily to higher information technology expenditures associated with the Company s migration to a common ERP platform and stock compensation expense related to the continued application of SFAS No. 123(R). These increased general and administrative costs are expected to be partially offset by cost savings in connection with the implementation of the hub and spoke shared services model.

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Amortization of Intangible Assets:

	2006	As a % of Segment Net Revenue	2005	As a % of Segment Net Revenue	$ Change	% Change
			(in thousands)			
eBusiness and Fulfillment						
Americas	$ 2,124		$ 2,864	1%	$ (740)	(26)%
Asia	2,040	1%	1,895	1%	145	8%
Europe	660		467		193	41%
Total eBusiness and Fulfillment	4,824		5,226		(402)	(8)%
Total	$ 4,824		$ 5,226		$ (402)	(8)%

The intangible asset amortization relates to certain amortizable intangible assets acquired by the Company in connection with its acquisition of Modus. These intangible assets are being amortized over lives ranging from 1 to 7 years.

Restructuring, net:

	2006	As a % of Segment Net Revenue	2005	As a % of Segment Net Revenue	$ Change	% Change
			(in thousands)			
eBusiness and Fulfillment						
Americas	$ 1,170		$ 2,805	1%	$ (1,635)	(58)%
Asia	264		937		(673)	(72)%
Europe	8,038	2%	1,397		6,641	475%
Total eBusiness and Fulfillment	9,472	1%	5,139		4,333	84%
Other	49		119	142%	(70)	(59)%
Total	$ 9,521	1%	$ 5,258		$ 4,263	81%

During the fiscal year ended July 31, 2006, the Company recorded net restructuring charges of approximately $9.5 million. These charges consisted of approximately $5.3 million relating to a workforce reduction of 146 employees, primarily due to the elimination of redundant positions in Europe related to the Company s hub and spoke initiative, and in the Americas related to the reorganization of certain operational and sales activities. In addition, the Company recorded approximately $3.9 million of restructuring charges related to certain contractual obligations and real estate leases in connection with the consolidation of two facilities in the Netherlands and the closure of facilities in Ireland

and Scotland as part of the Company s efforts to continue to drive lower costs and operating efficiencies, as well as approximately $0.3 million relating to the impairment of certain assets no longer in service.

During the fiscal year ended July 31, 2005, the Company recorded net restructuring charges of approximately $5.3 million. These charges consisted of approximately $2.5 million related to a workforce reduction of 135 employees, approximately $3.3 million related to unutilized facilities for which the Company expects to realize no future economic benefit and approximately $0.1 million related to the impairment of certain assets no longer in service. In addition, the Company recorded adjustments of approximately $0.1 million to previously recorded restructuring estimates for facility lease obligations primarily based on changes to the underlying assumptions regarding the estimated length of time required to sublease each vacant space and the expected rent recovery rates. The Company also recorded an adjustment of approximately $0.5 million as the result of a gain on the sale of previously impaired assets that had been reflected within restructuring expense.

Interest Income/Expense:

During the fiscal year ended July 31, 2006, interest income increased $2.4 million to $6.2 million from $3.8 million from the prior fiscal year. The increase in interest income was the result of both higher average interest rates and higher average cash and cash equivalent and short-term investment balances during the current period compared to the same period in the prior fiscal year.

Interest expense totaled approximately $2.8 million and $2.0 million for the fiscal years ended July 31, 2006 and 2005, respectively. The Company incurred interest expense related to the Company s stadium obligation of approximately $0.7 million and $0.8 million in 2006 and 2005, respectively. In both years, the remaining interest expense related primarily to outstanding borrowings on a revolving bank credit facility. The interest expense on the revolving line of credit increased due to an increase in the borrowing rate as well as an increase in the average outstanding balance maintained during the year.

Other Gains (losses), net:

Other gains (losses), net, totaled a gain of $28.5 million for the fiscal year ended July 31, 2006 as compared to a gain of $2.6 million for the prior fiscal year. During the fiscal year ended July 31, 2006, the Company recorded a gain of approximately $2.7 million related to the sale of a building in Europe. In addition, the Company recorded a gain of approximately $19.4 million as a result of the acquisition of WebCT Inc. by a third party, a gain of approximately $3.2 million as a result of the acquisition of Realm Business Solutions, Inc. by a third party and a gain of approximately $4.6 million as a result of the acquisition of Alibris, Inc. by a third party. Web CT Inc., Realm Business Solutions Inc. and Alibris, Inc. were all @Ventures portfolio companies. The Company also recorded an adjustment of approximately $0.5 million to increase a previously recorded gain as a result of the acquisition of Molecular Inc. (an @Ventures portfolio company), due to the release of funds held in escrow. The Company also incurred foreign exchange losses of approximately $2.3 million during the fiscal year ended July 31, 2006, primarily related to unhedged foreign currency exposures in Asia.

Other gains (losses) net, totaled $2.6 million for the fiscal year ended July 31, 2005. During the fiscal year ended July 31, 2005, the Company realized gains totaling approximately $5.7 million, of which approximately $5.1 million related to the acquisition by third parties of two @Ventures portfolio companies, Molecular and Classmates Online, Inc. These gains were partially offset by foreign exchange losses during the year of approximately $3.1 million, primarily related to unhedged foreign currency exposures, primarily in Asia.

Equity in losses of affiliates, net:

Equity in losses of affiliates, net, resulted from the Company s minority ownership in certain investments that are accounted for under the equity method. Under the equity method of accounting, the Company s proportionate share of each affiliate s income (losses) is included in equity in income (losses) of affiliates. Equity in losses of affiliates was approximately $0.1 million for the fiscal year ended July 31, 2006 compared to equity in losses of affiliates of $1.4 million for the prior fiscal year, primarily as a result of a decrease in net losses recognized by certain of the affiliate companies. Included in equity in losses of affiliates, net, for the fiscal years ended July 31, 2006 and 2005 are impairment charges of approximately $0.6 million and $0.4 million, respectively, for other than temporary declines in the carrying value of certain investments in affiliates.

Income Tax Expense/(Benefit):

During the fiscal year ended July 31, 2006, the Company recorded income tax expense of approximately $3.8 million, as compared to an income tax benefit of $19.9 million for the prior fiscal year. Included in the tax provision were income tax benefits of approximately $2.0 million and $24.7 million in fiscal 2006 and 2005, respectively, for the reduction in the Company s estimate of certain tax liabilities that had been included in accrued income taxes on the Company s balance sheets.

For the year ended July 31, 2006, the Company s U.S. taxable income has been offset by net operating loss carryovers from prior years. For the year ended July 31, 2005, no income tax benefit was recorded for losses generated in the U.S. due to the uncertainty of realizing such benefits and the fact that the Company has fully utilized its tax loss carryback benefits. The Company continues to maintain a full valuation allowance against its deferred tax asset in the U.S. and certain of its foreign subsidiaries due to the uncertainty of realizing such benefits. The Company provides income tax expense related to federal alternative minimum tax, state taxes and foreign taxes.

Discontinued Operations:

For the year ended July 31, 2006, the Company recorded a loss from discontinued operations of approximately $13.7 million primarily related to the sale of the Company s marketing distribution services business, SalesLink, to Automatic Data Processing, Inc. (ADP). This business had previously been included within the Company s Americas reporting segment. During the second quarter ended January 31, 2006, CMGI s Board of Directors authorized the divestiture of SalesLink, and at that time, management determined that its planned divestiture of SalesLink met the criteria for discontinued operations accounting in accordance with the provisions of Statement of Financial Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets . As such, the operating results of SalesLink have been segregated from continuing operations and have been reported as discontinued operations in the accompanying balance sheets, statements of operations and cash flows for all periods presented. SalesLink s business was sold in June 2006. See note 4 to the Consolidated Financial Statements. The $13.7 million loss from discontinued operations is comprised of revenues of $13.3 million, expenses of $14.6 million, a charge of $5.6 for unutililized facility and equipment leases, a non-cash charge of $2.7 million for the write down of goodwill, and a $1.5 million loss on sale of SalesLink to

ADP.

The Company also recorded a $2.6 million impairment charge to a previously recorded loss on sale of Tallan for an other than temporary decline in the carrying value of a note receivable and warrant.

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The Company does not expect any future residual costs related to discontinued operations to be significant.

Fiscal 2005 compared to Fiscal 2004

In the discussion below of the Company s results of operations, the use of the terms organic growth or organic decline are in reference to the Company s supply chain business pre-acquisition of Modus.

Net Revenue:

	2005	As a % of Total Net Revenue	2004	As a % of Total Net Revenue	$ Change	% Change
			($ in thousands)			
eBusiness and Fulfillment						
Americas	$ 433,147	41%	$ 194,623	51%	$ 238,524	123%
Asia	212,595	20%	33,053	9%	179,542	543%
Europe	407,681	39%	153,025	40%	254,656	166%
Total eBusiness and Fulfillment	1,053,423	100%	380,701	100%	672,722	177%
Other	84		614	4%	(530)	(86)%
Total	$ 1,053,507	100%	$ 381,315	100%	$ 672,192	176%

The year over year increase in net revenue for the fiscal year ended July 31, 2005, as compared to the prior year, was attributable to the Company s acquisition of Modus on August 2, 2004.

For the fiscal year ended July 31, 2005, the Company s Modus acquisition contributed approximately 98%, 100% and 99% of the year over year revenue growth within the Americas, Asia, and Europe segments, respectively. Additionally, the Americas region realized 3% year over year organic growth, primarily from $11.2 million of incremental volumes from new U.S.-based supply chain management client programs awarded during the third quarter of fiscal 2004. Within the Europe region, year over year organic revenue growth of 2% was realized as a result of stronger overall demand for our clients products in the region. Within the Asia region, year over year organic revenue declined by approximately $21.5 million primarily as a result of reduced order volumes attributable to the loss of a supply chain management program.

During the fiscal years ended July 31, 2005 and 2004, one client, Hewlett-Packard, accounted for approximately 36% and 74% of the Company s consolidated net revenues, respectively.

Cost of Revenue:

	2005	As a % of Segment Net	2004	As a % of Segment Net	$ Change	% Change

	Revenue		Revenue (in thousands)			
eBusiness and Fulfillment						
Americas	$ 397,225	92%	$ 184,285	95%	$ 212,940	116%
Asia	161,184	76%	31,364	95%	129,820	414%
Europe	374,654	92%	144,340	94%	230,314	160%
Total eBusiness and Fulfillment	933,063	89%	359,989	95%	573,074	159%
Total	$ 933,063	89%	$ 359,989	94%	$ 573,074	159%

Cost of revenue consists primarily of expenses related to the cost of products purchased for sale or distribution as well as salaries and benefit expenses, consulting and contract labor costs, fulfillment and shipping costs, and applicable facilities costs. The Company s cost of revenue for the fiscal year ended July 31, 2005 increased as compared to the prior year, as a result of the Company s acquisition of Modus. In addition, the Modus acquisition also contributed 100% of the increase in gross margins, which increased from 6% to 11%, year over year.

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Cost of revenue and gross margins within the Americas, Asia, and Europe segments increased for the fiscal year ended July 31, 2005, as compared to the prior year, primarily as a result of the cost of revenue and gross margin contributions from the Modus acquisition. Of the year over year cost of revenue increases within the Americas, Asia, and Europe segments, approximately 95%, 100% and 99%, respectively, of the increases were attributable to the Company s Modus acquisition. Additionally, the Americas region realized a 5% year over year organic increase in cost of revenue, partially as a result of 3% organic growth in revenue during the same period. This organic increase in cost of revenue, which outpaced the organic increase in revenue growth by 2%, resulted in a $5.1 million decline in gross margin dollars, year over year. In fiscal year 2005, the Company realized a shift in the composition of products distributed for certain of its clients as compared to the prior year. This shift in distributed product types yielded lower gross margins. In addition, start up costs associated with two new client programs also negatively impacted gross margin in fiscal year 2005. In Asia, organic cost of revenue was down approximately $20.5 million year over year due to the loss of a supply chain management program as noted in the revenue discussion above. The loss of this program in Asia resulted in a loss of approximately $1.0 million in gross margin year over year. In the Europe region, organic cost of revenues increased 2% year over year primarily as a result of a 2% organic growth in revenue during the same period. This organic increase in cost of revenue, which approximated the organic increase in revenue growth, resulted in a $0.2 million increase in gross margin dollars, year over year. The Company s gross margin percentages within the Americas, Asia and Europe regions were approximately 8%, 24% and 8%, respectively, for the fiscal year ended July 31, 2005, as compared to 5%, 5% and 6%, respectively, for the same period of the prior year. While gross margin percentages increased in each of our operating segments, these year over year improvements were partially offset by approximately $13.4 million of price reductions related to contract renegotiations with certain clients. Of these price reductions, approximately $2.0 million, $9.0 million and $2.4 million were realized in the Americas, Asia and Europe regions, respectively. These price reductions reduced fiscal year 2005 gross margin percentages by 1%, 3% and 1% in the Americas, Asia and Europe segments, respectively.

Selling Expenses:

	2005	**As a % of Segment Net Revenue**	**2004**	**As a % of Segment Net Revenue**	**$ Change**	**% Change**
			(in thousands)			
eBusiness and Fulfillment						
Americas	$ 7,019	2%	$ 2,152	1%	$ 4,867	226%
Asia	6,874	3%	289	1%	6,585	2,279%
Europe	7,688	2%	1,991	1%	5,697	286%
Total eBusiness and Fulfillment	21,581	2%	4,432	1%	17,149	387%
Other	(3)	(4)%	26	4%	(29)	(112