

2nd Quarter Fiscal 2005 Report

Prepared in Accordance with Canadian Generally Accepted Accounting Principles

Dear Shareholder,

The momentum continued in our second quarter as we added some key new accounts and grew our top line. Here are a few highlights:

- We signed eight new accounts.
- Revenues in the second quarter of fiscal 2005 increased 33% to \$5.5M compared to the second quarter of fiscal 2004 of \$4.1M.
- Our success in Europe continued with new projects beginning in Spain and Portugal.
- Although Income from Operations declined significantly, the bulk of the decline was due to a combination of the exchange swing and the change in GAAP requirements regarding stock based compensation.
- Cash balance rose to \$9.9M, up from \$9.2M at the end of the prior reporting quarter.

Our growth was sustained as we continued to close significant new business. We reached an agreement with a large multi-national pool products distributor, by the name of SCP Pools, to implement our *EliteSeries* software in Spain and Portugal. We now have implementations underway in Germany, France, Spain, Portugal, and the UK, in addition to our ongoing operations here in North America. There seems to be a real opportunity for us in Europe as manufacturing is pushed off shore and large multi-national distributors set up operations there. With Europe historically being more of a manufacturing economy, the domestic software companies have little distribution focus, which is opening up opportunity for us.

Other new accounts included a leading medical/surgical distributor in Quebec, the largest plumbing distributor in the Southwestern U.S. with nine branch offices, a distributor of plush toys, a distributor of home accents, a rug importer, and a distributor of fine quality furniture.

We have one of the highest successful implementation rates in the industry, and this continued with go-lives in quite a number of accounts covering industries such as: pharmaceutical, medical/surgical, healthcare services, golf products, books, pet food, fabrics and home furnishings, floral wholesale, and handmade tableware.

In our Transportation Systems division, our go-lives covered industries such as: automotive components; electronic components; dental, medical, and veterinary supplies; sportswear; educational products; hardware; publishing; safety footwear; and document management.

We have maintained a healthy gross margin with a continued focus on costs and streamlining business processes across the three (3) divisions. At the same time, the dramatic shift in exchange rate has had a significant impact on our results. During the second quarter of fiscal 2005, the strengthening of the Canadian dollar, compared to the corresponding quarter of last year, had an unfavorable impact of approximately \$86,000 on income from operations in addition to the loss on exchange of \$400,000. Although we do hedge to the extent that we can, hedging beyond both contracted and expected cash flows must be reported as speculative and should be avoided. We believe the problem will be resolved over the coming months as our cost controls and revenue trends continue to have a positive impact on our numbers.

Our stock price continues to be a concern for us, and while small cap tech stocks are still generally low, we believe that the right long term cure for a low stock price lies in the fundamentals of growth and earnings. We have made some progress in these areas but have more work to do. As we continue to make this our focus, we believe it will payoff for our shareholders.

Yours truly,



Peter Brereton
President and Co-CEO

Management's Discussion and Analysis of Financial Condition and Results of Operations dated November 18, 2004

The following discussion and analysis should be read in conjunction with the Consolidated Financial Statements and Notes thereto, which are included in this document. This discussion and analysis should also be read in conjunction with the annual report for fiscal year 2004. The Company's second quarter for fiscal year 2005 ended on October 31, 2004.

These interim unaudited consolidated financial statements have not been reviewed by the Company's auditors.

The Company's consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles, and all financial data derived therefrom in this interim report are expressed in U.S. dollars. The Company's reporting currency is the U.S. dollar; and the functional currency is the Canadian dollar. Accordingly, the consolidated financial statements for the three and six-month periods ended October 31, 2004 and October 31, 2003 are translated into U.S. dollars using the current rate method. All gains and losses resulting from the translation of the consolidated financial statements into U.S. dollars are reflected in the cumulative translation adjustment in shareholders' equity.

In addition, the consolidated financial statements include a reconciliation of the specific measurement differences between Canadian and United States generally accepted accounting principles as they relate to the Company.

Business Combination

On December 31, 2003, the Company acquired 100% of the issued and outstanding shares of PointForce Inc. ("PointForce"), a company which develops, markets, and sells Supply Chain Management ("SCM") software for the giftware distribution, office products distribution, and high-growth import-to-retail distribution market segments. PointForce was wound-up into TECSYS Inc. on January 1, 2004 and the results of its operations have been included in the consolidated financial statements commencing January 1, 2004.

Results of Operations

Three and six months ended October 31, 2004 compared to three and six months ended October 31, 2003

Revenue

For the three months ended October 31, 2004 total revenue increased by \$1.3 million or 33% to \$5.5 million compared to \$4.1 for the same period of fiscal 2004. PointForce accounted for the revenue increase during the second quarter of fiscal 2005 amounting to \$1.3 million.

Products revenue remained flat at \$1.8 million in the second quarter of fiscal 2005 compared to the same period in the previous fiscal year. PointForce contributed \$263,000 of products revenue. Excluding PointForce, products revenue decreased \$249,000 or 14% due exclusively to decreases of third-party products revenue. During the second quarter of fiscal 2004, there was a significant shipment of RF equipment to one of our major accounts for \$316,000.

Services revenue increased 59% or \$1.3 million to \$3.4 million during the second quarter of fiscal 2005 compared to \$2.2 million for the same fiscal period last year. PointForce contributed \$1.0 million in services revenue during the second quarter of fiscal 2005. Excluding PointForce, services revenues increased by \$242,000 or 11% in comparison to the same three-month period last year representing primarily increased activity for consulting in some key account implementations and support, partly offset by lower product adaptations.

As a percentage of total revenue, products accounted for 33% and services 63% in the second quarter of fiscal 2005 compared to 44% and 52%, respectively, in the second quarter of fiscal 2004. The increased services percentage of revenue is strongly influenced by the PointForce revenue mix, which was 20% for products and 78% for services.

The Canadian dollar has strengthened approximately 6% vis-à-vis the U.S. dollar for the second quarter of fiscal 2005 as compared to the same period in fiscal 2004. The U.S. dollar to Canadian dollar exchange rates for the three-month period ended October 31, 2004 have averaged 1.2822 in comparison to 1.3602 for same period last year. Consequently, excluding PointForce, the strengthening Canadian dollar exchange rate impact has affected the reported revenues favorably by approximately \$70,000 in the second quarter of fiscal 2005 in comparison to the same period last year.

During the first half of fiscal 2005 total revenue increased by \$2.9 million or 37% to \$10.8 million compared to \$7.9 million in the first half of fiscal 2004. PointForce contributed for most of the revenue increase during the first half of fiscal 2005 amounting to \$2.8 million.

Products revenue increased slightly by 5% or \$171,000 to \$3.6 million during the first half of fiscal 2005 compared to the same period in the previous fiscal year. PointForce contributed \$660,000 of products revenue. Excluding PointForce, products revenue decreased \$489,000 or 14% due exclusively to decreases of third-party products revenue amounting to \$637,000 while proprietary license revenues increased \$148,000. In the first half of fiscal 2004, there were a few large shipments of third-party products to a few significant customers.

Services revenue increased 66% or \$2.7 million to \$6.9 million during the first half of fiscal 2005 compared to \$4.1 million for the same fiscal period last year. PointForce contributed \$2.1 million in services revenue during the first half of fiscal 2005. Excluding PointForce, services revenues increased by \$643,000 or 16% in comparison to the same six-month period last year representing increased activity in all service areas including consulting, product adaptations, and support.

As a percentage of total revenue, products accounted for 33% and services 63% in the first half of fiscal 2005 compared to 43% and 52%, respectively, in the first half of fiscal 2004. The increased services percentage of revenue is strongly influenced by the PointForce revenue mix, which was 24% for products and 74% for services for the first six months, as well as the reduced activity in third-party products revenue.

The Canadian dollar has strengthened approximately 3.6% vis-à-vis the U.S. dollar for the first half of fiscal 2005 as compared to the same period in fiscal 2004. The U.S. dollar to Canadian dollar exchange rates for the six-month period ended October 31, 2004 have averaged 1.3174 in comparison to 1.3665 for same period last year. Consequently, excluding PointForce, the strengthening Canadian dollar exchange rate impact has affected the reported revenues favorably by approximately \$87,000 in the first half of fiscal 2005 in comparison to the same period last year.

Cost of Revenue

Total cost of revenue in the second quarter of fiscal 2005 was \$2.6 million representing an increase of \$731,000 or 38% compared to \$1.9 million for the same period last year. PointForce's cost of revenue for the three-month period ended October 31, 2004 accounted for \$648,000 of the increase.

Services costs increased by \$563,000 or 47% to \$1.8 million for the second quarter of fiscal 2005 compared to \$1.2 million for the comparable period of the previous fiscal year, reflecting primarily the impacts of the PointForce addition to the TECSYS group. Excluding PointForce and the reduction in tax credits, gross services expenses decreased slightly by 3% or \$46,000 for the second quarter of fiscal 2005 compared to the previous fiscal year primarily as a result of a slight reduction in average headcount. The total cost of services also includes multimedia tax credits of \$120,000 for the second quarter of fiscal 2005 compared to \$137,000 for the same period in the previous fiscal year. Multimedia tax credit rules are being enforced more stringently and hence the Company is taking a more conservative approach in accruing for these credits. The amounts accrued are consistent with the Company's budget.

Due to the strengthened Canadian dollar in the second quarter of fiscal 2005 in comparison to the same period in fiscal 2004, excluding PointForce, service expenses, net of multimedia tax credits, have been affected unfavorably by approximately \$56,000.

The cost of third-party products increased by \$108,000 or 20% to \$660,000 for the second quarter of fiscal 2005 in comparison to the same three-month period for the previous fiscal year, with PointForce accounting for about one-half of the increase. Excluding the PointForce impact, fiscal 2005 costs increased 10% or \$53,000 for the second quarter of fiscal 2005 in comparison to fiscal 2004.

Total cost of revenue in the first half of fiscal 2005 was \$5.1 million representing an increase of \$1.5 million or 42% compared to \$3.6 million for the same period last year. PointForce's cost of revenue for the six-month period ended October 31, 2004 accounted for \$1.4 million or 95% of the increase. This is consistent with the revenue increase, where PointForce accounted for 96% of the total increase.

Services costs increased by \$1.2 million or 51% to \$3.5 million for the first half of fiscal 2005 compared to \$2.3 million for the comparable period of the previous fiscal year, reflecting primarily the impacts of the PointForce addition to the TECSYS group. Excluding PointForce, services expenses increased slightly by 2% or \$53,000 for the first half of fiscal 2005 compared to the previous fiscal year primarily as a result of the strengthening Canadian dollar adverse effect of approximately \$71,000 offset by a slight reduction in average headcount. The total cost of services also includes multimedia tax credits of \$252,000 for the first half of fiscal 2005 compared to \$303,000 for the same period in the previous fiscal year. Multimedia tax credit rules are being enforced more stringently and hence the Company is taking a more conservative approach in accruing for these credits. The amounts accrued are in-line with the Company's budget.

The cost of third-party products increased by \$274,000 or 31% to \$1.2 million for the first half of fiscal 2005 in comparison to the same six-month period for the previous fiscal year, with PointForce accounting for 64% of the increase. Excluding the PointForce impact, fiscal 2005 costs increased 11% or \$99,000 for the first half of fiscal 2005 in comparison to fiscal 2004.

Gross Margin

The gross margin increased by \$617,000 or 28% to \$2.9 million for the second quarter of fiscal 2005 in comparison to \$2.2 million for the same fiscal period last year. PointForce contributed \$648,000 to the increased margin. Total gross margin percentage in the second quarter of fiscal 2005 was 52% compared to 54% in the same period of fiscal 2004. This decline in overall gross margin is due to a higher ratio of revenue derived from services, 63% in the second quarter of fiscal 2005 in comparison to 52% in the second quarter of fiscal 2004, which carries a lower margin compared to products as well as lower product margins, which were 64% in the second quarter of fiscal 2005 in comparison to 70% for the same three month period in fiscal 2004.

Services gross margin was considerably higher at 49% in the second quarter of fiscal 2005 compared to 44% in the same period last year. Excluding PointForce, the services gross margin increased to 51% in comparison to 44% for the same three-month period last year as a result of the increase in the consultation and support revenue despite the fact that the cost base decreased slightly due to a small reduction in the number of average resources. PointForce's service margin came in at 43% for the second quarter of fiscal 2005. Product margins decreased to 64% for the second quarter of fiscal 2005 compared to 70% for the same fiscal period last year due primarily to higher price pressure on third-party products.

The gross margin increased by \$1.4 million or 33% to \$5.8 million for the first half of fiscal 2005 in comparison to \$4.3 million for the same fiscal period last year. PointForce contributed 100% of the increased margin. Total gross margin percentage in the first half of fiscal 2005 was 53% compared to 55% in the same period of fiscal 2004. This decline in overall gross margin percentage is due to a higher ratio of revenue derived from services, 63% in the first half of fiscal 2005 in comparison to 52% in the first half of fiscal 2004, which carries a lower margin compared to products as well as lower product margins, which were 68% in the first half of fiscal 2005 in comparison to 74% for the same six-month period in fiscal 2004.

Services gross margin was considerably higher at 49% in the first half of fiscal 2005 compared to 44% in the same period last year. Excluding PointForce, the services gross margin increased to 50% in comparison to 44% for the same six-month period last year as a result of the increased revenues in all service areas of 16% while costs increased at the lower rate of 2% due primarily to the adverse effect of the strengthening Canadian dollar. PointForce's service margin came in at 45% for the first half of fiscal 2005. Product margins decreased to 68% for the first half of fiscal 2005 compared to 74% for the same fiscal period last year due primarily to price pressures on third-party products.

Operating Expenses

Total operating expenses increased by \$819,000 or 41% to \$2.8 million in the second quarter of fiscal 2005 compared to \$2.0 million in the second quarter of fiscal 2004. PointForce's operating expenses for the second quarter of fiscal 2005 amounted to \$666,000. The Company's adoption of the new stock-based compensation standards without restatement (see note 1) effective May 1, 2004 account for an additional \$62,000 of expenses in the second quarter of fiscal 2005. Total operating expenses, excluding newly acquired Pointforce and the stock-based compensation expense, increased by \$91,000 or 5% in the second quarter of fiscal 2005 compared to the same period in fiscal 2004.

Excluding PointForce and the stock-based compensation expense, the major variances for the operating expense increase in the second quarter of fiscal 2005 in comparison to the second quarter of fiscal 2004 are a \$115,000 unfavorable variance due to less tax credits applicable to the research and development activities offset by \$29,000 of favorable variances for the amortization of property, plant, and equipment and intangible assets. Approximately \$60,000 of the unfavorable variance for the tax credits is due to an adjustment for a prior year following a government audit.

Due to the strengthened Canadian dollar in the second quarter of fiscal 2005 in comparison to the same period in fiscal 2004, excluding PointForce and the stock-based compensation expense, operating expenses have been affected unfavorably by approximately \$100,000.

Total operating expenses increased by \$1.6 million or 39% to \$5.6 million in the first half of fiscal 2005 compared to \$4.0 million in the first half of fiscal 2004. PointForce's operating expenses for the first half of fiscal 2005 amounted to \$1.4 million. The Company's adoption of the new stock-based compensation standards without restatement (see note 1) effective May 1, 2004 account for an additional \$113,000 of expenses in the first half of fiscal 2005. Total operating expenses, excluding newly acquired Pointforce and the stock-based compensation expense, increased by \$104,000 or 3% in the first half of fiscal 2005 compared to the same period in fiscal 2004. The major variances for this increase are due primarily to an unfavorable variance of \$186,000 for tax credits offset by \$71,000 of favorable variances for the amortization of property, plant and equipment and intangible assets.

The decrease of \$186,000 of tax credits for the first six months of fiscal 2005 in comparison to the same period of fiscal 2004 is due mainly to a \$60,000 adjustment relating to a prior year as a result of a government audit. Additionally, the fiscal 2005 reduced credits reflect the legislative changes reducing research and development investment tax credit rates from 40% to 35% of the first \$2 million of eligible expenditures and the amendments to tax legislation which specified that an expenditure related to an activity for a given period may not give rise to more than one refundable tax credit.

Due to the strengthened Canadian dollar in the first half of fiscal 2005 in comparison to the same period in fiscal 2004, excluding PointForce and the stock-based compensation expense, operating expenses have been affected unfavorably by approximately \$133,000.

Other Income and Expenses

Interest income decreased 40% to \$48,000 in the second quarter of fiscal 2005 compared to \$80,000 for the same period in the previous fiscal year and also decreased 45% to \$91,000 for the first six months of fiscal 2005 in comparison to \$165,000 for the first half of fiscal 2004 primarily due to lower short-term interest rates and less funds available for investment principally as a result of the purchase of PointForce and the repayment of a term loan and capital lease obligations.

Interest expense decreased 62% to \$8,000 in the second quarter of fiscal 2005 compared to \$21,000 for the same period last year and also decreased 63% to \$17,000 for the first half of fiscal 2004 compared to \$46,000 for the same period of fiscal 2004. The reduction in interest expense is attributable to the reduction of long-term debt including the repayment of a term loan and capital lease obligations during the fiscal 2004 year.

During the second quarter of fiscal 2005, the Company recorded an exchange loss of \$400,000 compared to an exchange loss of \$281,000 for the same period in the previous fiscal year. For the first half of fiscal 2005, exchange losses amounted to \$433,000 compared to \$412,000 for the first six months of fiscal 2004. The exchange loss arises because the Company carries net monetary assets, primarily cash and accounts receivable, denominated in U.S. dollars. The net U.S. monetary assets are devalued due to the strengthened Canadian dollar vis-à-vis the U.S. dollar. The exchange rate at July 31, 2004, the beginning of the quarter, was \$1 US = \$1.3292 CA. The exchange rate at October 31, 2004 was \$1 US = \$1.2207 CA representing an 8.2% devaluation of U.S. monetary assets for the quarter. The exchange rate at July 31, 2003 was \$1 US = \$1.4073 CA and at October 31, 2003 the rate was \$1 US = \$1.3197 CA representing a 6.2% devaluation of U.S. monetary assets in the second quarter of the last fiscal year. In the first half of the current fiscal year U.S. monetary assets have been devalued 10.9% as the rate on April 30, 2004, the beginning of the current fiscal year was \$1 US = \$1.3707 CA in comparison to a 7.9% devaluation for the first half of fiscal 2004 as the rate on April 30, 2003 was \$1 US = \$1.4335 CA.

During the second quarter of fiscal 2005, the Company protected a portion of its net U.S. monetary assets by means of a forward exchange contract selling \$1 million U.S. dollars forward at an average rate of \$1.2958. The contract matured before the end of the quarter. There were no foreign exchange contracts outstanding at the end of the quarter. The hedging strategy in the second quarter of fiscal 2005 resulted in reduced exchange losses for US\$60,000. The Company followed a similar strategy of selling \$1.5 million U.S. dollars in the first quarter of the current fiscal year yielding cumulative reduced exchange losses of US\$108,000 for the six-month period. No hedging strategy or foreign exchange contracts were in effect in the first half of fiscal 2004.

Subsequent to the current quarter ended October 31, 2004, the Company undertook another foreign exchange contract to sell \$1.5 million U.S. dollars forward at a rate of 1.2042 on January 31, 2005.

The consolidated financial statements for the three and six-month periods ended October 31, 2004 and October 31, 2003 are translated into U.S. dollars using the current rate method. All gains and losses resulting from the translation of the Canadian dollar consolidated financial statements into U.S. dollars are reflected in the cumulative translation adjustment in shareholders' equity.

The Company has recorded increases in the cumulative translation adjustment (CTA) account within the shareholder's equity of \$1.2 million for the second quarter of fiscal 2005 (\$1.6 million for the first half of fiscal 2005) compared to an increase of \$820,000 for the second quarter of fiscal 2004 (\$1.1 million for the first half of fiscal 2004). The increases to CTA account represent exchange gains arising on the translation of the Canadian dollar financial statements into U.S. dollar financial statements where such exchange gains are posted directly into the shareholder's equity section rather than flowing through the statement of operations.

Net Earnings

The Company recorded a net loss of \$316,000 or \$0.02 per share in the second quarter of fiscal 2005 compared to net earnings of \$24,000 or \$0.00 per share for the same period last year. For the six month period ended October 31, 2004, the Company recorded a net loss of \$180,000 or \$0.01 per share in comparison to net earnings of \$34,000 or \$0.00 per share for the same six-month period in the previous fiscal year

Note 5 to the financial statements reflects that there are no material differences between the Company's reported net earnings (loss) and basic and diluted net earnings (loss) per share under Canadian GAAP as compared to U.S. GAAP for the three and six-month periods ended October 31, 2004 and 2003. However, under U.S. GAAP, the cumulative translation adjustment (CTA) is an integral part of arriving at the comprehensive income. The comprehensive income for the first half of fiscal 2005 under U.S. GAAP was \$1.4 million compared to the comprehensive income of \$1.1 million for the corresponding period in fiscal 2004 (\$904,000 comprehensive income for the second quarter of fiscal 2005 compared to \$844,000 comprehensive income for the second quarter of fiscal 2004).

Liquidity and Capital Resources

As of October 31, 2004, current assets totaled \$16 million compared to \$14.9 million at the end of fiscal 2004. Cash, restricted cash equivalents, and short-term and other investment securities increased to \$9.9 million compared to \$8.8 million as at April 30, 2004. Accounts receivable totaled \$4.7 million at the end of October 31, 2004, basically unchanged from the amount at the end of fiscal 2004. The Company's DSO (days sales outstanding) remained flat at 78 days at the end of the second quarter of fiscal 2005 in comparison to the end of fiscal 2004.

Current liabilities as at October 31, 2004 totaled \$5.5 million compared to \$5.7 million at the end of fiscal 2004. Working capital increased to \$10.5 million at the end of the second quarter of fiscal 2005 compared to \$9.2 million at the end of fiscal year 2004.

During the first half of fiscal 2005, operating activities generated funds of \$74,000 compared to \$441,000 for the same period last year. During the first half of fiscal 2005, results in operating activities generated \$438,000 and were partially offset by used funds to increase net non-cash working capital by \$364,000. During the first half of fiscal 2004, positive results in operating activities generated \$575,000 and were partially offset by used funds to increase net non-cash working capital by \$134,000.

The Company believes that funds on hand at October 31, 2004, together with short term investments and cash flow from operations will be sufficient to meet its needs for working capital, R&D, capital expenditures and debt repayment for at least the next twelve months.

Financing activities used funds of \$98,000 and \$953,000 respectively for the first half of fiscal 2005 and 2004. The repayment of long-term debt and capital lease obligations amounted to \$95,000 in the first half of fiscal 2005 compared to \$618,000 for the comparable period in fiscal 2004. Additionally, during the first half of fiscal 2004, the Company purchased 320,100 of its outstanding common shares for cancellation at an average price of \$1.04 per share under a Normal Course Issuer Bid (NCIB). The total cost related to purchasing these shares, including other related costs, was \$335,000. No shares have been repurchased in the first half of fiscal 2005, however the Company has incurred \$3,000 of fees to renew its NCIB. As per note 24 of the 2004 annual report, the Company may purchase common shares under the NCIB, if it considers it advisable, at any time, and from time to time, for one year from the date of filing.

During the first half of fiscal 2005, investing activities used funds amounting to \$1.5 million as compared to \$184,000 for the first half of fiscal 2004. The Company used funds of \$1.8 million and \$17,000 respectively for the first half of fiscal 2005 and 2004 by increases in short term investments. Funds of \$102,000 and \$167,000 were used for the first half of fiscal 2005 and 2004 respectively for the acquisition of property, plant, and equipment, and computer software for internal use (intangible assets). Additionally, in the first quarter of fiscal 2005, the company received funds of \$368,000 representing the purchase price adjustment from the former PointForce shareholders pursuant to the acquisition of PointForce.

Strategically, the Company will continue to consider growth opportunities through acquisition. Funding for these potential acquisitions will be determined as the opportunities and circumstances are identified.

Change in Accounting Policy

Stock-based compensation and other stock-based payments

The Company maintains a stock-based compensation plan, which is described in note 11(d) in the audited financial statements for the year ended April 30, 2004. Effective May 1, 2004, the Company has adopted the fair value based method of accounting for stock options and warrants granted to employees and directors and has elected to apply the new standard retroactively without restatement as prescribed by the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3870, Stock-based Compensation and Other Stock-based Payments. Under the fair value based method, compensation cost is measured at fair value at the date of grant and is

expensed over the award's vesting period with a corresponding credit to contributed surplus. The stock-based compensation expense is recorded in the financial statements for the three and six months ended October 31, 2004. Accordingly, for the three and six-month periods ended October 31, 2003, the Company provides only pro forma disclosures of net earnings (loss) and net earnings (loss) per common share as if the fair value based method of accounting had been used to account for stock options and warrants granted to employees and directors.

No compensation cost is recognized when shares are issued to employees. Any consideration received from plan participants is credited to capital stock. Any stock-based compensation costs related to awards to individuals other than employees and directors are accounted for at fair value.

The change in accounting for the stock-based compensation has resulted in an adjustment of the opening balance of the consolidated statement of deficit for the current fiscal year of \$4.8 million, with a corresponding credit to contributed surplus, reflecting the prior periods' cost of options and warrants granted since inception, which occurred in the 1998 fiscal year. Additionally, the capital stock account has been increased by \$353,000 with a corresponding reduction in contributed surplus representing the value of compensation cost associated with the options exercised since inception.

Critical Accounting Policies

The Company's critical accounting policies are those that it believes are the most important in determining its financial condition and results. A summary of the Company's significant accounting policies, including the critical accounting policies discussed below, is set out in the notes to the consolidated financial statements in the annual report for year ended April 30, 2004.

Use of estimates

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenue and expenses during the reporting periods.

As the Company's software implementation period may typically span from six to twelve months, the most significant area requiring judgement and estimation is revenue recognition relating to multiple element arrangements, where the resulting revenue recognition per element and the related timing must be assessed in relation to contract terms, Statement of Position ("SOP") 97-2 criteria, future services, and other criteria as discussed later. The estimates and assumptions are based on past experience and other factors that the Company considers reasonable. As this involves varying degrees of judgement and uncertainty, actual results could differ from those estimates.

The Company maintains an allowance for doubtful accounts at an amount estimated to be sufficient to provide adequate protection against losses resulting from collecting less than full payment on its receivables. Individual overdue accounts are reviewed and allowance adjustments are recorded when determined necessary to state receivables at the realizable value. If the financial condition of customers deteriorate resulting in their diminished ability or willingness to make payment, additional provisions for doubtful accounts are recorded. Considerable judgement is required to assess the realizable value of the receivables including the probability of collection and the current creditworthiness of each customer. As this involves varying degrees of judgement and uncertainty, actual results could differ from those estimates.

The company accrues refundable investment tax credit benefits related to qualifying activities, including research and development projects, as well as supplementary tax credits (multimedia tax credits). Considerable judgement is required to assess the various criteria of whether activities qualify. As these activities are audited periodically, the actual results attributable to a fiscal period may differ from the accounting estimates posted.

Goodwill represents the excess of the purchase price of businesses acquired over the fair value of the underlying net identifiable assets acquired or liabilities assumed. Goodwill related to business combinations initiated or completed prior to July 1, 2001 was amortized on a straight-line basis over the estimated useful life of five years. Following the adoption of the recommendations of the CICA Handbook Section 3062 on May 1, 2002, goodwill is not amortized, but rather is evaluated for impairment annually, or when events or changed circumstances indicate that an impairment may have occurred. In connection with the goodwill impairment test, if the carrying value of the Company's reporting unit to which goodwill relates exceeds its estimated fair value, the goodwill related to that reporting unit is tested for impairment. If the carrying value of such goodwill is determined to be in excess of its fair value, an impairment loss is recognized in the amount of the excess of the carrying value over the fair value. The goodwill impairment test entails the use of a number of estimates including future cash flows and involving varying degrees of judgement and uncertainty. Actual results will differ from those estimates.

The Company assesses the carrying value of its long-lived assets, which include property, plant and equipment and definite-life intangible assets, for future recoverability when events or changed circumstances indicate that the carrying value may not be recoverable. An impairment loss is recognized if the carrying value of a long-lived asset exceeds the sum of the estimated undiscounted future cash flows expected from its use. The amount of impairment loss, if any, is determined as the excess of the carrying value of the assets over their fair value. The long-lived assets impairment test entails the use of a number of estimates including future cash flows and involving varying degrees of judgement and uncertainty. Actual results will differ from those estimates.

Revenue Recognition

The Company licenses software under non-cancellable license agreements and provides services including training, installation, consulting and maintenance, which includes product support services and periodic updates. The Company recognizes revenue in accordance with the guidance set out in Statement of Position ("SOP") 97-2, "Software Revenue Recognition". Revenues generated by the Company include the following:

- **License Fees**

Revenues from licenses sold separately are recognized when a non-cancellable license agreement has been signed, the software product has been shipped, there are no uncertainties surrounding product acceptance, the fees are fixed or determinable, and collection is considered probable. Fees from multiple element arrangements are allocated to the various elements based on vendor-specific objective evidence of fair value provided that services, if any, are not essential to the functionality of the software. Revenues from licenses sold under multiple element arrangements are recognized upon shipment of the software product, provided that all of the above criteria have been met.

Where services are considered to be essential to the functionality of the software, fees from licenses and services are aggregated and recognized as revenue as the related services are performed using the percentage-of-completion method. The percentage of completion is generally determined based on the number of hours incurred to date in relation to the total expected hours of services. The cumulative impact of any revision in estimates of the percentage completed is reflected in the period in which the changes become known. Losses on such contracts in progress are recognized when known. Work in process is established for revenue based on the percentage completed in excess of progress billings as of the balance sheet date. Any excess of progress billings over revenue based on the percentage completed is deferred and included in deferred revenue. Generally, the terms of long-term contracts provide for progress billing based on completion of certain phases of work. Where acceptance criteria are tied to specific milestones, the percentage of completion up to that milestone is recognized upon acceptance.

- **Support Agreements**

Support agreements generally call for the Company to provide technical support and unspecified software updates to customers. Revenues from technical support and unspecified software update rights are recognized ratably over the term of the support agreement.

- **Consulting and Education Services**

The Company provides consulting and education services to its customers. Revenues from such services are recognized as the services are performed.

Related Party Transactions

The company has a subordinated loan for CA\$107,000 (US\$88,000) from a person related to certain shareholders, bearing interest at 12.67%. The loan is payable on the earlier of demand or on the death of the lender. The same amount was outstanding as at October 31, 2004 and October 31, 2003.

Management has compiled the unaudited interim consolidated financial information of TECSYS Inc. consisting of the interim Consolidated Balance Sheet as at October 31, 2004 and the Consolidated Statements of Deficit, Operations, and Cash Flows for the three and six-month periods ended October 31, 2004 and October 31, 2003. An accounting firm has not reviewed or audited these interim consolidated financial statements.

Consolidated Balance Sheets

Prepared in Accordance with Canadian Generally Accepted Accounting Principles

(in thousands of U.S. dollars)

	October 31, 2004 (unaudited)	April 30, 2004
Assets		
Current assets		
Cash and cash equivalents	883	2,388
Short-term investments	8,221	5,665
Accounts receivable	4,734	4,705
Other accounts receivable	80	579
Tax credits receivable	1,653	1,056
Prepaid expenses	463	501
	<u>16,034</u>	<u>14,894</u>
Restricted cash equivalents and other investments	839	747
Long-term trade account receivable	9	-
Property, plant and equipment	2,124	2,059
Intangible assets	1,215	1,215
Goodwill	1,396	1,242
	<u>21,617</u>	<u>20,157</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	3,513	3,691
Current portion of long-term debt	108	175
Deferred revenue	1,920	1,809
	<u>5,541</u>	<u>5,675</u>
Long-term debt	433	401
Other long-term liabilities	625	613
	<u>6,599</u>	<u>6,689</u>
Shareholders' Equity		
Capital stock (notes 1 and 2)	39,679	39,326
Contributed surplus (notes 1 and 3)	6,146	1,606
Cumulative translation adjustment	1,922	300
Deficit	<u>(32,729)</u>	<u>(27,764)</u>
	<u>15,018</u>	<u>13,468</u>
	<u>21,617</u>	<u>20,157</u>

Consolidated Statements of Deficit

Prepared in Accordance with Canadian Generally Accepted Accounting Principles

(in thousands of U.S. dollars)

	Six Months Ended October 31, 2004 (unaudited)	Six Months Ended October 31, 2003 (unaudited)
Balance - Beginning of period	(27,764)	(28,179)
Adjustment resulting from a change in accounting policy re: stock-based compensation (note 1)	(4,785)	-
Restated balance - Beginning of period	(32,549)	(28,179)
Net earnings (loss) for the period	(180)	34
Balance - End of period	(32,729)	(28,145)

Consolidated Statements of Operations

Prepared in Accordance with Canadian Generally Accepted Accounting Principles

(in thousands of U.S. dollars, except share and per share data)

	Three Months Ended October 31, 2004 (unaudited)	Three Months Ended October 31, 2003 (unaudited)	Six Months Ended October 31, 2004 (unaudited)	Six Months Ended October 31, 2003 (unaudited)
Revenue				
Products (note 4a)	1,838	1,824	3,591	3,420
Services	3,445	2,171	6,851	4,125
Reimbursable expenses	212	152	398	368
	<u>5,495</u>	<u>4,147</u>	<u>10,840</u>	<u>7,913</u>
Cost of revenue				
Products	660	552	1,164	890
Services (note 4b)	1,772	1,209	3,514	2,320
Reimbursable expenses	212	152	398	368
	<u>2,644</u>	<u>1,913</u>	<u>5,076</u>	<u>3,578</u>
Gross margin	<u>2,851</u>	<u>2,234</u>	<u>5,764</u>	<u>4,335</u>
Operating expenses				
Sales & marketing	1,142	893	2,320	1,758
General & administration	527	352	1,066	714
Gross research & development	933	754	1,842	1,538
Research & development tax credits	(74)	(189)	(175)	(361)
Stock-based compensation	62	-	113	-
Amortization of property, plant and equipment	140	145	270	295
Amortization of intangible assets	77	33	149	64
	<u>2,807</u>	<u>1,988</u>	<u>5,585</u>	<u>4,008</u>
Earnings from operations	44	246	179	327
Interest income	48	80	91	165
Interest expense	(8)	(21)	(17)	(46)
Foreign exchange losses	(400)	(281)	(433)	(412)
Net earnings (loss) for the period	<u>(316)</u>	<u>24</u>	<u>(180)</u>	<u>34</u>
Weighted average number of common shares outstanding				
- basic	<u>14,158,797</u>	<u>14,162,647</u>	<u>14,158,797</u>	<u>14,263,121</u>
- diluted	<u>14,158,797</u>	<u>14,252,136</u>	<u>14,158,797</u>	<u>14,311,304</u>
Basic and diluted net earnings (loss) per common share (in US dollars)	<u>\$ (0.02)</u>	<u>\$ 0.00</u>	<u>\$ (0.01)</u>	<u>\$ 0.00</u>

Consolidated Statements of Cash Flows

Prepared in Accordance with Canadian Generally Accepted Accounting Principles

(in thousands of U.S. dollars)

	Three Months Ended October 31, 2004 (unaudited)	Three Months Ended October 31, 2003 (unaudited)	Six Months Ended October 31, 2004 (unaudited)	Six Months Ended October 31, 2003 (unaudited)
Cash flows from				
Operating activities				
Net earnings (loss) for the period	(316)	24	(180)	34
Adjustments for				
Amortization of property, plant and equipment	140	145	270	295
Amortization of intangible assets	77	33	149	64
Stock-based compensation costs	62	-	113	-
Unrealized foreign exchange losses	76	115	86	182
Changes in non-cash working capital items related to operations				
Decrease in accounts receivable	335	427	627	191
Decrease (increase) in other accounts receivable	41	(32)	150	(232)
Decrease (increase) in tax credits receivable	(195)	1,338	(432)	1,032
Decrease (increase) in prepaid expenses	27	(131)	92	(3)
Decrease (increase) in long-term accounts receivable	28	-	(6)	-
Decrease in accounts payable and accrued liabilities	(110)	(492)	(617)	(566)
Increase (decrease) in deferred revenue	8	(510)	(178)	(556)
	<u>173</u>	<u>917</u>	<u>74</u>	<u>441</u>
Financing activities				
Repayment of long-term debt and capital lease obligations	(20)	(501)	(95)	(618)
Purchase of common shares for cancellation	(3)	-	(3)	(335)
	<u>(23)</u>	<u>(501)</u>	<u>(98)</u>	<u>(953)</u>
Investing activities				
Increase in short-term and other investments	(2,083)	(1,009)	(1,810)	(17)
Acquisitions of property, plant and equipment	(48)	(107)	(93)	(167)
Acquisitions of intangible assets	14	-	(9)	-
Business combination, purchase price adjustment	-	-	368	-
	<u>(2,117)</u>	<u>(1,116)</u>	<u>(1,544)</u>	<u>(184)</u>
Effect of foreign exchange rate fluctuations on cash and cash equivalents				
	<u>76</u>	<u>10</u>	<u>63</u>	<u>62</u>
Change in cash and cash equivalents	<u>(1,891)</u>	<u>(690)</u>	<u>(1,505)</u>	<u>(634)</u>
Cash and cash equivalents - Beginning of Period	<u>2,774</u>	<u>759</u>	<u>2,388</u>	<u>703</u>
Cash and cash equivalents - End of Period	<u>883</u>	<u>69</u>	<u>883</u>	<u>69</u>

1. Interim financial information

The interim financial statements for the three and six-month periods ended October 31, 2004 and October 31, 2003 are unaudited and have not been reviewed by the Company's auditors. In the opinion of management, all necessary adjustments were made to present fairly the results of these periods. The adjustments made were of a normal recurring nature. The results of operations for the three and six-month periods ended October 31, 2004 and 2003 are not necessarily indicative of the trends for the operating results for the full year.

The disclosures in these interim financial statements do not conform in all respects to the requirements of generally accepted accounting principles for annual financial statements; therefore these interim financial statements should be read in conjunction with the audited annual financial statements for the year ended April 30, 2004. These interim financial statements follow the same accounting policies and methods of their application as the annual financial statements for the year ended April 30, 2004, except for the change in accounting policy outlined below.

Change in Accounting Policy

Stock-based compensation and other stock-based payments

The Company maintains a stock-based compensation plan, which is described in note 11(d) in the audited financial statements for the year ended April 30, 2004. Effective May 1, 2004, the Company has adopted the fair value based method of accounting for stock options and warrants granted to employees and directors and has elected to apply the new standard retroactively without restatement as prescribed by the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3870, Stock-based Compensation and Other Stock-based Payments. Under the fair value based method, compensation cost is measured at fair value at the date of grant and is expensed over the award's vesting period with a corresponding credit to contributed surplus. The stock-based compensation expense is recorded in the financial statements for the three and six-month periods ended October 31, 2004. Accordingly, for the three and six-month periods ended October 31, 2003, the Company provides only pro forma disclosures of net earnings (loss) and net earnings (loss) per common share as if the fair value based method of accounting had been used to account for stock options and warrants granted to employees and directors.

No compensation cost is recognized when shares are issued to employees. Any consideration received from plan participants is credited to capital stock. Any stock-based compensation costs related to awards to individuals other than employees and directors are accounted for at fair value.

The change in accounting for the stock-based compensation has resulted in an adjustment of the opening balance of the consolidated statement of deficit for the current fiscal year of \$4.8 million, with a corresponding credit to contributed surplus, reflecting the prior periods' cost of options and warrants granted since inception, which occurred in the 1998 fiscal year. Additionally, the capital stock account has been increased by \$353,000 with a corresponding reduction in contributed surplus representing the value of compensation cost associated with the options exercised since inception.

2. Capital stock

As at October 31, 2004, options to purchase 922,163 common shares at exercise prices ranging between CA \$0.99 and CA \$27.64 and warrants to purchase 30,000 common shares at an exercise price of CA \$2.03 were outstanding. During the six-month period ended October 31, 2004, the Company granted options to purchase 4,000 common shares with exercise prices ranging from CA \$1.70 to CA \$1.76 (during the three months ended October 31, 2004, the Company granted options to purchase 3,000 common shares with exercise prices ranging from CA \$1.75 to CA \$1.76). During the six months ended October 31, 2004, options to purchase 41,691 common shares at exercise prices ranging from CA \$0.99 to CA \$27.64 were either forfeited or expired (during the three months ended October 31, 2004, options to purchase 20,447 common shares with exercise prices from CA \$0.99 to CA \$27.64 were either forfeited or expired). No options to purchase common shares were exercised during the six-month period ended October 31, 2004.

On July 15, 2004, the Company filed a one-year renewal with the Toronto Stock Exchange of the Notice of Intention to Make a Normal Course Issuer Bid (the "Notice"). The Notice stated the Company's intention to purchase on the open market at prevailing prices, through the facilities of the Toronto Stock Exchange, up to a maximum of 700,000 of its common shares, being approximately 5% of the 14,158,797 common shares outstanding as of June 30, 2004, but not more than 2% of such outstanding common shares as at

June 30, 2004 in any 30-day period. Under the renewal, the Company may purchase common shares, if it considers it advisable, at any time, and from time to time for one year from the date of filing. The common shares will be purchased for cancellation.

During the six-month period ended October 31, 2004, the Company did not purchase any of its outstanding common shares for cancellation, however did incur \$3,000 for fees related to the filing of the Notice. For the six-month period ended October 31, 2003, the Company purchased 320,100 of its outstanding common shares for cancellation at an average price of \$1.04 per share under a Normal Course Issuer Bid. The total cost related to purchasing these shares, including other related costs, was \$335,000.

The total number of common shares outstanding at October 31, 2004 is 14,158,797.

3. Stock-based compensation costs

Commencing May 1, 2004, the company uses the fair value based method to record within its financial statements the stock-based compensation costs related to stock options and warrants granted to employees and directors for all stock options and warrants granted. The stock-based compensation expense recorded for the six months ended October 31, 2004 was CA\$146,000 (US\$113,000). The stock-based compensation expense for the three months ended October 31, 2004 was CA\$79,000 (US\$62,000).

Stock-based compensation costs related to options and warrants are not reflected in the statement of operations for the three and six months ended October 31, 2003. Had the fair value based method been used to account for such stock-based compensation costs, the net earnings (loss) and related net earnings (loss) per common share figures would be as follows:

	Three months ended October 31, 2003	Six months ended October 31, 2003
Net earnings for the period	24	34
Stock-based compensation costs	(63)	(149)
Pro forma net loss for the period	<u>(39)</u>	<u>(115)</u>
Pro forma basic and diluted loss per common share	<u>(\$0.00)</u>	<u>(\$0.01)</u>

The fair value of options and warrants granted was estimated using the Black-Scholes options pricing model with the following weighted average assumptions:

	Three months ended October 31, 2004	Three months ended October 31, 2003	Six months ended October 31, 2004	Six months ended October 31, 2003
Volatility	75%	75%	75%	75%
Risk-free interest rate	3.00%	3.00%	3.00%	3.00%
Dividend yield	nil	nil	nil	nil
Expected lives (in years)	3	3	3	3

Following is a summary of the weighted average grant date fair value of options and warrants granted during the three and six-month periods ended October 31, 2004 and 2003:

	Three months ended October 31, 2004	Three months ended October 31, 2003	Six months ended October 31, 2004	Six months ended October 31, 2003
Number of options & warrants	3,000	362,500	4,000	367,800
Weighted avg. exercise price US \$	1.36	1.19	1.32	1.18
Weighted avg. grant date FV US \$	0.69	0.60	0.67	0.60

4. Other Information

a) Products revenue

Products revenue is broken down as follows:

	Three months ended October 31, 2004	Three months ended October 31, 2003	Six months ended October 31, 2004	Six months ended October 31, 2003
Software products	960	663	2,051	1,402
Third-party hardware and software	878	1,161	1,540	2,018
	<u>1,838</u>	<u>1,824</u>	<u>3,591</u>	<u>3,420</u>

b) Cost of services consist of the following:

	Three months ended October 31, 2004	Three months ended October 31, 2003	Six months ended October 31, 2004	Six months ended October 31, 2003
Gross expenses	1,892	1,346	3,766	2,623
Refundable tax credits	(120)	(137)	(252)	(303)
	<u>1,772</u>	<u>1,209</u>	<u>3,514</u>	<u>2,320</u>

c) Earnings (loss) per share

Basic earnings (loss) per share is calculated using the weighted average number of shares outstanding during the period.

Diluted earnings per share is calculated based on the weighted average number of common shares outstanding during the period plus the effects of dilutive potential common shares outstanding during the period. This method requires that the dilutive effect of outstanding options and warrants be calculated using the treasury stock method, as if all dilutive options and warrants had been exercised at the later of the beginning of the reporting period or date of issuance, and that the funds obtained thereby were used to purchase common shares of the Company at the average trading price of the common shares during the period.

The diluted weighted average number of shares has been calculated as follows:

	Three months ended October 31, 2004	Three months ended October 31, 2003	Six months ended October 31, 2004	Six months ended October 31, 2003
Weighted average number of shares - basic	14,158,797	14,162,647	14,158,797	14,263,121
Additions to reflect the impacts of:				
Exercise of employee stock options and warrants	-	89,489		48,183
Weighted average number of shares-diluted	<u>14,158,797</u>	<u>14,252,136</u>	<u>14,158,797</u>	<u>14,311,304</u>

Options and warrants to purchase 952,163 common shares for the three and six months ended October 31, 2004 (six months ended October 31, 2003 – 749,293, three months ended October 31, 2003 – 399,043) have been excluded from the above calculations since they would have an anti-dilutive effect. There are no differences between basic and diluted per share figures.

5. Significant differences between Canadian and United States GAAP

The Company's financial statements are prepared in accordance with Canadian GAAP, which differs in some respects from U.S. GAAP. Significant measurement differences between Canadian GAAP and U.S. GAAP as they relate to the Company, are set forth below:

a) Statement of Operations

There are no differences between Canadian GAAP and U.S. GAAP affecting the net earnings (loss) or the basic and diluted net earnings (loss) per share for the three and six months ended October 31, 2004 and 2003. The following summary is a reconciliation of the net earnings (loss) to the comprehensive income for each period presented.

	Three months ended October 31, 2004	Three months ended October 31, 2003	Six months ended October 31, 2004	Six months ended October 31, 2003
Net earnings (loss) for the period in accordance with Canadian GAAP and U.S. GAAP	(316)	24	(180)	34
Other comprehensive income:				
Foreign currency translation adjustments	1,220	820	1,622	1,055
Comprehensive income	<u>904</u>	<u>844</u>	<u>1,442</u>	<u>1,089</u>

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The statements in this report relating to matters that are not historical fact are forward looking statements that are based on management's beliefs and assumptions. Such statements are not guarantees of future performance, and are subject to a number of uncertainties, including but not limited to future economic conditions, the markets that TECSYS Inc. serves, the actions of competitors, major new technological trends and other factors beyond the control of TECSYS Inc., which could cause actual results to differ materially from such statements.

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