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TECHTEAM GLOBAL INC
Form 10-Q
November 05, 2004

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: September 30, 2004

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

For the transition period from ___ to ___

Commission file number 0-16284

TECHTEAM GLOBAL, INC.

(Name of issuer in its charter)

DELAWARE

38-2774613

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

27335 W. 11 Mile Road, Southfield, MI 48034

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (248) 357-2866

Registrant's Internet address: www.techteam.com

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 No

Indicate by check mark whether the registrant is an accelerated filer.
Yes No

The number of shares of the registrant's common stock outstanding at October 29, 2004 was 8,710,437.

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TECHTEAM GLOBAL, INC.

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PART 1 -- FINANCIAL INFORMATION

ITEM 1 -- FINANCIAL STATEMENTS

TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

(In thousands, except per share data)

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| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTH SEPTEMBER |
|--|-------------------------------------|-----------|-------------------------|
| | 2004 | 2003 | 2004 |
| REVENUE | | | |
| Corporate services | | | |
| Corporate help desk services | \$ 19,274 | \$ 17,211 | \$ 57,289 |
| Professional services/systems integration | 12,837 | 2,242 | 31,176 |
| Technical staffing | 1,781 | 2,233 | 5,767 |
| Training programs | 133 | 213 | 440 |
| Total corporate services | 34,025 | 21,899 | 94,672 |
| Leasing operations | 94 | 409 | 397 |
| TOTAL REVENUE | 34,119 | 22,308 | 95,069 |
| COST OF SERVICES DELIVERED | | | |
| Cost of corporate services | 26,134 | 17,305 | 71,635 |
| Cost of leasing operations | 60 | 752 | 304 |
| TOTAL COST OF SERVICES DELIVERED | 26,194 | 18,057 | 71,939 |
| GROSS PROFIT | 7,925 | 4,251 | 23,130 |
| Selling, general, and administrative expense | 5,781 | 4,703 | 17,986 |
| OPERATING INCOME (LOSS) | 2,144 | (452) | 5,144 |
| OTHER INCOME (EXPENSE) | | | |
| Interest income, net | 175 | 388 | 464 |
| Foreign currency transaction gain (loss) | (50) | 86 | (268) |
| TOTAL OTHER INCOME | 125 | 474 | 196 |
| INCOME (LOSS) BEFORE INCOME TAXES | 2,269 | 22 | 5,340 |
| Income tax provision | 751 | 453 | 2,122 |
| NET INCOME (LOSS) | \$ 1,518 | \$ (431) | \$ 3,218 |
| BASIC EARNINGS (LOSS) PER SHARE | \$ 0.18 | \$ (0.04) | \$ 0.37 |
| DILUTED EARNINGS (LOSS) PER SHARE | \$ 0.16 | \$ (0.04) | \$ 0.34 |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES AND COMMON SHARE EQUIVALENTS OUTSTANDING | | | |
| Basic | 8,636 | 9,723 | 8,640 |
| Net effect of dilutive stock options | 268 | -- | 224 |
| Effect of redeemable convertible preferred stock | 690 | -- | 690 |
| Diluted | 9,594 | 9,723 | 9,554 |

See accompanying notes.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(In thousands)

| ASSETS | SEPTEMBER 30, 2004 | DECEMBER 31, 2003 |
|---|--------------------|-------------------|
| ----- | ----- | ----- |
| | (Unaudited) | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$40,103 | \$35,1 |
| Accounts receivable -- corporate services (less allowances of \$705 at September 30, 2004 and \$637 at December 31, 2003) | 24,527 | 22,4 |
| Accounts receivable -- leasing (less allowances of \$738 at September 30, 2004 and \$740 at December 31, 2003) | 116 | 7 |
| Prepaid expenses and other | 2,296 | 1,6 |
| Deferred income taxes | 76 | 5 |
| | ----- | ----- |
| TOTAL CURRENT ASSETS | 67,118 | 60,6 |
| PROPERTY, EQUIPMENT, AND PURCHASED SOFTWARE | | |
| Computer equipment and office furniture | 21,819 | 20,6 |
| Purchased software | 11,291 | 11,0 |
| Leasehold improvements | 4,580 | 4,5 |
| Transportation equipment | 316 | 2 |
| | ----- | ----- |
| Less -- Accumulated depreciation and amortization | 38,006 | 36,4 |
| | 29,732 | 26,5 |
| | ----- | ----- |
| NET PROPERTY, EQUIPMENT, AND PURCHASED SOFTWARE | 8,274 | 9,9 |
| OTHER ASSETS | | |
| Intangible assets, net | 3,750 | 3,6 |
| Goodwill | 2,743 | 2,0 |
| Deferred income taxes | 75 | 8 |
| Other | 290 | 6 |
| | ----- | ----- |
| TOTAL OTHER ASSETS | 6,858 | 7,1 |
| | ----- | ----- |
| TOTAL ASSETS | \$82,250 | \$77,7 |
| | ===== | ===== |

See accompanying notes.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (continued)

(In thousands, except share and per share amounts)

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| LIABILITIES AND SHAREHOLDERS' EQUITY | SEPTEMBER 2004 |
|---|-------------------|
| ----- | ----- |
| | (Unaudited) |
| CURRENT LIABILITIES | |
| Notes payable | \$ 91 |
| Accounts payable | 3,008 |
| Accrued payroll, related taxes, and withholdings | 7,280 |
| Accrued expenses | 1,303 |
| Accrued income taxes | 822 |
| Deferred revenue | 1,600 |
| | ----- |
| TOTAL CURRENT LIABILITIES | 14,104 |
| LONG-TERM LIABILITIES | 332 |
| REDEEMABLE CONVERTIBLE PREFERRED STOCK, 5,000,000 shares authorized, 689,656 shares issued and outstanding; liquidation preference of \$5,000 at September 30, 2004 and December 31, 2003 | 5,000 |
| SHAREHOLDERS' EQUITY | |
| Common stock, par value \$0.01, 45,000,000 shares authorized, 8,710,437 and 8,817,265 shares issued and outstanding at September 30, 2004 and December 31, 2003, respectively | 87 |
| Additional paid-in capital | 58,587 |
| Retained earnings | 3,286 |
| Accumulated other comprehensive income -- cumulative foreign currency translation adjustment | 854 |
| | ----- |
| TOTAL SHAREHOLDERS' EQUITY | 62,814 |
| | ----- |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | \$82,250 |
| | ===== |

See accompanying notes.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(In thousands)

| | NINE MONTHS ENDED SEP |
|---|-----------------------|
| | ----- |
| | 2004 |
| | ----- |
| OPERATING ACTIVITIES | |
| Net income (loss) | \$ 3,218 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | |
| Depreciation and amortization | 3,348 |

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| | |
|---|-----------|
| Non-cash expense related to stock options and common stock issued to 401(k) plan and directors | 305 |
| Other | 131 |
| Changes in current assets and liabilities | 2,496 |
| Changes in long-term assets and liabilities | 147 |
| | ----- |
| Net cash provided by operating activities | 9,645 |
| INVESTING ACTIVITIES | |
| Purchase of property, equipment and software | (1,252) |
| Cash paid for acquisitions, net of cash acquired | (1,036) |
| Sale of marketable securities available for sale | -- |
| Proceeds from disposal of property and equipment | -- |
| | ----- |
| Net cash provided by (used in) investing activities | (2,288) |
| FINANCING ACTIVITIES | |
| Purchase of Company common stock | (2,744) |
| Payments on long-term borrowings | (1,045) |
| Proceeds from issuance of common stock | 1,093 |
| Proceeds from issuance of preferred stock | -- |
| | ----- |
| Net cash used in financing activities | (2,696) |
| | ----- |
| EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS | 247 |
| | ----- |
| INCREASE IN CASH AND CASH EQUIVALENTS | 4,908 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD | 35,195 |
| | ----- |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | \$ 40,103 |
| | ===== |

See accompanying notes.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 -- BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared by TechTeam Global, Inc. ("TechTeam" or the "Company" or "we") in accordance with accounting principles generally accepted in the United States for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission Rules and Regulations. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included, and such adjustments are of a normal recurring nature. Operating results for the three and nine months ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003.

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Certain reclassifications have been made to the 2003 financial statements in order to conform to the 2004 financial statement presentation.

NOTE 2 -- EARNINGS PER SHARE

Earnings (loss) per share is computed using the weighted average number of common shares and common share equivalents outstanding. Common share equivalents consist of stock options and convertible preferred stock.

During the nine months ended September 30, 2004 and 2003, 508,900 and 721,077 stock options, respectively, were excluded from the computation of diluted earnings per share because the options' exercise prices were higher than the average market price of the common shares during the respective period. During the nine months ended September 30, 2003, an additional 496,504 stock options and 689,656 outstanding shares of convertible preferred stock were excluded from the computation of diluted earnings per share due to the net loss for the period.

NOTE 3 -- COMPREHENSIVE INCOME

Comprehensive income (loss) consists of net income (loss) and foreign currency translation adjustments. A summary of comprehensive income is as follows:

| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS ENDED SEPTEMBER 30, | |
|---|-------------------------------------|----------|------------------------------------|------------|
| | 2004 | 2003 | 2004 | 2003 |
| | (In thousands) | | | |
| COMPREHENSIVE INCOME (LOSS) | | | | |
| Net income (loss) | \$ 1,518 | \$ (431) | \$ 3,218 | \$ (1,796) |
| Other comprehensive income (loss)-- | | | | |
| Foreign currency translation adjustment ... | 299 | (28) | 172 | 335 |
| Comprehensive income (loss) | \$ 1,817 | \$ (459) | \$ 3,390 | \$ (1,461) |

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(continued)

NOTE 4 -- INCOME TAXES

The consolidated effective tax rate in 2004 and 2003 differs from the statutory tax rate of 34% primarily due to providing a valuation allowance against the future tax benefit of operating loss carryforwards in certain foreign tax jurisdictions.

NOTE 5 -- STOCK-BASED COMPENSATION

We account for stock-based compensation awards granted to employees using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), and related interpretations. The effect on net income and earnings per share had

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compensation costs been recognized based on the fair value method prescribed by Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," is as follows:

| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS SEPTEMBER |
|--|-------------------------------------|-----------|--------------------------|
| | 2004 | 2003 | 2004 |
| | (In thousands) | | |
| Reported net income (loss) | \$ 1,518 | \$ (431) | \$ 3,218 |
| Add -- total stock-based compensation expense included in reported net income, net of tax | -- | 3 | -- |
| Deduct -- total stock-based compensation expense determined under the fair value method for all awards, net of tax | (699) | (72) | (974) |
| Pro forma net income (loss) | \$ 819 | \$ (500) | \$ 2,244 |
| Basic earnings (loss) per share: | | | |
| As reported | \$ 0.18 | \$ (0.04) | \$ 0.37 |
| Pro forma | \$ 0.09 | \$ (0.05) | \$ 0.26 |
| Diluted earnings (loss) per share: | | | |
| As reported | \$ 0.16 | \$ (0.04) | \$ 0.34 |
| Pro forma | \$ 0.09 | \$ (0.05) | \$ 0.23 |

The Financial Accounting Standards Board has issued an Exposure Draft, "Share-Based Payment - an Amendment of FASB Statements No. 123 and 95," and is expected to issue a final Statement by December 31, 2004. The proposed Statement would eliminate the ability to account for share-based compensation transactions using APB 25, and generally would require instead that such transactions be accounted for using a fair-value-based method. This Statement is expected to be effective for the Company for awards that are granted, modified, or settled in periods beginning after June 15, 2005, or the Company's third quarter. As we use the fair value method of accounting under the original provisions of SFAS 123 for pro forma disclosure purposes, we are also required to apply the provisions of this Statement in recognizing compensation cost for any portion of awards granted or modified after December 15, 1994, that are not yet vested at the date this Statement is adopted. Based on the number of non-vested stock options the Company has outstanding at September 30, 2004, adoption of this Statement will not have a material affect on our financial position or operating results.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(continued)

NOTE 6 -- LINE OF CREDIT

In August 2004, we entered into a revolving line-of-credit agreement with Standard Federal Bank, N.A. whereby the Company may borrow up to \$5 million. Outstanding borrowings bear interest at 0.5% and are collateralized by a compensating balance cash deposit required to be held at the bank equal to the amount of any outstanding borrowings. The Company has not borrowed any amounts

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under this agreement at September 30, 2004. The agreement expires on September 7, 2006.

NOTE 7 -- SEGMENT REPORTING

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. Our chief operating decision-making group is the Senior Management Committee, which is comprised of the President and the lead executives of each of our functional divisions. The operating segments are managed separately because each operating segment represents a strategic business unit that offers different services.

Our reportable operating segments include corporate help desk services, professional services/systems integration (formerly referred to as "systems integration"), technical staffing, and training programs (collectively referred to as "corporate services") and leasing operations.

CORPORATE HELP DESK SERVICES -- this segment provides corporations and governments with around-the-clock (24x7x365) technical and customer support for their end-users and other constituencies. We support the full range of a client's information technology ("IT"), client service, and business process infrastructure. We also provide technical support to customers of our clients' products and software.

PROFESSIONAL SERVICES/SYSTEMS INTEGRATION -- this segment provides IT infrastructure (personal computers, printers, phone systems, networks, servers, switches, etc.) support through systems integration, technology deployment, and implementation services from project planning and maintenance to full-scale network server and workstation installations. We offer a wide range of information technology services for the customer, ranging from technology consulting to desk-side support to network monitoring. We also provide full-service IT staff and consulting services to companies to help manage their IT infrastructure.

TECHNICAL STAFFING -- this segment maintains a staff of trained technical personnel, which we place at our clients' facilities to provide technical support services including help desk technicians, software developers, and network support.

TRAINING PROGRAMS -- this segment provides custom training and documentation solutions that include computer-based training, distance learning, course catalogs, registration, instructional design consultants, customized course materials, certified trainers, evaluation options, desk-side tutorials, and custom reports. We provide customized training programs for many of our customers' proprietary applications.

LEASING OPERATIONS -- this segment previously wrote leases for computer, telecommunications, and other types of capital equipment. Effective March 31, 2000, we ceased looking for new leasing opportunities and are currently running out our lease portfolio.

The accounting policies of the operating segments are the same as those described in Note 1 to the Company's consolidated financial statements contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2003. We evaluate segment performance based on segment gross profit.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 -- SEGMENT REPORTING (continued)

Financial information for our operating segments is as follows:

| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS ENDED SEPTEMBER 30, | |
|--|-------------------------------------|-----------|------------------------------------|---------|
| | 2004 | 2003 | 2004 | 2003 |
| | (In thousands) | | | |
| REVENUE | | | | |
| Corporate services | | | | |
| Corporate help desk services | \$ 19,274 | \$ 17,211 | \$ 57,289 | \$ 49,6 |
| Professional services/systems integration | 12,837 | 2,242 | 31,176 | 6,5 |
| Technical staffing | 1,781 | 2,233 | 5,767 | 7,0 |
| Training programs | 133 | 213 | 440 | 6 |
| | 34,025 | 21,899 | 94,672 | 63,8 |
| Leasing operations | 94 | 409 | 397 | 2,1 |
| | \$ 34,119 | \$ 22,308 | \$ 95,069 | \$ 65,9 |
| | ===== | ===== | ===== | ===== |
| GROSS PROFIT (LOSS) | | | | |
| Corporate services: | | | | |
| Corporate help desk services | \$ 4,898 | \$ 3,522 | \$ 14,939 | \$ 10,4 |
| Professional services/systems integration | 2,671 | 600 | 6,865 | 1,6 |
| Technical staffing | 300 | 436 | 1,141 | 1,4 |
| Training programs | 22 | 36 | 93 | 1 |
| | 7,891 | 4,594 | 23,038 | 13,6 |
| Leasing operations | 34 | (343) | 92 | (1,6 |
| | 7,925 | 4,251 | 23,130 | 11,9 |
| Selling, general, and administrative expense | (5,781) | (4,703) | (17,986) | (14,6 |
| Interest income, net | 175 | 388 | 464 | 8 |
| Foreign currency transaction gain (loss) | (50) | 86 | (268) | 4 |
| | \$ 2,269 | \$ 22 | \$ 5,340 | \$ (1,3 |
| | ===== | ===== | ===== | ===== |

We attribute revenue to different geographic areas on the basis of the location providing the services to the customer. Revenue by geographic area is presented below:

| THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS ENDED SEPTEMBER 30, | |
|-------------------------------------|------|------------------------------------|------|
| 2004 | 2003 | 2004 | 2003 |
| (In thousands) | | | |

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| | | | | |
|---------------------|----------|----------|----------|----------|
| REVENUE | | | | |
| United States | \$23,297 | \$14,993 | \$66,080 | \$46,537 |
| Europe: | | | | |
| Belgium | 7,663 | 4,574 | 18,631 | 11,965 |
| United Kingdom ... | 1,272 | 1,326 | 4,263 | 3,949 |
| Other | 1,887 | 1,415 | 6,095 | 3,536 |
| | ----- | ----- | ----- | ----- |
| Total Europe | 10,822 | 7,315 | 28,989 | 19,450 |
| | ----- | ----- | ----- | ----- |
| Total revenue | \$34,119 | \$22,308 | \$95,069 | \$65,987 |
| | ===== | ===== | ===== | ===== |

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(continued)

NOTE 7 -- SEGMENT REPORTING (continued)

We provide corporate services for major companies on an international scale. Revenue from customers that comprise 10% or greater of our total revenue in any period presented are as follows:

| | THREE MONTHS ENDED | | NINE MONTHS ENDED | |
|---|--------------------|-------|-------------------|-------|
| | SEPTEMBER 30, | | SEPTEMBER 30, | |
| | 2004 | 2003 | 2004 | 2003 |
| | ---- | ---- | ---- | ---- |
| Ford Motor Company | 33.8% | 46.6% | 37.9% | 49.6% |
| United States Department of Defense ... | 9.7% | -- | 10.5% | -- |
| DaimlerChrysler | 7.4% | 13.0% | 8.6% | 14.1% |
| | ---- | ---- | ---- | ---- |
| Total | 50.9% | 59.6% | 57.0% | 63.7% |
| | ==== | ==== | ==== | ==== |

NOTE 8 -- CONTINGENCIES

DIGITAL SUPPORT CORPORATION:

TechTeam acquired 100% of the outstanding capital stock of Digital Support Corporation ("DSC") on December 31, 2003. DSC provides services to various departments within the United States Department of Defense ("DoD"). A Facility Security Clearance ("FSC") is required as a condition for DSC to perform its services for the DoD. As the acquiring entity, TechTeam also needs to obtain an FSC or negate any foreign ownership, control, or influence that could impair our ability to obtain an FSC. We have applied for an FSC, but as of the date of the filing of this document, we have not received a response from the DoD. It is reasonably possible that we will not be deemed eligible for an FSC due to the beneficial ownership of over 5% of our capital stock by ChrysCapital II, LLC, a Mauritius entity ("ChrysCapital"), and ChrysCapital's right to appoint a member of our Board of Directors. We have applied to the DoD for a Security Control Agreement ("SCA") between DSC and the DoD in order to negate the foreign interest. The SCA, if approved, would negate the impact of the foreign interest without affecting TechTeam's ability to integrate DSC into the TechTeam group of

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companies.

LEGAL PROCEEDINGS:

The Company is a party to various legal proceedings that are routine and incidental to its business. Although the consequences of these proceedings are not presently determinable, in the opinion of management, they will not have a material adverse affect on our liquidity, financial condition, or results of operations, although no assurances can be given in this regard.

NOTE 9 -- ACQUISITIONS

ADVANCED NETWORK ENGINEERING:

On May 13, 2004, TechTeam Global NV/SA, the Company's wholly-owned subsidiary in Belgium, completed the acquisition of all of the outstanding stock of Advanced Network Engineering NV/SA (formerly Advanced Network Engineering CVBA) ("A.N.E.") for (euro)885,000 plus acquisition costs of (euro)143,000 for an initial purchase price of (euro)1.03 million (\$1.22 million at May 13, 2004). Of the initial purchase price, (euro)750,000 was paid at closing, (euro)178,000 will be paid in 2004, and (euro)100,000 will be paid on May 13, 2005, provided there are no claims asserted by us based upon the representations and warranties of the sellers in the Share Purchase Agreement. In addition to the initial purchase price, an additional (euro)150,000 is payable on May 13, 2007 provided a cumulative operating income target is met for the three-year period ending April 30, 2007. The additional consideration paid to selling shareholders will be recorded as additional goodwill when it is earned.

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(continued)

NOTE 9 -- ACQUISITIONS (continued)

A.N.E. is an information technology services and solutions company headquartered in Gent, Belgium, that provides software application, network, and systems integration services to various global, pan-European, and Belgian customers. The acquisition of A.N.E. will complement our subsidiary in Belgium, which primarily provides corporate help desk services. The acquisition was accounted for using the purchase method of accounting and, accordingly, the operating results of A.N.E. are included in the consolidated operating results of TechTeam since the acquisition date. Goodwill and other intangible assets acquired totaled (euro)810,000 (\$961,000 at May 13, 2004). Of this amount, other intangible assets totaled (euro)378,000 (\$449,000 at May 13, 2004) and consist of customer relationship assets, which are being amortized on a straight-line basis over their estimated useful life of six years. A.N.E. has been assigned to our professional services/systems integration operating segment. Subsequent to the acquisition, A.N.E.'s name has been changed to TechTeam A.N.E. NV/SA.

The following table summarizes the allocation of the initial purchase price at May 13, 2004:

AMOUNT

(In thousands)

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| | |
|--|---------|
| Customer relationship assets | \$ 449 |
| Goodwill | 512 |
| Property, equipment and software | 72 |
| Other current and non-current assets, net of cash acquired of \$128 | 1,367 |
| Accounts payable and accrued liabilities assumed | (1,117) |
| Accrued purchase price | (261) |
| Notes payable assumed | (191) |
| | ----- |
| Net cash used | \$ 831 |
| | ===== |

The unaudited pro forma condensed consolidated results of operations for the nine months ended September 30, 2004, and the three and nine months ended September 30, and 2003 are presented below as though A.N.E. had been acquired on January 1, 2003.

| | THREE MONTHS ENDED SEPTEMBER 30, 2003 | NINE MONTHS ENDED SEPTEMBER 30, 2004 | 2003 |
|-----------------------------------|--|--|------------|
| | ----- | | |
| | (In thousands) | | |
| Revenue | | | |
| As reported | \$ 22,308 | \$ 95,069 | \$ 65,987 |
| Pro forma | \$ 23,615 | \$ 97,593 | \$ 69,659 |
| Net income (loss) | | | |
| As reported | \$ (431) | \$ 3,218 | \$ (1,796) |
| Pro forma | \$ (506) | \$ 3,205 | \$ (1,879) |
| Diluted earnings (loss) per share | | | |
| As reported | \$ (0.04) | \$ 0.34 | \$ (0.18) |
| Pro forma | \$ (0.05) | \$ 0.34 | \$ (0.19) |

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(continued)

NOTE 9 -- ACQUISITIONS (continued)

DIGITAL SUPPORT CORPORATION:

TechTeam acquired 100% of the outstanding capital stock of DSC on December 31, 2003. The unaudited pro forma condensed consolidated results of operations for the three and nine months ended September 30, 2003 are presented below as though DSC had been acquired on January 1, 2003.

| THREE MONTHS ENDED SEPTEMBER 30, 2003 | NINE MONTHS ENDED SEPTEMBER 30, 2003 |
|---|--|
|---|--|

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| | ----- | | ----- | |
|------------------------|----------------|--------|-------|---------|
| | (In thousands) | | | |
| Revenue | | | | |
| As reported | \$ | 22,308 | \$ | 65,987 |
| Pro forma | \$ | 27,386 | \$ | 80,160 |
| Net loss | | | | |
| As reported | \$ | (431) | \$ | (1,796) |
| Pro forma | \$ | (188) | \$ | (1,284) |
| Diluted loss per share | | | | |
| As reported | \$ | (0.04) | \$ | (0.18) |
| Pro forma | \$ | (0.02) | \$ | (0.13) |

The unaudited pro forma condensed consolidated results of operations for the three and nine months ended September 30, 2003 are presented below as though both DSC and A.N.E. had been acquired on January 1, 2003.

| | THREE MONTHS ENDED SEPTEMBER 30, 2003 | | NINE MONTHS ENDED SEPTEMBER 30, 2003 | |
|------------------------|---------------------------------------|--------|--------------------------------------|---------|
| | ----- | | | |
| | (In thousands) | | | |
| Revenue | | | | |
| As reported | \$ | 22,308 | \$ | 65,987 |
| Pro forma | \$ | 28,693 | \$ | 83,832 |
| Net loss | | | | |
| As reported | \$ | (431) | \$ | (1,796) |
| Pro forma | \$ | (263) | \$ | (1,367) |
| Diluted loss per share | | | | |
| As reported | \$ | (0.04) | \$ | (0.18) |
| Pro forma | \$ | (0.03) | \$ | (0.14) |

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TECHTEAM GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(continued)

NOTE 10 -- GOODWILL AND OTHER INTANGIBLE ASSETS

Changes in the carrying amount of goodwill by operating segment consist of the following:

| | CORPORATE HELP DESK SERVICES | PROFESSIONAL SERVICES/ SYSTEMS INTEGRATION | TOTAL |
|-------------------------------------|------------------------------------|---|---------|
| | ----- | ----- | ----- |
| | (In thousands) | | |
| Balance as of January 1, 2004 | \$ 371 | \$1,728 | \$2,099 |

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| | | | |
|---|--------|---------|---------|
| Goodwill acquired from A.N.E. and DSC | -- | 624 | 624 |
| Foreign currency translation adjustment ... | -- | 20 | 20 |
| | | ----- | ----- |
| Balance as of September 30, 2004 | \$ 371 | \$2,372 | \$2,743 |
| | ===== | ===== | ===== |

Other intangible assets consist of the following:

| | SEPTEMBER 30, 2004 | | DECEMBER 31, 2003 | | |
|--|--------------------|-----------------------------|-------------------|-----------------------------|-----------------|
| | COST | ACCUMULATED AMORTIZATION | COST | ACCUMULATED AMORTIZATION | AMORTIZ PERI |
| | (In thousands) | | | | |
| Customer relationships -- DSC | \$3,367 | \$ 253 | \$3,367 | \$ -- | 10 ye |
| Customer relationships -- Cyntergy ... | 701 | 502 | 701 | 434 | 5 ye |
| Customer relationships -- A.N.E. | 466 | 29 | -- | -- | 6 ye |
| | ----- | ----- | ----- | ----- | |
| | \$4,534 | \$ 784 | \$4,068 | \$ 434 | |
| | ===== | ===== | ===== | ===== | |

We evaluate definite-lived intangible assets based on undiscounted operating cash flows whenever significant events or changes occur that might indicate impairment of recorded costs. If undiscounted cash flows are insufficient to recover recorded costs, we write down the carrying value of the assets to fair value based on discounted cash flows or market values. We did not record an impairment loss for definite-lived intangible assets in any period presented.

On September 30, 2004 and 2003, we conducted our annual impairment test of goodwill and concluded that no component of goodwill was impaired at either balance sheet date. In conducting the test, we compared the estimated fair value of each reporting unit, as that term is defined by SFAS 142, with the reporting unit's carrying amount. The estimated fair values of the reporting units exceeded their carrying values.

Our expected amortization expense for definite-lived intangible assets is as follows: \$123,000 for the remainder of 2004, \$499,000 for 2005, \$499,000 for 2006, \$411,000 for 2007, and \$411,000 for 2008.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 2, contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause the results of TechTeam Global, Inc. and its consolidated subsidiaries ("TechTeam") to differ materially from those expressed or implied by such forward-looking statements. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including any projections of revenue, gross margin, expenses, earnings or losses from operations, synergies, or other financial items; any statements of the plans, strategies, and objectives of management for future operations; any statement concerning developments or performance relating to our services; any statements

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regarding future economic conditions or performance; any statements of expectation or belief; and any statements of assumptions underlying any of the foregoing. The risks, uncertainties and assumptions referred to above include the performance of contracts by suppliers, customers, and partners; employee management issues; the difficulty of aligning expense levels with revenue changes; complexities of global political and economic developments; and other risks that are described herein, including but not limited to the items discussed in "Factors that Could Affect Future Results" set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 2 of this report, and that are otherwise described from time to time in TechTeam's Securities and Exchange Commission reports filed after this report. TechTeam assumes no obligation and does not intend to update these forward-looking statements.

ITEM 2 -- MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

We are an information technology ("IT") and business process outsourcing support services provider, offering our customers with assistance in designing, implementing, managing, and maintaining their IT infrastructure and computer systems through our provision of corporate help desk services, professional/systems integration services (formerly referred to as "systems integration"), technical staffing, and training programs. Thus far in 2004, we have significantly improved our operating performance over 2003 by pursuing four strategic initiatives: (1) grow our overall business through strategic and accretive acquisitions both domestically and internationally, (2) expand our footprint in the IT professional services sector, as we believe infrastructure support services and systems and software implementation services offer significant opportunity for complementary growth and improved gross margin, (3) improve operating efficiencies and profitability, primarily in our corporate help desk services operating segment, through various performance improvement and cost saving initiatives, and (4) continue our growth in Europe and establish multilingual call center operations in Romania to realize operational efficiencies and cost savings from offering our customers a blended solution with our multilingual call center operations in Belgium.

Our progress with the first two strategic initiatives is demonstrated by our acquisition of two companies in our professional services/systems integration operating segment -- Advanced Network Engineering NV/SA ("A.N.E.") on May 13, 2004 and Digital Support Corporation ("DSC") on December 31, 2003. A.N.E. is an information technology services and solutions company in Belgium that provides software application, network infrastructure, and systems integration services to various global, pan-European, and Belgian customers. DSC is an information technology services and solutions company that provides network infrastructure, information assurance, enterprise application, systems integration, and hardware services and solutions to various governmental and commercial customers. Together A.N.E. and DSC contributed revenue and gross profit of \$23.8 million and \$5.01 million, respectively, to our operating results for the nine months ended September 30, 2004, which resulted in an increase in professional services/systems integration revenue of 378% to \$31.2 million and increase in gross profit of 309% to \$6.87 million, over the comparable period in 2003.

Our 2004 results to date reflect progress toward our third strategic initiative of realizing operating efficiencies and cost savings from initiatives implemented in 2003 and 2004. These efficiencies and cost savings primarily relate to our corporate help desk services operating segment and include, but

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are not limited to, consistently aligning our headcount with the level of business being generated from our customers, reducing operational office space in the U.S. and Belgium, and implementing a global performance management process to promote operational improvements. As a result, gross profit from corporate help desk services increased 43.4% to \$14.9 million for the nine months ended September 30, 2004, from \$10.4 million for the comparable period in 2003. Gross margin (gross profit as a percentage of revenue) from corporate help desk services increased to 26.1% for the nine months ended September 30, 2004, from 21.0% for the comparable period in 2003. The increase in gross profit and gross margin was primarily due to increased business with new customers in Europe and realization of the aforementioned operational efficiencies and cost savings on a global basis. Gross margin from corporate help desk services in the United States increased to 25.4% for the nine months ended September 30, 2004, from 23.2% for the comparable period in 2003. Gross margin from corporate help desk services in Europe increased to 26.9% for the nine months ended September 30, 2004, from 17.2% for the comparable period in 2003.

Lastly, our progress toward meeting our fourth strategic initiative is demonstrated by revenue generated in Europe increasing 49.0% to \$29.0 million for the nine months ended September 30, 2004, from \$19.5 million for the comparable period in 2003, and by successfully establishing call center operations in Bucharest, Romania with the delivery of customer support services beginning in April 2004. And as noted, we significantly improved gross margin performance in Europe. Excluding revenue contributed by A.N.E., revenue generated in Europe increased 37.7% to \$26.8 million for the nine months ended September 30, 2004, from the comparable period in 2003, primarily due to growth in business at our Belgian and Swedish subsidiaries and the strengthening of European currencies relative to the U.S. dollar. If revenue in Europe for the nine months ended September 30, 2004 were translated at the average exchange rate for the comparable period in 2003, reported revenue would have been reduced by approximately \$2.59 million for the nine months ended September 30, 2004. Since most of the Company's international operating expenses are also incurred in the same foreign currencies in which the associated revenue is denominated, the net impact of exchange rate fluctuations on gross profit and operating income is considerably less than the estimated impact on revenue.

While making solid progress toward our strategic initiatives, we recently reported that DaimlerChrysler, AG ("DaimlerChrysler"), following a formal request for proposal and bid process, has decided to transition the majority of its North American Dealership Help Desk to a new vendor by January 31, 2005. DaimlerChrysler remains a very valued customer. We will continue to provide DaimlerChrysler with Dealership Help Desk services for DaimlerChrysler's European dealers, technical staffing, and desktop training services. We also reported that Liberty Mutual Insurance Company ("Liberty Mutual") has extended the Company's contract for help desk services from August 31, 2004 through June 30, 2005. Liberty Mutual also informed us of its decision not to renew the help desk services contract beyond June 30, 2005 as a result of a strategic business decision to provide these services with internal resources to Liberty Mutual, and that their decision was not influenced by the quality of services rendered or the price charged by the Company.

We expect the effect of the transition in business with DaimlerChrysler to result in a reduction in revenue of approximately \$3.7 million in 2005, as compared to 2004. The volume of work activity for the North American Dealership Help Desk has been trending downward over the past twelve months as it is an established and stable help desk. We expect the loss in revenue from the Liberty Mutual contract to be less than \$1.5 million for 2005, all in the last five months of the year.

Furthermore, we also recently announced that we have been awarded business with new customers worth approximately \$6.8 million in annual revenue, which we will begin to realize before the end of this year.

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RESULTS OF OPERATIONS

THREE MONTHS ENDED SEPTEMBER 30, 2004 COMPARED TO SEPTEMBER 30, 2003

| | THREE MONTHS ENDED SEPTEMBER 30, | | INCREASE (DECREASE) | % CHANGE |
|--|-------------------------------------|-----------|------------------------|-------------|
| | 2004 | 2003 | | |
| (In thousands) | | | | |
| REVENUE | | | | |
| Corporate services: | | | | |
| Corporate help desk services | \$ 19,274 | \$ 17,211 | \$ 2,063 | 12.0% |
| Professional services/systems integration..... | 12,837 | 2,242 | 10,595 | 472.6% |
| Technical staffing | 1,781 | 2,233 | (452) | (20.2)% |
| Training programs | 133 | 213 | (80) | (37.6)% |
| Total corporate services | 34,025 | 21,899 | 12,126 | 55.4% |
| Leasing operations | 94 | 409 | (315) | (77.0)% |
| Total revenue | \$ 34,119 | 22,308 | \$ 11,811 | 52.9% |

Revenue from corporate help desk services increased 12.0% to \$19.3 million for the three months ended September 30, 2004, from \$17.2 million for the comparable period in 2003, primarily due to additional business from new customers in Belgium and the strengthening of the euro, British pound sterling, and Swedish kroner relative to the U.S. dollar, partially offset by a contractual price reduction granted to Ford Motor Company ("Ford") effective August 1, 2004. Revenue from professional services/systems integration increased 473% to \$12.8 million for the three months ended September 30, 2004, from \$2.24 million for the comparable period in 2003, due to our acquisitions of DSC and A.N.E. and additional business from existing customers. Excluding revenue contributed by DSC and A.N.E., professional services/systems integration revenue increased 13.5% to \$2.54 million for the three months ended September 30, 2004, from the comparable period in 2003. Revenue from technical staffing services decreased 20.2% to \$1.78 million for the three months ended September 30, 2004, from \$2.23 million for the comparable period in 2003, primarily due to staffing reductions in the United States, which were only partially offset by additional business received in Europe.

Revenue from leasing operations decreased 77.0% to \$94,000 for the three months ended September 30, 2004, from \$409,000 for the comparable period in 2003. The decline in leasing operations revenue was the result of our decision in March 2000 to discontinue actively seeking new leasing business and to commence the wind down of our lease portfolio. The trend of declining revenue from our leasing operations will continue.

Revenue generated in the United States increased 55.4% to \$23.3 million for the three months ended September 30, 2004, from \$15.0 million for the comparable period in 2003, due to our acquisition of DSC. Excluding revenue contributed by DSC and our leasing operations, revenue generated in the United States decreased 0.8% to \$14.5 million for the three months ended September 30, 2004, from the comparable period in 2003, primarily due additional business from new and

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existing customers, offset by a contractual price reduction to Ford effective August 1, 2004, and reduced volumes from established and stable help desks such as DaimlerChrysler.

Revenue generated in Europe increased 47.9% to \$10.8 million for the three months ended September 30, 2004, from \$7.32 million for the comparable period in 2003, primarily due to growth in business at our Belgian and Swedish subsidiaries, our acquisition of A.N.E., and the strengthening of European currencies relative to the U.S. dollar, partially offset by a contractual price reduction to Ford effective August 1, 2004. Excluding revenue contributed by A.N.E., revenue generated in Europe increased 26.6% to \$9.26 million for the three months ended September 30, 2004, from the comparable period in 2003. If revenue in Europe for the three months ended September 30, 2004 were translated at the average exchange rate for the comparable period in 2003, reported revenue would have been reduced by approximately \$834,000 for the three months ended September 30, 2004. Within Europe, revenue from our Belgian operation increased 67.5% to \$7.66 million for the three months ended September 30, 2004, from \$4.57 million for the comparable period in 2003, primarily due to additional business from new customers, the strengthening of the euro relative to the U.S. dollar, and our acquisition of A.N.E.

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Excluding revenue contributed by A.N.E., revenue generated in Belgium increased 33.4% to \$6.10 million for the three months ended September 30, 2004, from the comparable period in 2003. If revenue in Belgium for three months ended September 30, 2004 were translated at the average exchange rate for the comparable period in 2003, reported revenue would have been reduced by approximately \$487,000 for the three months ended September 30, 2004. Since most of the Company's international operating expenses are also incurred in the same foreign currencies in which the associated revenue is denominated, the net impact of exchange rate fluctuations on gross profit and operating income is considerably less than the estimated impact on revenue.

Under our contract with Ford for its global help desk, we provide corporate help desk services on a fixed-price-per-seat, or "managed service," basis. Under the contract, we were required to reduce the price of our services on a per-seat basis effective August 1, 2004. The contract also provides for an adjustment to the number of seats that we are compensated for supporting at Ford, adjusted up or down and applied prospectively, effective August 1, 2004. We estimate that the combination of these two events resulted in a decrease in consolidated monthly revenue of approximately \$225,000 - \$250,000 since August 1, 2004. We expect to offset the majority of the reduction in revenue with continued growth in the Ford Global Help Desk. Revenue from the Ford Global Help Desk for the nine months ended September 30, 2004 is approximately \$1.2 million greater than revenue for the comparable period in 2003.

| THREE MONTHS ENDED SEPTEMBER 30, | | | | |
|------------------------------------|-------------------|--------|-------------------|------------------------|
| 2004 | | 2003 | | |
| AMOUNT | GROSS MARGIN % | AMOUNT | GROSS MARGIN % | INCREASE (DECREASE) |
| (In thousands, except percentages) | | | | |
| GROSS PROFIT (LOSS) | | | | |
| Corporate services: | | | | |

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| | | | | | |
|---|----------|-------|----------|---------|----------|
| Corporate help desk services ... | \$ 4,898 | 25.4% | \$ 3,522 | 20.5% | \$ 1,376 |
| Professional services/ systems integration | 2,671 | 20.8% | 600 | 26.8% | 2,071 |
| Technical staffing | 300 | 16.8% | 436 | 19.5% | (136) |
| Training programs | 22 | 16.5% | 36 | 16.9% | (14) |
| | ----- | | ----- | | ----- |
| Total corporate services | 7,891 | 23.2% | 4,594 | 21.0% | 3,297 |
| Leasing operations | 34 | 36.2% | (343) | (83.9)% | 377 |
| | ----- | | ----- | | ----- |
| Total gross profit | \$ 7,925 | 23.2% | \$ 4,251 | 19.1% | \$ 3,674 |
| | ===== | | ===== | | ===== |

Gross profit from corporate help desk services increased 39.1% to \$4.90 million for the three months ended September 30, 2004, from \$3.52 million for the comparable period in 2003. Gross margin from corporate help desk services increased to 25.4% for the three months ended September 30, 2004, from 20.5% for the comparable period in 2003. The increase in gross profit dollars and gross margin was primarily due to realization of the aforementioned operational efficiencies from re-aligning our cost structure, expanding our help desk capabilities in Europe, and increased business with new and existing customers. These improvements were partially offset by the impact of reductions in revenue under our Ford contract, as discussed earlier in this section. We estimate that the combination of a reduced price per seat and reduced number of seats being supported on our Ford contract reduced our gross margin on corporate help desk services by 50 - 100 basis points and our overall gross margin on corporate services by 30 - 60 basis points for the three months ended September 30, 2004. We expect to offset a portion of the reduction in gross profit through additional business from Ford and our management of costs; however, we can give no assurances in this regard.

Gross profit from professional services/systems integration increased 345% to \$2.67 million for the three months ended September 30, 2004, from \$600,000 for the comparable period in 2003. Gross margin from professional services/systems integration decreased to 20.8% for the three months ended September 30, 2004, from 26.8% for the comparable period in 2003. The increase in gross profit dollars and decrease in gross margin was primarily due to our acquisitions of DSC and A.N.E., and more specifically, lower margin hardware sales. Excluding the gross profit contributed by DSC and A.N.E., gross profit decreased 3.2% to \$581,000 and gross margin decreased to 22.8% for the three months ended September 30, 2004, from 26.8% for the comparable period in 2003, primarily due to a temporary delay in the implementation of certain projects by one customer. These delayed projects are in

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operation. As noted, gross margin from professional services/systems integration was negatively affected by hardware sales at DSC and A.N.E. of approximately \$4.26 million for the three months ended September 30, 2004. Excluding these hardware sales, gross margin from professional services/systems integration was 27.0% for the three months ended September 30, 2004.

Gross profit from technical staffing decreased 31.2% to \$300,000 for the three months ended September 30, 2004, from \$436,000 for the comparable period in 2003, which is consistent with the decrease in technical staffing revenue.

THREE MONTHS ENDED
SEPTEMBER 30,

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| | 2004 | 2003 | INCREASE (DECREASE) | %CHANGE |
|--|----------|----------|------------------------|----------|
| (In thousands) | | | | |
| OPERATING EXPENSES AND OTHER | | | | |
| Selling, general, and administrative expense ... | \$ 5,781 | \$ 4,703 | \$ 1,078 | 22.9% |
| Net interest income | \$ 175 | \$ 388 | \$ (213) | (54.9)% |
| Foreign currency transaction gain (loss) | \$ (50) | \$ 86 | \$ (136) | (158.1)% |
| Income tax provision | \$ 751 | \$ 453 | \$ 298 | 65.8% |

Selling, general, and administrative expense increased 22.9% to \$5.78 million, or 16.9% of total revenue, for the three months ended September 30, 2004, from \$4.70 million, or 21.1% of total revenue, for the comparable period in 2003, primarily due to our acquisition of DSC and A.N.E. and expense related to the Company's incentive compensation plans. Excluding revenue and expenses contributed by DSC and A.N.E., selling, general, and administrative expense decreased \$26,000 to \$4.68 million, or 19.6% of total revenue, for the three months ended September 30, 2004. Expenses have increased to support revenue growth and expansion in Romania, but expenses as a percentage of revenue have decreased due to efforts to control costs in all areas of the Company and reduced overall depreciation and amortization expense of \$196,000 for the three months ended September 30, 2004, as certain assets have become fully depreciated or amortized. Under the Company's incentive compensation plans which were effective January 1, 2004, certain members of management are entitled to bonuses if specific revenue and operating income targets are met for 2004. Under these plans, we accrued \$336,000 of expense for the three months ended September 30, 2004, of which \$269,000 was accrued to selling, general, and administrative expense and \$67,000 was accrued to cost of services delivered.

Net interest income decreased to \$175,000 for the three months ended September 30, 2004, from \$388,000 for the comparable period in 2003, due to higher average cash balances maintained in 2003 and interest income received in 2003 related to a tax refund.

Foreign currency transaction gain (loss) decreased to a loss of \$(50,000) for the three months ended September 30, 2004, from a gain of \$86,000 for the comparable period in 2003, primarily due to the U.S. dollar strengthening since December 31, 2003 relative to the euro and British pound sterling whereas the U.S. dollar weakened relative to the euro and pound sterling in the three months ended September 30, 2003.

The consolidated effective tax rate in 2004 and 2003 differs from the statutory tax rate of 34% primarily due to recognizing a favorable tax benefit from a change in estimate regarding the Company's tax liabilities for prior years, which is partially offset by the unfavorable tax effect of providing a valuation allowance against the future tax benefit of operating loss carryforwards in certain foreign tax jurisdictions.

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RESULTS OF OPERATIONS

NINE MONTHS ENDED SEPTEMBER 30, 2004 COMPARED TO SEPTEMBER 30, 2003

| NINE MONTHS ENDED SEPTEMBER 30, | INCREASE | % |
|------------------------------------|----------|---|
|------------------------------------|----------|---|

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| | 2004 | 2003 | (DECREASE) | CHANGE |
|--|----------------|-----------|------------|---------|
| | ----- | ----- | ----- | ----- |
| | (In thousands) | | | |
| REVENUE | | | | |
| Corporate services: | | | | |
| Corporate help desk services | \$ 57,289 | \$ 49,677 | \$ 7,612 | 15.3% |
| Professional services/systems integration..... | 31,176 | 6,524 | 24,652 | 377.9% |
| Technical staffing | 5,767 | 7,011 | (1,244) | (17.7)% |
| Training programs | 440 | 674 | (234) | (34.7)% |
| | ----- | ----- | ----- | |
| Total corporate services | 94,672 | 63,886 | 30,786 | 48.2% |
| Leasing operations | 397 | 2,101 | (1,704) | (81.1)% |
| | ----- | ----- | ----- | |
| Total revenue | \$ 95,069 | \$ 65,987 | \$ 29,082 | 44.1% |
| | ===== | ===== | ===== | |

Revenue from corporate help desk services increased 15.3% to \$57.3 million for the nine months ended September 30, 2004, from \$49.7 million for the comparable period in 2003, primarily due to additional business from new customers in Europe and the strengthening of the euro, British pound sterling, and Swedish kroner relative to the U.S. dollar. Revenue from professional services/systems integration increased 378% to \$31.2 million for the nine months ended September 30, 2004, from \$6.52 million for the comparable period in 2003, due to our acquisitions of DSC and A.N.E. and additional business from existing customers. Excluding revenue contributed by DSC and A.N.E., professional services/systems integration revenue increased 13.6% to \$7.41 million for the nine months ended September 30, 2004, from the comparable period in 2003. Revenue from technical staffing services decreased 17.7% to \$5.77 million for the nine months ended September 30, 2004, from \$7.01 million for the comparable period in 2003, primarily due to staffing reductions in the United States, which were only partially offset by additional business received in Europe.

Revenue from leasing operations decreased 81.1% to \$397,000 for the nine months ended September 30, 2004, from \$2.10 million for the comparable period in 2003. The decline in leasing operations revenue was the result of our decision in March 2000 to discontinue actively seeking new leasing business and to commence the wind down of our lease portfolio. The trend of declining revenue from our leasing operations will continue.

Revenue generated in the United States increased 42.0% to \$66.1 million for the nine months ended September 30, 2004, from \$46.5 million for the comparable period in 2003, due to our acquisition of DSC. Excluding revenue contributed by DSC and our leasing operations, revenue generated in the United States decreased 0.7% to \$44.1 million for the nine months ended September 30, 2004, from \$44.4 million for the comparable period in 2003, primarily due additional business from new and existing customers, offset by a contractual price reduction to Ford effective August 1, 2004, and reduced volumes from established and stable help desks such as DaimlerChrysler, as discussed in the Overview of this section.

Revenue generated in Europe increased 49.0% to \$29.0 million for the nine months ended September 30, 2004, from \$19.5 million for the comparable period in 2003, primarily due to growth in business at our Belgian and Swedish subsidiaries, our acquisition of A.N.E., and the strengthening of European currencies relative to the U.S. dollar. Excluding revenue contributed by A.N.E., revenue generated in Europe increased 37.7% to \$26.8 million for the nine months ended September 30, 2004, from the comparable period in 2003. If revenue in Europe for the nine months ended September 30, 2004 were translated at the average exchange rate for the comparable period in 2003, reported revenue would have been reduced by approximately \$2.59 million for the nine months ended September 30, 2004. Within Europe, revenue from our Belgian operation increased 55.7% to \$18.6 million for

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the nine months ended September 30, 2004, from \$12.0 million for the comparable period in 2003, primarily due to additional business from new and existing customers, such as our recently-announced contract with Proximus; our acquisition of A.N.E.; and the strengthening of the euro relative to the U.S. dollar. Excluding revenue contributed by A.N.E., revenue generated in Belgium increased 37.2% to \$16.4 million for the nine months ended

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September 30, 2004, from the comparable period in 2003. If revenue in Belgium for the nine months ended September 30, 2004 were translated at the average exchange rate for the comparable period in 2003, reported revenue would have been reduced by approximately \$1.53 million for the nine months ended September 30, 2004. Since most of the Company's international operating expenses are also incurred in the same foreign currencies in which the associated revenue is denominated, the net impact of exchange rate fluctuations on gross profit and operating income is considerably less than the estimated impact on revenue.

| NINE MONTHS ENDED SEPTEMBER 30, | | | | | |
|---|-------------------|--------|-------------------|---------------------|----------|
| 2004 | | 2003 | | | |
| AMOUNT | GROSS MARGIN % | AMOUNT | GROSS MARGIN % | INCREAS (DECREAS | |
| (In thousands, except percentages) | | | | | |
| GROSS PROFIT (LOSS) | | | | | |
| Corporate services: | | | | | |
| Corporate help desk services | \$ 14,939 | 26.1% | \$ 10,417 | 21.0% | \$ 4,52 |
| Professional services/ systems integration | 6,865 | 22.0% | 1,678 | 25.7% | 5,18 |
| Technical staffing | 1,141 | 19.8% | 1,450 | 20.7% | (30 |
| Training programs | 93 | 21.1% | 116 | 17.2% | (2 |
| Total corporate services | 23,038 | 24.3% | 13,661 | 21.4% | 9,37 |
| Leasing operations | 92 | 23.2% | (1,692) | (80.5)% | 1,78 |
| Total gross profit | \$ 23,130 | 24.3% | \$ 11,969 | 18.1% | \$ 11,16 |

Gross profit from corporate help desk services increased 43.4% to \$14.9 million for the nine months ended September 30, 2004, from \$10.4 million for the comparable period in 2003. Gross margin from corporate help desk services increased to 26.1% for the nine months ended September 30, 2004, from 21.0% for the comparable period in 2003. The increase in gross profit dollars and gross margin was primarily due to realization of the aforementioned operational efficiencies and cost savings from re-aligning our cost structure and expanding our help desk capabilities in Europe, and increased business with new and existing customers. These improvements were partially offset by the impact of reductions in revenue under our Ford contract, as discussed earlier in this section. We estimate that the combination of a reduced price per seat and reduced number of seats being supported on our Ford contract reduced our gross margin on corporate help desk services by less than 30 basis points and our overall gross margin on corporate services by less than 20 basis points for the nine months ended September 30, 2004. We expect to offset a portion of the reduction in gross profit through additional business from Ford and our

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management of costs; however, we can give no assurances in this regard.

Gross profit from professional services/systems integration increased 309% to \$6.87 million for the nine months ended September 30, 2004, from \$1.68 million for the comparable period in 2003. Gross margin from professional services/systems integration decreased to 22.0% for the nine months ended September 30, 2004, from 25.7% for the comparable period in 2003. The increase in gross profit dollars and decrease in gross margin was primarily due to our acquisitions of DSC and A.N.E., and more specifically, lower margin hardware sales. Excluding the gross profit contributed by DSC and A.N.E., gross profit increased 10.7% to \$1.86 million and gross margin decreased to 25.1% for the nine months ended September 30, 2004, from 25.7% for the comparable period in 2003, primarily due to a temporary delay in the implementation of certain projects by one customer during the third quarter. These delayed projects are in operation. As noted, gross margin from professional services/systems integration was negatively affected by hardware sales of approximately \$6.93 million for the nine months ended September 30, 2004. Excluding these hardware sales, gross margin from professional services/systems integration was 26.5% for the nine months ended September 30, 2004.

Gross profit from technical staffing decreased 21.3% to \$1.41 million for the nine months ended September 30, 2004, from \$1.45 million for the comparable period in 2003, which is consistent with the decrease in technical staffing revenue.

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Gross profit from leasing operations increased to \$92,000 for the nine months ended September 30, 2004, from a gross loss of \$(1.69) million for the comparable period in 2003, primarily due to charges of \$1.65 million for the write-down of off-lease equipment inventories and assets under lease in 2003. During 2003, we determined that we would not be able to obtain the value previously expected from the sale of off-lease equipment inventories due to a significant decline in the fair market value of the equipment in the secondary market.

| | NINE MONTHS ENDED SEPTEMBER 30, | | INCREASE (DECREASE) | % |
|--|------------------------------------|-----------|------------------------|----------|
| | 2004 | 2003 | | CHANGE |
| | (In thousands) | | | |
| OPERATING EXPENSES AND OTHER | | | | |
| Selling, general, and administrative expense ... | \$ 17,986 | \$ 14,630 | \$ 3,356 | 22.9% |
| Net interest income | \$ 464 | \$ 875 | \$ (411) | (47.0)% |
| Foreign currency transaction gain (loss) | \$ (268) | \$ 449 | \$ (717) | (159.7)% |
| Income tax provision | \$ 2,122 | \$ 459 | \$ 1,663 | 362.3% |

Selling, general, and administrative expense increased 22.9% to \$18.0 million, or 18.9% of total revenue, for the nine months ended September 30, 2004, from \$14.6 million, or 22.2% of total revenue, for the comparable period in 2003, primarily due to our acquisition of DSC and A.N.E. and expense related to the Company's incentive compensation plans. Excluding revenue and expenses contributed by DSC and A.N.E., selling, general, and administrative expense increased 2.9% to \$15.1 million, or 21.1% of total revenue, for the nine months ended September 30, 2004. Expenses have increased to support revenue growth and

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expansion in Romania, but expenses as a percentage of revenue have decreased due to efforts to control costs in all areas of the Company and reduced overall depreciation and amortization expense of \$1.23 million for the nine months ended September 30, 2004, as certain assets have become fully depreciated or amortized. Under the Company's incentive compensation plans which were effective January 1, 2004, certain members of management are entitled to bonuses if specific revenue and operating income targets are met for 2004. Under these plans, we accrued \$729,000 of expense for the nine months ended September 30, 2004, of which \$577,000 was accrued to selling, general, and administrative expense and \$152,000 was accrued to cost of services delivered.

Net interest income decreased to \$464,000 for the nine months ended September 30, 2004, from \$875,000 for the comparable period in 2003, due to higher average cash balances maintained in 2003.

Foreign currency transaction gain (loss) decreased to a loss of \$(268,000) for the nine months ended September 30, 2004, from a gain of \$449,000 for the comparable period in 2003, primarily due to the U.S. dollar strengthening since December 31, 2003 relative to the euro, British pound sterling, and Swedish kroner whereas the U.S. dollar weakened relative to the euro, pound sterling, and Swedish kroner in the nine months ended September 30, 2003.

The consolidated effective tax rate in 2004 and 2003 differs from the statutory tax rate of 34% primarily due to providing a valuation allowance against the future tax benefit of operating loss carryforwards in certain tax jurisdictions.

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NEW ACCOUNTING PRONOUNCEMENTS

The Financial Accounting Standards Board has issued an Exposure Draft, Share-Based Payment - an Amendment of FASB Statements No. 123 and 95, and is expected to issue a final Statement by December 31, 2004. The proposed Statement would eliminate the ability to account for share-based compensation transactions using APB 25, and generally would require instead that such transactions be accounted for using a fair-value-based method. This Statement is expected to be effective for the Company for awards that are granted, modified, or settled in periods beginning after June 15, 2005, or the Company's third quarter. As we use the fair value method of accounting under the original provisions of SFAS 123 for pro forma disclosure purposes, we are also required to apply the provisions of this Statement in recognizing compensation cost for any portion of awards granted or modified after December 15, 1994, that are not yet vested at the date this Statement is adopted. Based on the number of non-vested stock options the Company has outstanding at September 30, 2004, adoption of this Statement will not have a material affect on our financial position or operating results.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents were \$40.1 million at September 30, 2004, as compared to \$35.2 million at December 31, 2003. During the nine months ended September 30, 2004, cash and cash equivalents increased \$4.91 million primarily due to \$9.65 million in cash provided by operations and \$1.09 million in proceeds from the exercise of stock options, offset by \$2.74 million in cash used to repurchase 350,000 shares of our common stock under our stock repurchase program, \$831,000 in cash used to acquire A.N.E., \$205,000 in cash used to pay expenses related to our acquisition of DSC, \$1.25 million in cash used for capital expenditures, and \$1.04 million in payments on long-term debt, primarily related to notes payable acquired in our acquisitions of DSC and A.N.E.

A significant source of operating cash flow of \$9.65 million for the nine months

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ended September 30, 2004 was generated by income prior to non-cash charges for depreciation and amortization of \$6.57 million. An additional source of operating cash flow resulted from converting working capital to cash as current liabilities less notes payable increased greater than current assets less cash and cash equivalents.

In February 2004, we announced a new stock repurchase program to repurchase up to 1,000,000 shares of the Company's common stock. Under this program, we purchased 350,000 shares of our common stock from a director of the Company and his immediate family for \$7.84 per share, inclusive of sales commission expense, during the first quarter of 2004. There were no stock repurchases during the second or third quarter of 2004.

Long-term cash requirements, other than for normal operating expenses, are anticipated for the continued expansion in Europe, enhancements of existing technologies, possible repurchases of our common stock, additional consideration that is payable to the selling shareholders of DSC and A.N.E. if specific performance conditions and operating targets are met in 2004-2007, and the possible acquisition of businesses complementary to the Company's existing business. We believe that positive cash flows from operations, together with existing cash balances, will continue to be sufficient to meet our ongoing requirements for working capital, capital expenditures, and possible stock repurchases for the next twelve months and foreseeable future. We have historically not paid dividends.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

There have been no changes in the selection and application of critical accounting policies and estimates disclosed in Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2003.

FACTORS INFLUENCING FUTURE RESULTS

Refer to Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2003.

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ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in reported market risks since December 31, 2003.

ITEM 4 -- CONTROLS AND PROCEDURES

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

During the first quarter of 2004, the Company converted its accounting and financial reporting system in Europe, with the exception of Romania, to a pre-existing common information technology platform that had been deployed in the United States in prior periods. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to December 31, 2003. As of September 30,

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2004, an evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer, Chief Financial Officer, and Chief Accounting Officer of the effectiveness of the design and operations of the Company's disclosure controls and procedures. Based upon that evaluation, the Company's management, including the CEO, CFO, and CAO, concluded that the Company's disclosure controls and procedures were effective as of September 30, 2004.

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PART II -- OTHER INFORMATION

ITEM 1 -- LEGAL PROCEEDINGS

The Company is a party to various legal proceedings that are routine and incidental to its business. Although the consequences of these proceedings are not presently determinable, in the opinion of management, they will not have a material adverse affect on our liquidity, financial condition, or results of operations, although no assurances can be given in this regard.

ITEM 2 -- UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The Company purchased shares of its common stock during the six months ended September 30, 2004 as follows:

| PERIOD ----- | TOTAL NUMBER OF SHARES PURCHASED ----- | AVERAGE PRICE PAID PER SHARE ----- | TOTAL NUMBER OF SHARES PURCHASED AS PART OF PUBLICLY ANNOUNCED PROGRAMS ----- |
|---|---|---|--|
| July 1, 2004 to July 31, 2004 | -- | -- | -- |
| August 1, 2004 to August 31, 2004 | -- | -- | -- |
| September 1, 2004 to September 30, 2004 | -- | -- | -- |

- (a) A stock repurchase program to repurchase up to 1,000,000 shares of the Company's common stock was announced on February 18, 2004. The program expires on January 27, 2005.

ITEM 6 -- EXHIBITS

- 31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.3 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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32.3 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

ITEMS 3, 4, AND 5 ARE NOT APPLICABLE AND HAVE BEEN OMITTED

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SIGNATURES

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

TechTeam Global, Inc.

(Registrant)

/s/ William F. Coyro, Jr.

Date: November 5, 2004

By: William F. Coyro, Jr.
President and Chief Executive Officer

/s/ David W. Morgan

Date: November 5, 2004

By: David W. Morgan
Vice President, Chief Financial Officer,
and Treasurer

/s/ Marc J. Lichtman

Date: November 5, 2004

By: Marc J. Lichtman
Vice President and Chief Accounting Officer

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EXHIBIT INDEX

| EXHIBIT NUMBER | DESCRIPTION |
|----------------|---|
| ----- | ----- |
| 31.1 | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
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32.3 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002