



Six Month Report 2005

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and June 30th, 2004

Management Discussion and Analysis for the Six Months ended June 30, 2005

FORWARD LOOKING STATEMENTS

This report contains statements that involve expectations, plans or intentions relating to future business or financial results, new features or services, or management strategies. These statements are forward-looking and are subject to risks and uncertainties, so actual results may vary materially. You can identify these forward-looking statements by words such as “may,” “will,” “should,” “expect,” “anticipate,” “believe,” “estimate,” “intend,” “plan” and other similar expressions. The Company assumes no obligation to update any forward-looking statements.

Overview

About artnet

artnet.com AG was incorporated under the laws of Germany in 1998. In 1999, Management took the company public on the Neuer Markt of the Frankfurt Stock Exchange. In 2002, artnet.com AG changed its name to artnet AG. Its principal holding is its wholly owned subsidiary, Artnet Worldwide Corp., a New York corporation that was founded in 1989. On October 4, 2002, artnet AG left the Neuer Markt and is now listed at the Geregelter Market at the Frankfurt Stock Exchange.

artnet AG and Artnet Worldwide Corp. (collectively, “the Company”) operate under the trade name artnet. artnet provides services to fine art professionals that improve the economics of their businesses. The art business is international but is conducted locally by tens of thousands of geographically dispersed dealers, galleries, auction houses, print publishers, museums and collectors in a relatively inefficient marketplace. Observing the inefficiencies in the art business, artnet developed its first product, the Price Database, a historical database with now over 2.9 million artworks sold at auction, in an effort to bring price transparency to the art market. Today the Price Database has a broad base of customers composed of major auction houses, art dealers, museums, insurance companies, and collectors. In 1995, the Company transitioned the Price Database to the Internet and introduced a second product, the online Gallery Network, building and hosting websites for art dealers and galleries. An online art trade magazine edited by a veteran art journalist to draw attention to the site supplemented the online Gallery Network. Today artnet is a critical tool, providing its member dealers with global market access, significant incremental revenue opportunities, and cost-effective marketing solutions.

Impact of Foreign Currency Translation

The Company’s business is primarily conducted in U.S. dollars. Moreover, the majority of the Company’s operations are located in the U.S. However, Management provides financial information in both U.S. dollars and euros for the convenience of financial investors worldwide. Because of the weakening of the U.S. dollar, euro comparisons in the adjoining financial statements are not indicative of actual performance.

Therefore, for clarification purposes, results for categories significantly affected by the foreign exchange differential will be stated first in U.S. dollar terms, then in euro terms. Currency translation in the statement of operations is based on the average exchange rate for the period ending June 30, 2005 and 2004, respectively. For 2005, the average rate was .7783 euros/dollar as compared to .8154 euros/dollar in 2004, thus representing an exchange differential of -5%. Currency translation for the balance sheet is

based on the exchange rate at the end of the period. As of June 30, 2005, the rate was .8290 euros/dollar as compared to .7342 at December 31, 2004, thus representing an exchange differential of 13%.

Transition of group accounting to IFRS

artnet prepares the consolidated financial statement in 2005 according to International Financial Reporting Standards (IFRS). The transition to IFRS had no material effects in comparison with our former accounting according to US-GAAP.

Results of operations

For the first six months ended June 30, 2005 artnet greatly increased its profitability. artnet earned a net profit of \$701,100 compared with \$10,900 in the prior year period. The increase in profit was driven by revenue growth of 29 % whereas total operating costs only increased by 2 %. The revenue growth was primarily due to an increase in sales efforts as well as the Company operating under favorable market conditions. Additionally, the Company decreased its non-cash deferred compensation by \$245,000 due to the vesting of options related to the initial public offering in 1999.

Revenue

Total revenue was \$3,838,000 and \$2,967,000 for the six months ended June 30, 2005 and 2004, respectively, representing an increase of \$871,000 or 29%. Overall, the Company is operating under favorable market conditions that are helping the Company's growth. Additionally, the Company has increased its sales efforts as well as increased the market recognition of the brand. In euro terms, total revenue was Euro 2,987,000 and Euro 2,419,000 for the six months ended June 30, 2005 and 2004, respectively.

Online Gallery Network revenue increased by 30% to \$1,758,000 for the six months ended June 30, 2005 from \$1,348,000 in the same period a year ago. The revenue growth is primarily attributable to increased sales efforts as well as increased market recognition of the brand.

Price Database revenue increased by 27% to \$1,581,000 for the six months ended June 30, 2005 up from \$1,243,000 in the same period a year ago. The increase is primarily attributable to the implementation of advantageous pricing and new subscription offerings as well as two new products, the imageless search and Market Alert, which have resulted in increased market share.

Advertising revenue in the form of banners and tiles increased by 33% to \$499,000 for the six months ended June 30, 2005 up from \$376,000 for the same period a year ago. The increase in advertising revenue is primarily attributable to increased site traffic increased search functions on the site.

Operating Expenses

Client Service, Production, and Editorial

Client Service, Production and Editorial expenses were \$707,000 and \$492,000 for the six months ended June 30, 2005 and 2004, respectively, representing an increase of \$215,000 or 44%. This category

includes all editorial, content and production-related costs for the online Gallery Network, Price Database, and the artnet magazine. The primary costs consist of payroll, consulting fees, and customer service costs related to database production and content management. The increase is primarily due to increased staff and consultants related to the German Magazine that went live in the fourth quarter of 2004 as well as production costs to support the increase in gallery members. Additionally, Artnet increased staffing in the Price Database production department in order to support the current Sotheby's project as well as support the upcoming auctions page on the site. In euro terms, Client Service Production and Editorial expenses were Euro 550,000 and Euro 401,000 for the six months ended June 30, 2005 and 2004, respectively.

Selling and Marketing

Selling and Marketing expenses were \$537,000 and \$471,000 for the six months ended June 30, 2005 and 2004 respectively, representing an increase of \$66,000 or 14%. This category includes advertising, marketing and promotional activities, salesperson salaries and commissions, and marketing staff costs. The increase was primarily related to employee-related commission costs that increased as a result of the growth in sales. Management anticipates that as revenue increases in future periods, necessitating larger commission payments, and additional marketing resources are utilized to launch new products, expenses for this category will continue to increase. In euro terms, Selling and Marketing expenses were Euro 418,000 and Euro 384,000 for the six months ended June 30, 2005 and 2004, respectively.

General and Administrative

General and Administrative expenses were \$1,644,000 and \$1,580,000 for the six months ended June 30, 2005 and 2004 respectively, representing an increase of \$64,000 or 4%. This category includes executive and administrative salaries, professional fees, compliance costs, bad debt expense, communications costs including Internet access, and premises and facilities costs. The increase was primarily due to increased rental and facilities costs for the Berlin office, which opened at the end of 2004, as well as costs related to the renovation of the New York facility. Additionally, the increase was due to network maintenance costs related to increasing the security of the site. The increase was offset by a one-time expense in 2004, in the amount of \$85,000, related to a prior year payroll tax inquiry for New York State. In euro terms, General and Administrative expenses were Euro 1,280,000 and Euro 1,288,000 for the six months ended June 30, 2005 and 2004, respectively.

Product Development

Product Development expenses were \$164,000 and \$219,000 for the six months ended June 30, 2005 and 2004, respectively, representing a decrease of \$(55,000) or (25%). This category includes technology staff and consulting fees for new product conception, planning, and software development as well as post-implementation phases of our website development efforts. Product development expenses are net of capitalization of major site and other product development efforts. The product development expense for this period is reflective of Management's emphasis on building new products and further developing existing products to accelerate revenue growth and reduce costs in the coming years. The Company anticipates that it will continue to devote resources to product development in the future as it adds new features and functionality as well as new product lines to the site. In euro terms, Product Development expenses were Euro 128,000 and Euro 178,000 for the six months ended June 30, 2005 and 2004, respectively.

Non-Cash Compensation Expense

Non-Cash Compensation expense was \$5,000 and \$251,000 for the six months ended June 30, 2005 and 2004, respectively. Non-cash compensation expense in 2004 reflects a charge to compensation arising from a one-time grant of employee stock options with a strike price of Euro 6.72 prior to the initial public offering in 1999. The options were completely vested during the second quarter of 2004 and therefore all compensation expense related to these stock options has been recorded. Additionally, in 2004 and 2005, stock option expense was recorded related to the adoption of the new IFRS standards in which all stock options must be expensed based on their vesting period.

Depreciation and Amortization

Depreciation and Amortization expenses were \$64,000 and \$42,000 for the six months ended June 30, 2005 and 2004, respectively, representing an increase of \$22,000 or 52%. Depreciation and Amortization Expenses relate to computer equipment, software purchases, website development and leasehold improvements. The increase is primarily due to the website development and equipment purchases completed during the year 2004. In Euro terms, Depreciation and Amortization expenses were Euro 50,000 and Euro 34,000 for the six months ended June 30, 2005 and 2004, respectively.

Non Operating Items

Interest Expense

Interest expense was \$(20,100) and \$(18,500) for the six months ended June 30, 2005 and 2004, respectively, representing an increase of \$1,600. Interest expense primarily represents interest on loans due to shareholders.

Other Income, net

Other Income, net, was \$3,400 and \$110,400 for the six months ended June 30, 2005 and 2004, respectively, representing a decrease of \$107,000. In 2004, other income, net, consisted primarily of write-offs and settlements related to prior year accruals.

Asset Position, Liquidity and Capital Resources

The Company has managed to increase its positive net cash flows from operating activities from \$ 202,000 in 2004 to \$ 665,000 in 2005. The net cash flows used for investing activities were \$158,000 and \$216,000 for the six months ended June 30, 2005 and 2004, respectively. The investing activities related primarily to purchases of leasehold improvements, computer equipment and website development. The net cash flows used for financing activities were \$41,000 and \$(45,000) for the six months ended June 30, 2005 and 2004, respectively, and related primarily to loan repayments as well as foreign currency translation adjustments.

Because of the positive operating cash flows the cash resources of artnet increased from \$393,000 as at December 31, 2004, to \$934,000 as at June 30, 2005.

Other information

As of June 30, 2005 and 2004 the company had 41 full time employees.

The employees of artnet held 219,250 stock options as of June 30, 2005, of which 172,750 were exercisable. Of these 219,250 stock options the management of Artnet Worldwide Corp. held 150,000 as of June 30, 2005, of which 128,500 were exercisable.

artnet held 78,081 treasury shares of stock representing 1.4 % of the common stock as of June 30, 2005 and December 31, 2004.

Outlook

The Company expects that continued growth in revenues during 2005 will result primarily from increased advertising and growth in the online Gallery Network as well as from new products such as Market Alert and the Imageless Price Database search. The Company's venture in providing historical results alongside Sotheby's auction lots has resulted in increased Price Database subscription awareness and is anticipated to continue to increase the Company's profile with art investors and thus continue growth in this product.

The Company expects to continue its investment in the business as well as strive for cost and operational efficiencies in order to help the Company achieve its long-term growth objectives. The Company anticipates continued investment in the areas of Selling and Marketing as well as Product Development and corporate infrastructure. The Company believes these investments are necessary to support the long-term demands of its growing business. With the introduction of new products, additional selling and marketing resources, and continued focus on revenue enhancement, Management continues strive for financial gain in 2005.

artnet AG
CONSOLIDATED BALANCE SHEETS
As of June 30, 2005 and December 31, 2004

	6/30/2005 Consolidated USD	12/31/2004 Consolidated USD	6/30/2005 Consolidated EURO	12/31/2004 Consolidated EURO
<u>CURRENT ASSETS</u>				
Cash and cash equivalents	\$ 934,226	\$ 392,510	774,473	288,165
Accounts receivable-net	669,322	698,134	554,868	512,542
Prepays and other current assets	<u>162,320</u>	<u>104,469</u>	<u>134,563</u>	<u>76,696</u>
Total current assets	1,765,868	1,195,113	1,463,904	877,403
PROPERTY AND EQUIPMENT, Net	190,632	132,430	158,034	97,225
<u>OTHER ASSETS</u>				
Intangible assets	107,438	94,016	89,066	69,023
Security deposit	185,202	185,202	153,532	135,968
Due from shareholder	<u>196,837</u>	<u>171,511</u>	<u>163,178</u>	<u>125,917</u>
Total other assets	<u>489,477</u>	<u>450,729</u>	<u>405,776</u>	<u>330,908</u>
TOTAL ASSETS	<u>\$ 2,445,977</u>	<u>\$ 1,778,272</u>	<u>2,027,714</u>	<u>1,305,536</u>
<u>LIABILITIES AND SHAREHOLDER'S DEFICIT</u>				
<u>CURRENT LIABILITIES</u>				
Accounts payable	\$ 802,637	\$ 930,638	665,386	683,240
Accrued expenses	633,302	702,487	525,007	515,738
Due to shareholder	416,906	532,001	345,615	390,574
Unearned revenue	<u>1,176,003</u>	<u>1,052,008</u>	<u>974,906</u>	<u>772,343</u>
TOTAL LIABILITIES	<u>3,028,848</u>	<u>3,217,134</u>	<u>2,510,914</u>	<u>2,361,895</u>
<u>SHAREHOLDERS' DEFICIT</u>				
Common stock	5,941,512	5,941,512	5,631,067	5,631,067
Treasury stock	(269,241)	(269,241)	(264,425)	(264,425)
Additional paid-in capital	51,321,936	51,316,497	50,184,806	50,180,573
Accumulated deficit	(55,819,980)	(55,175,190)	(54,122,681)	(53,604,303)
Current income/(loss)	701,103	(644,790)	545,449	(518,378)
Foreign currency translation adjustment	<u>(2,458,201)</u>	<u>(2,607,650)</u>	<u>(2,457,416)</u>	<u>(2,480,893)</u>
TOTAL SHAREHOLDERS' DEFICIT	<u>(582,871)</u>	<u>(1,438,862)</u>	<u>(483,200)</u>	<u>(1,056,359)</u>
TOTAL LIABILITIES AND SHAREHOLDERS' DEFICIT	<u>\$ 2,445,977</u>	<u>\$ 1,778,272</u>	<u>2,027,714</u>	<u>1,305,536</u>

artnet AG
CONSOLIDATED STATEMENTS OF OPERATIONS

	For the Six Months ended June 30, 2005 and 2004				For the Three Months ended June 30, 2005 and 2004			
	6/30/2005 Consolidated USD	6/30/2004 Consolidated USD	6/30/2005 Consolidated EURO	6/30/2004 Consolidated EURO	6/30/2005 Consolidated USD	6/30/2004 Consolidated USD	6/30/2005 Consolidated EURO	6/30/2004 Consolidated EURO
REVENUE								
Online Gallery Network	\$ 1,757,610	\$ 1,348,143	1,367,930	1,099,303	\$ 910,751	\$ 707,236	708,828	576,694
Price Database	1,581,350	1,242,885	1,230,749	1,013,472	812,203	603,133	632,129	491,807
Advertising	<u>498,556</u>	<u>376,126</u>	<u>388,021</u>	<u>306,700</u>	<u>267,524</u>	<u>181,901</u>	<u>208,211</u>	<u>148,325</u>
TOTAL REVENUE	<u>3,837,516</u>	<u>2,967,154</u>	<u>2,986,700</u>	<u>2,419,475</u>	<u>1,990,478</u>	<u>1,492,270</u>	<u>1,549,168</u>	<u>1,216,826</u>
OPERATING EXPENSES								
Client Service, Production and Editorial	706,786	491,910	550,084	401,113	346,351	251,033	269,562	204,697
Selling and Marketing	536,699	470,509	417,707	383,659	268,598	214,269	209,047	174,719
General and Administrative	1,644,220	1,580,153	1,279,893	1,288,490	873,055	923,013	679,490	752,642
Product Development	164,049	218,834	127,678	178,442	73,464	112,427	57,176	91,676
Noncash Compensation Expense	5,439	251,388	4,233	204,987	4,126	62,847	3,211	51,247
Depreciation and Amortization	<u>64,041</u>	<u>41,611</u>	<u>49,842</u>	<u>33,930</u>	<u>31,882</u>	<u>21,571</u>	<u>24,813</u>	<u>17,589</u>
			--					
TOTAL OPERATING EXPENSES	<u>3,121,234</u>	<u>3,054,405</u>	<u>2,429,437</u>	<u>2,490,621</u>	<u>1,597,476</u>	<u>1,585,160</u>	<u>1,243,299</u>	<u>1,292,570</u>
INCOME FROM OPERATIONS	716,282	(87,251)	557,263	(71,146)	393,002	(92,890)	305,869	(75,744)
INTEREST EXPENSE	(20,118)	(18,496)	(15,658)	(15,081)	(10,281)	(9,074)	(8,002)	(7,399)
INTEREST INCOME	1,497	6,156	1,165	5,019	1,057	2,205	823	1,798
OTHER INCOME	<u>3,442</u>	<u>110,439</u>	<u>2,679</u>	<u>90,054</u>	<u>1,686</u>	<u>30,250</u>	<u>1,312</u>	<u>24,666</u>
INCOME FROM OPERATIONS BEFORE PROVISION FOR INCOME TAXES	<u>701,103</u>	<u>10,848</u>	<u>545,449</u>	<u>8,846</u>	<u>385,464</u>	<u>(69,509)</u>	<u>300,002</u>	<u>(56,679)</u>
INCOME TAX PROVISION	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>
NET INCOME/(LOSS)	<u>\$ 701,103</u>	<u>\$ 10,848</u>	<u>545,449</u>	<u>8,846</u>	<u>\$ 385,464</u>	<u>\$ (69,509)</u>	<u>300,002</u>	<u>(56,679)</u>
Net Income/(Loss) Per Share Attributable to Common Shareholders:								
Net Income/(Loss) (Basic and Diluted)	<u>0.13</u>	<u>0.00</u>	<u>0.10</u>	<u>0.00</u>	<u>0.07</u>	<u>(0.01)</u>	<u>0.05</u>	<u>(0.01)</u>
Weighted Average Common and Common Equivalent Shares Outstanding:								
Basic	<u>5,552,986</u>	<u>5,482,867</u>	<u>5,552,986</u>	<u>5,482,867</u>	<u>5,552,986</u>	<u>5,482,867</u>	<u>5,552,986</u>	<u>5,482,867</u>
Diluted	<u>5,552,986</u>	<u>5,482,867</u>	<u>5,552,986</u>	<u>5,482,867</u>	<u>5,552,986</u>	<u>5,482,867</u>	<u>5,552,986</u>	<u>5,482,867</u>

artnet AG
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' DEFICIENCY (USD)
For the Periods Ended June 30, 2005 and December 31, 2004

	Common Stock		Additional Paid-in Capital	Treasury Stock	Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
	Shares Issued	Amount						
<u>BALANCE - DECEMBER 31, 2003</u>	<u>5,631,067</u>	<u>5,941,512</u>	<u>56,222,097</u>	<u>(455,631)</u>	<u>(5,166,738)</u>	<u>(55,033,533)</u>	<u>(2,486,672)</u>	<u>(978,965)</u>
Net (Loss)						(644,790)		(644,790)
Foreign Currency Translation							(120,978)	(120,978)
Sale of Treasury stock				186,390		(131,907)		54,483
Non-cash Compensation			9,750		251,388	(9,750)		251,388
Unearned deferred compensation			(4,915,350)		4,915,350			-
<u>BALANCE - DECEMBER 31, 2004</u>	<u>5,631,067</u>	<u>5,941,512</u>	<u>51,316,497</u>	<u>(269,241)</u>	<u>--</u>	<u>(55,819,980)</u>	<u>(2,607,650)</u>	<u>(1,438,862)</u>
Net Income						701,103		701,103
Foreign Currency Translation							149,449	149,449
Sale of Treasury stock								-
Non-cash Compensation			5,439					5,439
<u>BALANCE - JUNE 30, 2005</u>	<u>5,631,067</u>	<u>5,941,512</u>	<u>51,321,936</u>	<u>(269,241)</u>	<u>--</u>	<u>(55,118,877)</u>	<u>(2,458,201)</u>	<u>(582,871)</u>

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CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' DEFICIENCY (EURO)
For the Periods Ended June 30, 2005 and December 31, 2004

	Common Stock		Additional Paid-in Capital	Treasury Stock	Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
	Shares Issued	Amount						
<u>BALANCE - DECEMBER 31, 2003</u>	<u>5,631,067</u>	<u>5,631,067</u>	<u>54,170,003</u>	<u>(447,481)</u>	<u>(4,199,158)</u>	<u>(53,453,409)</u>	<u>(2,480,641)</u>	<u>(779,619)</u>
Net (Loss)						(518,378)		(518,378)
Foreign Currency Translation							(252)	(252)
Sale of Treasury Stock				183,056		(143,056)		40,000
Non-cash Compensation			7,838		201,890	(7,838)		201,890
Unearned deferred compensation			(3,997,268)		3,997,268			--
<u>BALANCE - DECEMBER 31, 2004</u>	<u>5,631,067</u>	<u>5,631,067</u>	<u>50,180,573</u>	<u>(264,425)</u>	<u>--</u>	<u>(54,122,681)</u>	<u>(2,480,893)</u>	<u>(1,056,359)</u>
Net Income						545,449		545,449
Foreign Currency Translation							23,477	23,477
Sale of Treasury Stock								--
Non-cash Compensation			4,233					4,233
<u>BALANCE - JUNE 30, 2005</u>	<u>5,631,067</u>	<u>5,631,067</u>	<u>50,184,806</u>	<u>(264,425)</u>	<u>--</u>	<u>(53,577,232)</u>	<u>(2,457,416)</u>	<u>(483,200)</u>

artnet AG
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Six Months Ended June 30, 2005 and 2004

	6/30/2005 Consolidated <u>USD</u>	6/30/2004 Consolidated <u>USD</u>	6/30/2005 Consolidated <u>EURO</u>	6/30/2004 Consolidated <u>EURO</u>
<u>CASH FLOWS FROM OPERATING ACTIVITIES</u>				
Net Income	\$ 701,103	\$ 10,848	545,449	8,847
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Depreciation and amortization	60,701	41,611	47,243	33,930
Provision for doubtful accounts	17,787	(35,601)	13,843	(29,030)
Non-cash compensation	5,439	251,388	4,233	204,987
Changes in operating assets and liabilities:				
Accounts receivable	11,025	56,669	(56,169)	25,648
Prepaid and other current assets	(57,851)	(31,774)	(57,867)	(29,014)
Security deposits	--	--	(17,564)	(7,834)
Accounts payable	(128,001)	(126,108)	(34,120)	(82,079)
Accrued expenses	(69,185)	35,806	9,269	47,317
Deferred Revenue	123,995	(413)	202,563	29,107
TOTAL ADJUSTMENTS	(36,090)	191,578	111,431	193,032
NET CASH PROVIDED BY OPERATING ACTIVITIES	665,013	202,426	656,880	201,879
<u>CASH FLOWS FROM INVESTING ACTIVITIES</u>				
Purchase of property and equipment	(93,604)	(31,382)	(72,851)	(28,663)
Purchase of intangible assets	(38,721)	(42,575)	(30,136)	(36,673)
Receivables from shareholder, advance	(25,326)	(142,411)	(20,995)	(127,414)
NET CASH USED IN INVESTING ACTIVITIES	\$ (157,651)	\$ (216,368)	(123,982)	\$ (192,750)
<u>CASH FLOWS FROM FINANCING ACTIVITIES</u>				
Loan Payments to Shareholders	(57,766)	(30,188)	(44,959)	(24,986)
Change in foreign currency translation adjustment	98,403	(14,511)	(33,648)	(34,416)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	40,637	(44,699)	(78,607)	(59,402)
Effects of exchange rate changes on cash	(6,283)	(2,098)	32,017	10,160
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	541,716	(60,739)	486,308	(40,113)
<u>CASH – Beginning</u>	392,510	324,467	288,165	258,395
<u>CASH – Ending</u>	\$ 934,226	\$ 263,728	774,473	218,282