

CSP Inc.
43 Manning Road
Billerica, MA 01821
(800) 325-3110 / (978) 663-7598
Fax: (978) 663-0150
www.cspi.com



Dear Shareholders,

Fiscal 2009 turned out to be two different years in many respects. The year began on a strong note, with CSP reporting solid results for the first two quarters while the worldwide recession deepened. Our revenue growth slowed dramatically in the second half as the economic downturn finally began triggering cuts in IT spending. Nonetheless, both our Systems and our Service and Systems Integration businesses posted revenue growth for the full fiscal year. CSP's sales in fiscal 2009 increased 9% from a year earlier, or 13% adjusting for foreign exchange, to \$83.4 million.

In response to weakening customer demand in the second half of the fiscal year, we took decisive actions to reduce the size of our operating structure. These steps included headcount reductions at each one of our operating subsidiaries. At the same time, we continued to invest in CSP's future by focusing significant time and resources on increasing the level of higher margin offerings at our Service and Systems Integration segment.

CSP's GAAP profitability for fiscal 2009 was significantly affected by a \$3.9 million impairment charge for goodwill as a result of market and industry volatility, changes in projected forecast and the decrease in the company's market capitalization, as required under Accounting Standards Codification Topic 805. Including this charge, we reported a GAAP net loss of \$3.8 million, or \$1.05 per share, compared with a net loss of \$407,000, or \$0.11 per share, for fiscal 2008. Excluding the goodwill impairment charge, CSP's non-GAAP net loss for fiscal 2009 would have been \$321,000, or \$0.09 per share. Reflecting improved performance in working capital management, CSP's cash and short-term investments were \$18.9 million as of September 30, 2009, compared with \$18.5 million a year earlier.

As we expected, fiscal 2009 was a solid year for CSP's Systems segment. Our latest-generation FastCluster 3000 SERIES multicomputer systems precisely target airborne and naval radar, sonar and ISR (intelligence, surveillance and reconnaissance) applications where space, power, weight and cooling are at a premium and rugged design is a prerequisite. Year-over-year growth at our Systems segment was driven by follow-on orders for our high-performance digital signal processing systems, as well as high-margin royalty payments from Lockheed Martin related to the pilot phase of the E2D Advanced Hawkeye ISR aircraft. CSP's multicomputers provide radar processing that enables the E2D to deliver the critical data that warfighters require to advance their missions.

Looking ahead to fiscal 2010, we expect our Systems segment to receive high-margin royalty payments from Lockheed Martin for five additional aircraft as the E2D Hawkeye enters the Low Rate Initial Production (LRIP) Phase. We also anticipate follow-on orders from Raytheon and other key customers during the year, as we continue to advance our multicomputer technology and pursue new programs.

In our Service and Systems Integration segment, we reported sales growth for fiscal 2009 despite a difficult second half of the year, driven mainly by strong demand in the first half at our U.S. Systems and Solutions subsidiary. Early in the fiscal year, the demand environment still looked positive. We were well-positioned in our markets, augmented by the addition of the unified communications segment with our fiscal 2008 acquisition of R2 Technologies.

President's Letter continued

MODCOMP posted increased sales at each of its businesses in the first quarter of fiscal 2009. In Germany we continued to see demand for our lifecycle management, archiving and network migration professional services practice as well as our security practice. In the United States, the Systems and Solutions Division reported an outstanding first quarter as well, winning a multi-million dollar contract with a national mortgage company. Our results also benefited from a full quarter of sales from R2 Technologies. Our UK subsidiary continued to produce solid results on both the top and bottom lines in the quarter despite negative currency effects.

This momentum carried into the second quarter of fiscal 2009. Although we began to see the recessionary impacts of slowing customer purchases and pricing pressures as the quarter unfolded, the Systems and Solutions Division realized significant growth in a developing market niche focused on selling servers and storage to web hosting companies. We continued to expand our high-margin professional services business to new practice areas such as application delivery infrastructure using Citrix technology.

It was in the third and fourth quarters of fiscal 2009 that we clearly felt the impact of the global recession and its effect on IT budgets – particularly in Germany. We saw a dramatic contraction in our German subsidiary's pipeline of large installation deals, as well as pricing pressure and lower utilization rates as our customers focused on conserving cash. Demand for hardware declined, and professional service contracts were challenged by tighter customer budgets and the bankruptcy of a large customer.

Although we pared our workforce in Germany in response to the slowdown, we have continued to maintain a staff of highly experienced engineers in this market. When IT spending resumes, we expect that our professional services business will provide CSP with significant high-margin sales as well as opportunities to expand our practice areas.

While our U.S.-based Systems and Solutions Division experienced deep discounting as IT spending slowed, continued growth in this business offset the lower revenue in Germany in the second half of fiscal 2009. We continue to be optimistic about the potential for the Systems and Solutions segment to accelerate its growth when the economic rebound takes hold. Companies are increasingly buying technology as a service instead of managing their own IT infrastructure – freeing valuable time and resources to focus on their core competencies.

Looking forward to fiscal 2010, our strategy for all three of our Services and Systems Integration businesses is to focus our resources on higher margin growth opportunities. A key part of this strategy centers on increasing our higher level managed services offerings. We expect increased sales of managed services, not only to improve our margins but also to increase the number and size of our recurring revenue streams.

The Systems and Solutions Division has become a member of the Cisco Managed Services Channel Program for Managed Business Communication, Firewall, IDS/IPS, Secure Router, Router and LAN Services. We expect our participation in Cisco's program to enable us to grow our managed services business in a repeatable and predictable fashion worldwide. We are focused on building comprehensive customer solutions by integrating software and hardware into a managed service that can be run at a customer's datacenter or on our Network Operations Center (NOC). Modcomp's NOC is a competitive advantage that we plan to leverage as the global foundation for our managed services offerings.

President's Letter continued

To capitalize on the opportunities we foresee in managed services, we also are judiciously investing in enhancing our sales capabilities. For example, we are hiring engineers who can demonstrate our expertise and offer solutions during the sales process. While this focus on increasing higher margin business may put some pressure on sales in fiscal 2010, we believe that it will accelerate profitable growth for Modcomp in the long term.

Although we believe that we hit the bottom of the IT spending downturn in fiscal 2009, the near-term outlook remains difficult to forecast. Our sales force is beginning to generate growth in our new business pipeline, as well as increased customer activity. Given the continued economic uncertainty, however, we will continue to manage CSP conservatively in fiscal 2010.

Our financial priorities for fiscal 2010 include maintaining a strict control on our expenses, maintaining our focus on working capital management and continuing to make the investments necessary to drive long-term profitable growth. In the event that customer demand begins to strengthen, the improved leverage we have developed in our business positions the company for stronger financial results.

On behalf of all of us at CSP, I would like to express my sincere thanks to our suppliers and customers for the strong support they have provided this past year. I also thank you, our shareholders, for your continued confidence. We look forward to reporting further progress in fiscal 2010.

Sincerely,



Alexander R. Lupinetti
Chairman, President, and CEO
December 2009

