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ATSI COMMUNICATIONS INC/DE
Form 10-Q
June 14, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

ACT OF 1934 For the quarterly period ended April 30, 2002

or

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 0-23007

ATSI COMMUNICATIONS, INC.

(Exact name of registrant as specified in its charter)

Delaware	74-2849995
(State or other jurisdiction	(IRS Employer
of incorporation or organization)	Identification No.)

6000 Northwest Parkway, Suite 110
San Antonio, Texas 78249
(210) 547-1000

(Address, including zip code, of registrant's principal executive
offices and telephone number, including area code)

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

The number of shares outstanding of the registrant's common stock at
June 13, 2002 was 91,670,700

ATSI COMMUNICATIONS, INC.
AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED APRIL 30, 2002

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ATSI COMMUNICATIONS, INC.
 AND SUBSIDIARIES
 CONSOLIDATED BALANCE SHEETS
 (In thousands, except share information)

	July 31 2001 -----
ASSETS	

CURRENT ASSETS:	
Cash and cash equivalents	\$ 1
Accounts receivable, net of allowance of \$92 and \$46, respectively	2,6
Inventory	
Prepaid expenses & other current assets	7

Total current assets	3,6

PROPERTY AND EQUIPMENT (At cost):	21,7
Less - Accumulated depreciation and amortization	(11,9)

Net property and equipment	9,7

OTHER ASSETS, net	
Goodwill, net	4,8
Concession cost, net	4,2
Cute FTP costs, net	3
Other	4

Total assets	\$ 23,3
	=====
LIABILITIES AND STOCKHOLDERS' EQUITY	

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CURRENT LIABILITIES:

Accounts payable	4,7
Accrued liabilities	2,5
N/P current	6
Current portion of obligations under capital leases	4,9
Deferred revenue	1

Total current liabilities	12,9

LONG-TERM LIABILITIES:

Obligations under capital leases, less current portion	1
Customer deposits	1

Total long-term liabilities	2

Minority Interest 3

COMMITMENTS AND CONTINGENCIES:

REDEEMABLE PREFERRED STOCK

Series D Cumulative Convertible Preferred Stock, 3,000 shares authorized, 1,642 shares issued and outstanding at July 31, 2001, 742 shares issued and outstanding at April 30, 2002	1,3
Series E Cumulative Convertible Preferred Stock, 10,000 shares authorized, 3,490 shares issued and outstanding at July 31, 2001, 1,655 shares issued and outstanding at April 30, 2002	2,2

STOCKHOLDERS' EQUITY:

Preferred stock, \$0.001 par value, 10,000,000 shares authorized Series A Cumulative Convertible Preferred Stock, 50,000 shares authorized, 4,370 shares issued and outstanding at July 31, 2001 and January 31, 2002, respectively	
Series F Cumulative Convertible Preferred Stock, 10,000 shares authorized, 9,210 shares issued and outstanding at July 31, 2001 and 8,510 shares issued and outstanding at April 30, 2002	
Series G Cumulative Convertible Preferred Stock, 42,000 shares authorized, 6,500 shares issued and outstanding at July 31, 2001 and April 30, 2002, respectively	
Common stock, \$0.001 par value, 200,000,000 shares authorized, 77,329,379 issued and outstanding at July 31, 2001	
91,670,700 issued and outstanding at April 30, 2002	
Additional paid in capital	58,1
Accumulated deficit	(52,5
Warrants outstanding	1,8
Deferred compensation	(
Other comprehensive loss	(1,2

Total stockholders' equity	6,2

Total liabilities and stockholders' equity \$ 23,3

The accompanying notes are an integral part of these consolidated financial statements.

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ATSI COMMUNICATIONS, INC.
 AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF OPERATIONS
 (In thousands, except per share amounts)
 (unaudited)

	Three months ended April 30,		Nine months ended April 30,	
	2001	2002	2001	2002
OPERATING REVENUES:				
Telco services				
Carrier services	\$ 7,733	\$ 10,758	\$ 15,801	\$ 30,788
Network services	597	510	2,003	1,788
Retail services	1,689	1,983	5,088	5,648
Internet e-commerce	1,449	1,335	4,125	3,808
Total operating revenues	\$ 11,468	\$ 14,586	\$ 27,017	\$ 42,018
OPERATING EXPENSES:				
Cost of services	7,619	11,425	18,564	31,928
Selling, general and administrative	4,498	3,933	13,776	11,768
Bad debt expense	39	(8)	169	108
Depreciation and amortization	1,041	1,205	3,277	3,498
Total operating expenses	13,197	16,555	35,786	47,288
Operating loss	(1,729)	(1,969)	(8,769)	(5,268)
OTHER INCOME (EXPENSE):				
Other income (expense), net	28	(85)	779	(148)
Interest expense	(250)	(517)	(1,110)	(1,588)
Total other income (expense)	(222)	(602)	(331)	(1,728)
LOSS BEFORE INCOME TAX EXPENSE (BENEFIT)	(1,951)	(2,571)	(9,100)	(6,998)
INCOME TAX EXPENSE (BENEFIT)	-	26	65	88
MINORITY INTEREST	122	207	251	198
NET LOSS	(1,829)	(2,390)	(8,914)	(6,888)
LESS: PREFERRED DIVIDENDS	(475)	(96)	(1,596)	(378)
NET LOSS TO COMMON STOCKHOLDERS	\$ (2,304)	\$ (2,486)	\$ (10,510)	\$ (7,258)
BASIC AND DILUTED LOSS PER SHARE	(\$0.03)	(\$0.03)	(\$0.15)	(\$0.03)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	74,331	91,486	69,831	84,278

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The accompanying notes are an integral part of these consolidated financial statements.

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ATSI COMMUNICATIONS, INC.
AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(In thousands)
(unaudited)

	For the three months ended April 30,		For th
	2001	2002	20
Net loss to common stockholders	(\$2,304)	(\$2,486)	
Other comprehensive income (loss), net of tax:			
Foreign currency translation adjustments	\$185	\$30	
Comprehensive loss to common stockholders	(\$2,119)	(\$2,456)	

The accompanying notes are an integra part of these consolidated financial statements.

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ATSI COMMUNICATIONS, INC.
AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
(In thousands)
(unaudited)

	Nine months ended April 30,	
	2001	2002
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (8,914)	\$ (6,882)
Adjustments to reconcile net income to net cash provided by (used in) operating activities-		
Depreciation and amortization	3,277	3,494
Amortization of debt discount	129	-
Deferred compensation	724	12
Minority Interest	(251)	(242)
Provision for losses on accounts receivable	169	106
Changes in operating assets and liabilities- net of effects from acquisition		
Change in accounts receivable	163	(140)

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Change in other assets-current and long-term	(313)	210
Change in accounts payable	1,269	3,774
Change in accrued liabilities	(160)	1,284
Change in deferred revenue	(25)	43
	-----	-----
Net cash (used in) provided by operating activities	(3,932)	1,659
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property & equipment	(716)	(854)
	-----	-----
Net cash used in investing activities	(716)	(854)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of debt	432	11
Principal payments under capital lease obligations	(945)	(510)
Payments on debt	(445)	(65)
Net increase in advanced funding arrangements	116	-
Proceeds (costs) from issuance of preferred stock, net	3,564	(20)
Proceeds from issuance of common stock, net	614	180
	-----	-----
Net cash provided by (used in) financing activities	3,336	(404)
	-----	-----
Net (decrease) increase in cash	(1,312)	401
Cash, beginning of period	1,550	103
	-----	-----
Cash, end of period	\$ 238	\$ 504
	=====	=====

The accompanying notes are an integral part of these consolidated financial statements.

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ATSI COMMUNICATIONS, INC.
AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. PRINCIPLES OF CONSOLIDATION AND BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements, which include the following subsidiaries: ATSI-Delaware, ATSI-Canada, ATSI-Texas, ATSI-Mexico, ATSI-COM, Computel, ATSI de CentroAmerica, Telespan, Sinfra and GlobalSCAPE have been prepared in accordance with Rule 10-01 of Regulation S-X, "Interim Financial Statements," and accordingly do not include all information and footnotes required under accounting principles generally accepted in the U.S. for complete financial statements. In the opinion of management, these interim financial statements contain all adjustments, without audit, necessary to present fairly the consolidated financial position of ATSI and its subsidiaries ("ATSI" or "the Company") as of April 30, 2002, the results of their operations for the three and nine months ended April 30, 2001 and 2002, comprehensive loss for the three and nine months ended April 30, 2001 and 2002, and cash flows for the nine months ended April 30, 2001 and 2002. All adjustments are of a normal recurring nature. All significant intercompany

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balances and transactions have been eliminated in consolidation. It is recommended that these interim consolidated financial statements be read in conjunction with the audited consolidated financial statements and the notes thereto for the year ended July 31, 2001 included in the Company's annual report on Form 10-K filed with the SEC on October 30, 2001. Certain prior period amounts have been reclassified for comparative purposes. The results of operations for any interim period are not necessarily indicative of the results to be expected for the full year.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets". SFAS No. 142, which supercedes APB Option No. 17, "Intangible Assets" provides financial accounting and reporting for acquired goodwill and other intangible assets. While SFAS 142 is effective for fiscal years beginning after December 15, 2001, early adoption is permitted for companies whose fiscal years begin after March 15, 2001. SFAS 142 addresses how intangible assets that are acquired individually or with a group of assets should be accounted for in financial statements upon their acquisition as well as after they have been initially recognized in the financial statements. While the Company is not yet required to adopt SFAS 142, it believes the adoption will not have a material effect on the financial condition or results of the Company unless at some future time it is determined that an impairment of its intangible assets exists.

2. FUTURE OPERATIONS

The consolidated financial statements of the Company have been prepared on the basis of accounting principles applicable to a going concern. For the period from December 17, 1993 to April 30, 2002, the Company has incurred cumulative net losses of approximately \$59.8 million. Further, we have a working capital deficit of approximately \$13.6 million at April 30, 2002. We have limited capital resources available to us, and these resources may not be available to support our ongoing operations until such time as we are able to continuously generate positive cash flows from operations. There is no assurance we will be able to achieve future revenue levels sufficient to support operations or recover our investment in property and equipment, goodwill and other intangible assets. These matters raise substantial doubt about our ability to continue as a going concern. Our ability to continue as a going

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concern is dependent upon the ongoing support of our stockholders and customers, our ability to obtain capital resources to support operations and our ability to successfully market our services.

We are likely to require additional financial resources in the near term and could require additional financial resources in the long-term to support our ongoing operations. We plan on securing funds through equity offerings and entering into lease or long-term debt financing agreements to raise capital. There can be no assurances, however, that such equity offerings or other financing arrangements will actually be consummated or that such funds, if received, will be sufficient to support existing operations until revenue levels are achieved sufficient to generate positive cash flow from operations. If we are not successful in completing additional equity offerings or entering into other financial arrangements, or if the funds raised in such stock offerings or other financial arrangements are not adequate to support us until a successful level of operations is attained, we have limited additional sources of debt or equity capital and would likely be unable to continue operating as a going concern.

3. PREFERRED STOCK

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During the quarter, holders of the Series F Preferred Stock converted 700 of the 9,210 shares outstanding and accumulated interest into common stock resulting in the issuance of 269,230 shares of common stock.

4. SEGMENT REPORTING

We have determined that we have three reportable segments: (1) U.S. Telco; (2) Mexico Telco; and (3) Internet e-commerce. Our Internet e-commerce subsidiary, GlobalSCAPE, Inc. and its operations can be differentiated from the telecommunication focus of the rest of ATSI. Additionally, we believe that our U.S. and Mexican subsidiaries should be separate segments even though many of the products are borderless. Both the U.S. Telco and Mexican Telco segments include revenues generated from Retail Services and Network Services. Our Carrier Services revenues, generated as a part of our U.S. Telco segment, are the only revenues not currently generated by both the U.S. Telco and Mexico Telco segments. We have included the operations of ATSI-Canada, ATSI-Delaware and all businesses falling below the reporting threshold in the "Other" segment. The "Other" segment also includes intercompany eliminations.

We have used earnings (loss) before interest, taxes, depreciation and amortization (EBITDA) in our segment reporting as it is the chief measure of profit or loss used in assessing the performance of each of our segments.

	For the three months ended		For the nine months ended	
	April 30, 2001	April 30, 2002	April 30, 2001	April 30, 2002
U.S. Telco				

External revenues	\$8,246,234	\$ 11,112,916	\$ 17,737,946	\$ 32,092,673
Intercompany revenues	\$ 344,533	\$ 790,517	\$ 1,215,183	\$ 1,089,229
	-----	-----	-----	-----
Total revenues	\$8,590,767	\$ 11,903,433	\$ 18,953,129	\$ 33,181,902
	=====	=====	=====	=====
 EBITDA	 (\$133,714)	 (\$930,876)	 (\$3,807,677)	 (\$1,684,243)
Operating loss	(\$631,095)	(\$1,435,621)	(\$5,504,418)	(\$3,088,642)

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Net loss		(\$712,676)	(\$529,033)	
Total assets		\$ 19,873,827	\$ 15,935,517	\$
Mexico Telco				

External revenues		\$ 1,773,424	\$ 2,138,303	\$
Intercompany revenues		\$441,865	\$ 532,825	\$
		-----	-----	-----
Total revenues		\$ 2,215,289	\$ 2,671,128	\$
		=====	=====	=====
 EBITDA		 (\$245,954)	 (\$133,408)	

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Operating loss		(\$654,065)	(\$696,105)	
Net loss		(\$803,680)	(\$1,299,858)	
Total assets		\$ 8,421,175	\$ 11,262,523	\$
Internet e-commerce				
External revenues		\$ 1,448,773	\$ 1,335,236	\$
Intercompany revenues		-	-	
	Total revenues	\$ 1,448,773	\$ 1,335,236	\$
EBITDA		(\$307,722)	\$ 301,599	
Operating income (loss)		(\$442,989)	\$ 163,713	
Net loss		(\$451,697)	(\$767,854)	
Total assets		\$ 1,680,654	\$ 1,598,864	\$
Other				
External revenues		-	-	
Intercompany revenues		(\$786,398)	(\$1,323,342)	
	Total revenues	(\$786,398)	(\$1,323,342)	
EBITDA		-	-	
Operating loss		-	-	
Net loss		(\$336,158)	\$ 111,150	
Total assets		(\$6,430,483)	\$ 7,991,996)	
Total				
External revenues		\$ 11,468,431	\$ 14,586,455	\$
Intercompany revenues		-	-	
	Total revenues	\$ 11,468,431	\$ 14,586,455	\$
EBITDA		(\$687,390)	(\$762,685)	
Depreciation and Amortization		(\$1,040,759)	(\$1,205,327)	
Operating loss		(\$1,728,149)	(\$1,968,013)	
Net loss to Common Stockholders		(\$2,304,211)	(\$2,485,595)	
Total assets		\$ 23,545,173	\$ 20,814,908	\$

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5. LEGAL PROCEEDINGS

We are also a party to additional claims and legal proceedings arising in the ordinary course of business. We believe it is unlikely that the final outcome of any of the claims or proceedings to which we are a party would have a material adverse effect on our financial statements; however, due to the inherent uncertainty of litigation, the range of possible loss, if any, cannot be estimated with a reasonable degree of precision and there can be no assurance that the resolution of any particular claim or proceeding would not have an adverse effect on our results of operations in the period in which it occurred.

6. SUBSEQUENT EVENTS

The Company's current liabilities include a total of approximately \$4.7 million and \$1.4 million, respectively, owed to IBM de Mexico and NTFC Capital Corporation. The Company has classified all amounts as current under the note obligations due to being in technical default on both notes. As such, each lender could call their notes as immediately due and payable.

In May 2002, the Company announced that it had renegotiated its capital lease agreement with IBM. The modification will result in a reduction in our capital lease obligations of approximately \$2.3 million, and a reduction in current liabilities of approximately \$4.3 million. The agreement calls for forty-two payments commencing August 1, 2002, consisting of six payments of \$50,000 and thirty-six payments of \$75,000.

In May 2002, the Company entered into a Forbearance Agreement with NTFC Capital Corporation related to its capital lease facility. In exchange for a payment of approximately \$500,000 NTFC agreed to release GlobalSCAPE, Inc. as a co-borrower under the facility. Additionally, NTFC agreed to waive the default of covenants until the earliest of 1) July 31, 2002, 2) a default by the Company under the Forbearance Agreement, 3) any other default under the facility by the Company or 4) the date an amended agreement is executed. Both parties have agreed to make their best efforts to negotiate the terms of an amended agreement, the purpose of which will be to restructure the current facility including the financial covenants. On June 12, 2002, the Company completed the sale of its majority ownership of GlobalSCAPE, our Internet e-commerce segment, for \$2.25 million resulting in a gain. A portion of the proceeds were used to make payment to NTFC in accordance with the forbearance agreement to release GlobalSCAPE as a co-borrower on the facility.

The Company's current liabilities also include approximately \$1.3 million of equipment purchased from Northern Telecom, a subsidiary of Nortel Networks in fiscal 2001. In June 2002, the Company reached an agreement with Nortel related to this payable. In return for a price reduction of \$314,000 and technical support related to the equipment, ATSI has agreed to make payments over a ten-month period beginning July 15, 2002 totaling approximately \$936,000.

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

SPECIAL NOTE: Certain Statements set forth below under this caption constitute "forward-looking statements" within the meaning of the Securities Act.

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The following is a discussion of the consolidated financial condition and results of operations of ATSI for the three and nine months ended April 30, 2001 and 2002. It should be read in conjunction with our Consolidated Financial

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Statements, the Notes thereto and the other financial information included elsewhere in the annual report on Form 10-K filed with the SEC on October 30, 2001.

General

ATSI Communications, Inc. is an international carrier serving the rapidly expanding communications markets in and between Latin America and the United States. The Company's mission is to connect the Americas with exceptional communications services guided by our core values that drive everything we do. The Company's strategy is to become a dominant provider of services to businesses and consumers in this American/Latin American corridor through the deployment of a high quality, 'next generation' network. Founded in 1993, the Company's traffic is generated from more than 650 retail points of presence throughout Mexico, as well as from relationships with major carriers based in the United States. ATSI carries the traffic generated from these sources over a hybrid, redundant satellite and fiber-based ATM network between the United States and Mexico, as well as a satellite-based network between the United States, Costa Rica and El Salvador.

The Company's current core focus today is on the communications corridor between the United States and Mexico. Already one of the two largest international communications corridors in the world, this corridor is growing due to increasing phone density in Mexico and large-scale emigration of Mexicans to the United States. The Company is uniquely positioned within this growing market niche as one of only a handful of viable carriers, and the only operating company whose focus is international services, as opposed to domestic services.

Operationally, the Company's strength lies in its framework of licenses, interconnection agreements and business relationships in Mexico, as well as in its customer relationships and industry knowledge in the United States. The Company has over 400 employees based in Mexico, and operates Mexican subsidiaries with licenses that allow it to sell local and long distance traffic, transport long distance traffic, and operate a network utilizing packet-switching technology. Utilizing these strengths, the Company has leveraged off of the networks of third parties to build a reliable customer base, and has established its own international satellite and fiber-based network to long haul consumer, corporate and carrier-generated traffic between the U.S. and Mexico.

We also own approximately 70% of GlobalSCAPE, Inc., which is rapidly becoming a leader in electronic commerce of top Internet-based software, utilizing the Web as an integral component of its development, marketing, distribution and customer relationship strategies. On June 12, 2002, the Company completed the sale of its majority ownership of GlobalSCAPE.

As discussed in Note 4 to our consolidated financial statements we have determined that we have three reportable segments: 1) U.S Telco; 2) Mexico Telco; and 3) Internet e-commerce.

Additionally, we have determined that our U.S. and Mexican subsidiaries should be reported as separate segments although many of our products are borderless and utilize the operations of entities in both the U.S. and Mexico. Both the U.S. Telco and Mexico Telco segments include revenues generated from Network Services and Retail Services. All of the carrier services revenues are recorded in the U.S. Telco segment. GlobalSCAPE, Inc. and its operations are accounted for exclusively as a part of the Internet e-commerce operating segment.

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Our consolidated financial statements have been prepared assuming that we will continue as a going concern. We have incurred losses since inception and have a working capital deficit as of April 30, 2002. Additionally, we have had recurring negative cash flows from operations with the exception of the quarters ended January 31, 1998, October 31, 2001, January 31, 2002 and April 30, 2002. For the reasons stated in Liquidity and Capital Resources and subject to the risks referred to in Liquidity and Capital Resources, we expect improved results of operations and liquidity in the last quarter of fiscal 2002 and in fiscal 2003. However, we cannot assure you that this will be the case.

Results of Operations

The following table sets forth certain items included in our results of operations in dollar amounts and as a percentage of total revenues for the three and nine-month periods ended April 30, 2001 and 2002.

	Three months ended April 30,				Nin
	2001		2002		200
	\$	%	\$	%	\$
	(unaudited)				
	-----	-----	-----	-----	-----
Operating revenues:					

Telco Services					
Carrier services	\$7,733	67%	\$10,758	74%	\$15,801
Network services	597	5%	510	3%	2,003
Retail services	1,689	15%	1,983	14%	5,088
Internet e-commerce	1,449	13%	1,335	9%	4,125
	-----	-----	-----	-----	-----
Total operating revenues	11,468	100%	14,586	100%	27,017
	-----	-----	-----	-----	-----
Cost of services	7,619	66%	11,425	78%	18,564
	-----	-----	-----	-----	-----
Gross margin	3,849	34%	3,161	22%	8,453
Selling, general and administrative expense	4,498	39%	3,933	27%	13,776
Bad debt expense	39	1%	(8)	0%	169
Depreciation and amortization	1,041	9%	1,205	8%	3,277
	-----	-----	-----	-----	-----
Operating loss	(1,729)	(15%)	(1,969)	(13%)	(8,769)
Other, net	(222)	(2%)	(602)	(4%)	(331)
	-----	-----	-----	-----	-----
Loss before income tax expense and minority interest	(1,951)	(17%)	(2,571)	(17%)	(9,100)
Income tax & minority interest, net	122	1%	181	1%	186

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Net loss	(1,829)	(16%)	(2,390)	(16%)	(8,914)
Less: preferred dividends	(475)	(4%)	(96)	(1%)	(1,596)
	-----	-----	-----	-----	-----
Net loss to common stockholders	(\$2,304)	(20%)	(\$2,486)	(17%)	(\$10,510)
	=====	=====	=====	=====	=====

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Three Months ended April 30, 2002 Compared to Three Months ended April 30, 2001

Operating Revenues. Consolidated operating revenues increased 30% between quarters from \$11.5 million to \$14.6 million.

Telco revenues (all revenues other than e-commerce) increased from \$10.0 million to \$13.3 million while e-commerce revenues generated by GlobalSCAPE declined by approximately \$114,000 between periods.

Carrier services revenues increased approximately \$3.0 million, or 39% from the quarter ended April 2001 to the quarter ended April 2002. The increased revenue resulted from an increase in traffic from approximately 75.5 million units during the quarter ended April 30, 2001 to approximately 123.6 million units during the quarter ended April 30, 2002. The increased traffic was partially offset by reduced revenues per unit, quarter to quarter.

Network services declined by approximately \$87,000 or 15% between periods. The decline is primarily due to the net loss of two private network customers between periods. Additionally, our 800- service business declined between periods by approximately \$17,000. The decline is attributed to decreased volume of units transported via our network. Units transported declined from 1.0 million to 860,000, period to period.

Retail services revenues increased approximately \$294,000 between periods. Our integrated prepaid revenues within Mexico, collected at the point of sale, increased approximately \$344,000 between quarters. This increase in revenues was reduced by an approximate \$50,000 decline in postpaid, primarily operated-assisted service revenues. The improved revenues between quarters resulted from our efforts to become more competitive in the products we offered as we evaluated our core business to strategically relocate communication centers to concentrated areas where growth would be realized. As for the declining operated-assisted services, management does not expect this revenue stream to contribute significantly to the Company's operating results in fiscal 2002 and beyond.

Our Internet e-commerce services decreased approximately \$114,000 between periods. The decline in revenues between quarters was due to the loss of advertising revenues, quarter to quarter and a decline in the number of registrations, quarter to quarter.

Cost of Services. Cost of services increased as a percentage of revenue from 66% to 78%, period to period. Cost of services for e-commerce slightly increased from 4% for the quarter ended April 2001 to 8% for the period ended April 2002. The increase was a result of increased royalty expense related to GlobalSCAPE's distribution agreement with Trellix Corporation. Cost of services as a percentage of revenues on the Company's telco business increased from 75% to 85% between quarters due primarily to lower carrier services margins in the current quarter. The Company continues to try to improve its carrier services margins through reductions in variable costs and improvements realized from the

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installation of Nortel Passport equipment in the latter half of fiscal 2001. The increase in carrier services traffic as a percentage of overall revenues from 67% to 74%, between quarters, contributed to the increased cost of services.

Selling, General and Administrative (SG&A) Expenses. SG&A expenses decreased approximately \$565,000, or 13% between periods. SG&A expenses associated with our e-commerce subsidiary decreased approximately \$356,000, or 28% between periods due to the decline in expenses

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related to research and development, professional fees, recruiting and compensation expense associated with the granting of options. SG&A expenses associated with our telco operations decreased approximately 7% or \$209,000 between periods and decreased as a percentage of revenues from 32% to 23%.

Bad Debt Expense. Bad Debt Expense decreased by approximately \$47,000 between periods due primarily to positive adjustments to GlobalSCAPE's bad debt during the quarter.

Depreciation and Amortization. Depreciation and amortization increased by approximately 16% or \$164,000 between periods due to equipment purchases.

Operating Loss. The Company's operating loss increased by approximately 14% or \$240,000 from the third quarter of fiscal 2001, primarily due to decreased gross margins and increased depreciation and amortization.

Other Income(expense). Other expense increased approximately \$380,000 between quarters due to the recording of additional incremental interest expense under the provision of the IBM capital lease of approximately \$401,000.

Preferred Stock Dividends. During the quarter ended April 2002, we recorded approximately \$96,000 of non-cash dividends related to our cumulative convertible preferred stock. This compares favorably to the approximate \$475,000 of non-cash dividends and beneficial conversion feature expense recognized during the quarter ended April 2001.

Net loss to Common Stockholders. The net loss for the quarter ended April 2002 declined by approximately \$182,000 to \$2.5 million from the \$2.3 million net loss for the quarter ended April 2001. The decline was due primarily to decreased gross margins and increased other expense offset somewhat by the reduced selling, general and administrative expenses.

Nine Months Ended April 30, 2002 Compared to Nine Months Ended April 30, 2001

Operating Revenues. Consolidated operating revenues increased 56% between periods from \$27.0 million for the nine months ended April 30, 2001 to \$42.0 million for the nine months ended April 30, 2002. In response to the increasing demand for its services, the Company began adding capacity to both its switch and its network backbone in October 2001. The Company continues to work to increase its terminating capacity with third party carriers to process traffic outside of its own network backbone in Mexico. The net effect of our efforts during the nine months was three of the four highest quarters of revenues in our history.

Telco revenues (all revenues other than e-commerce) increased from \$23.0 million to \$38.2 million while e-commerce revenues generated by GlobalSCAPE declined by approximately \$316,000 between periods.

Carrier services revenues increased approximately \$15.0 million, or 95%

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from the nine months ended April 2001 to the nine months ended April 2002. As a result of the Company's effort to add capacity, the units transported via our network increased from approximately 171.2 million units during the period ended April 2001 to approximately 331.1 million units during the period ended April 2002.

Network services decreased by approximately \$217,000 or 11% between periods. Our 800-

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service business declined between periods by approximately \$138,000. The decline is attributable to a decreased volume of units transported via our network. Units transported declined from 4.3 million to 3.3 million, period to period. Our private network services decreased approximately \$79,000 between periods primarily due to the net loss of two customers from April 2001 to April 2002.

Retail services revenues increased approximately \$552,000 between periods. Our integrated prepaid revenues within Mexico, collected at the point of sale, increased approximately \$853,000 between quarters, but were offset by an approximate \$301,000 decline in postpaid, primarily operated-assisted service revenues. The improved revenues between quarters resulted from our efforts to become more competitive in the products we offered as we evaluated our core business to strategically relocate communication centers to concentrated areas where growth would be realized. As for the declining operated-assisted services, management does not expect this revenue stream to contribute significantly to the Company's operating results in fiscal 2002 and beyond.

Our Internet e-commerce services decreased approximately \$316,000, or 8% between periods. The expected elimination of advertising revenue accounted for approximately \$41,000 of the decline. As for the remaining decline, it was attributed to a decline in CuteFTP site license sales between periods. This decline, however, was partially offset by the sales of a desktop web-site creation and management tool, and the introduction of CuteFTP Pro. Additionally, other product sales, such as CuteHTML, CuteMAP, and CuteZIP, increased between periods to contribute to the offset.

Cost of Services. Cost of services increased as a percentage of revenue from 69% to 76%, period to period. Cost of services for e-commerce increased from 4% for the nine months ended April 2001 to 8% for the nine months ended April 2002. The increase was a result of increased royalty expense related to GlobalSCAPE's distribution agreement with Trellix Corporation. Cost of services as a percentage of revenues on the Company's telco business increased from 80% to 83% between periods. The Company continues to try to improve its carrier services margins through reductions in variable costs and improvements realized from the installation of Nortel Passport equipment in the latter half of fiscal 2001. The increase in carrier services traffic as a percentage of overall revenues from 59% to 73%, between periods, contributed greatly to the increased cost of services.

Selling, General and Administrative (SG&A) Expenses. SG&A expenses decreased approximately \$2.0 million, or 15% between periods. SG&A expenses associated with our e-commerce subsidiary decreased approximately \$1.4 million, or 33% between periods due to the decline in expenses related to research and development, recruiting, professional fees and compensation expense associated with the granting of stock options. SG&A expenses associated with our telco operations decreased approximately 6% or \$586,000 between periods. This improvement resulted from management's efforts to cut excess spending by each department. Also, during the quarter ended October 2000, telco operations recognized significant expenses related to severance packages, professional fees

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associated with the Genesis transaction, and strategic research services. As a percentage of revenues, telco SG&A declined from 42% to 23% period to period.

Bad Debt Expense. Bad Debt Expense declined by approximately 37% or \$63,000 between periods due primarily to the decline in the Company's postpaid call services business between periods and positive adjustments to GlobalSCAPE's bad debt. These improvements were partially offset by approximately \$37,000 of expense related to one of our carrier service customers.

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Depreciation and Amortization. Depreciation and amortization increased by approximately 7% or \$217,000 between periods due to equipment purchases.

Operating Loss. The Company's operating loss improved significantly by approximately 40% or \$3.5 million period to period, primarily due to increased revenues and consequently increased gross margins and reductions in selling, general and administrative expenses.

Other Income(expense). Other expense increased approximately \$1.4 million between periods primarily due to three factors. First, during the quarter ended January 2001, the Company recognized a gain of \$500,000 related to the settlement of a litigation case with one of our carrier customers. Secondly, during the nine months ended April 30, 2001, the Company recognized a gain related to the extinguishment of a liability for approximately \$184,000. Finally, during the nine months ended April 30, 2002, the Company recognized approximately \$1.0 million of additional interest expense under the provision of the IBM capital lease.

Preferred Stock Dividends. During the nine months ended April 30, 2002, we recorded approximately \$373,000 of non-cash dividends related to our cumulative convertible preferred stock. This compares favorably to the approximate \$1.6 million of non-cash dividends and beneficial conversion feature expense recognized during the nine months ended April 2001.

Net loss to Common Stockholders. The net loss for the nine months ended April 2002 improved by approximately \$3.3 million to \$7.2 million from the \$10.5 million net loss for the nine months ended April 2001. The improvement was due primarily to a significant increase in revenues, which improved our gross margin dollars. Additionally, the reduction in selling, general and administrative expenses and preferred dividends contributed to our improved net loss to stockholders between periods.

Liquidity and Capital Resources

During the nine months ended April 30, 2002, we generated positive cash flows from operations of approximately \$1.7 million. The Company was able to generate this positive cash flow from operations by reducing the net loss incurred during the period, shortening the cash conversion cycle of customer receivables, and working with vendors related to payments. As a result, the Company had the ability to operate with minimal assistance from private equity placements or issuances of debt.

For the nine months ended April 30, 2002, after adjustments for non-cash items (depreciation and amortization, amortization of debt discount, deferred compensation, provision for losses on accounts receivable and minority interest), we had a net loss of approximately \$3.5 million. Management of the operating assets and liabilities, which consist mainly of collections on accounts receivable and payments made on outstanding payables and accrued liabilities, produced positive cash flows of approximately \$5.2 million,

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resulting in positive operating cash flows for the period of \$1.7 million. By generating positive cash flows during the nine months ended April 30, 2002, we improved over the nine months ended April 30, 2001 by \$5.6 million or 142% in operating cash flows. Due primarily to the positive operating cash flows produced during the first nine months of fiscal 2002, our net loss, after adjustments for non-cash items, improved over the nine months ended April 30, 2001, when our net loss, after adjustments for non-cash items, was \$4.9 million.

Although we were able to produce positive cash flows from operations during the quarters ended October 31, 2001, January 31, 2002 and April 30, 2002, we must produce positive cash flows on a

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recurring basis, and reduce or eliminate our working capital deficit. Until that time, management will be faced with deciding whether to use available funds to pay vendors and suppliers for services necessary for operations, to service our debt requirements, or to purchase equipment to be used in the growth of our business. Should our available funds not be sufficient to pay vendors and suppliers, to service debt requirements and purchase equipment, we will need to continue to raise additional capital. As noted in the risk factors of the Form 10-K filed with the SEC on October 30, 2001, we have not always paid all of our suppliers on time. Some of these suppliers are critical to our operations. These suppliers have given us payment extensions in the past, although there is no guarantee they will do so in the future.

During the nine months ended April 30, 2002, the Company acquired approximately \$854,000 in equipment which was not financed through capital lease or financing arrangements. Additional cash outflows included the payment of approximately \$510,000 towards our capital lease obligations and an additional \$65,000 towards debt.

During the nine months ended April 2002, we received cash proceeds, net of issuance costs, of approximately \$180,000 from the issuance of common stock as a result of an investment option exercise. These funds along with the cash flows generated from operations were used to pay payables, to make payments on our debt and capital lease obligations, and to purchase additional equipment used in our network operations.

Overall, the Company's net operating, investing and financing activities during the nine months ended April 2002 provided approximately \$401,000 in cash flows. The Company's working capital deficit at April 30, 2002 was approximately \$13.6 million. This represents an increase of approximately \$4.3 million from the working capital deficit of \$9.3 million at July 31, 2001. The Company's current liabilities include a total of approximately \$4.7 million and \$1.4 million, respectively, owed to IBM de Mexico and NTFC Capital Corporation. The Company classified all amounts as current under the note obligations due to being in technical default on both notes.

In May 2002, the Company announced that it had renegotiated its capital lease agreement with IBM. The modification will result in a reduction in our capital lease obligations of approximately \$2.3 million, and a reduction in current liabilities of approximately \$4.3 million. The agreement calls for forty-two payments commencing August 1, 2002, consisting of six payments of \$50,000 and thirty-six payments of \$75,000.

In May 2002, the Company entered into a Forbearance Agreement with NTFC Capital Corporation related to its capital lease facility. In exchange for a payment of approximately \$500,000 NTFC agreed to release GlobalSCAPE, Inc. as a co-borrower under the facility. Additionally, NTFC agreed to waive the default

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of covenants until the earliest of 1) July 31, 2002, 2) a default by the Company under the Forbearance Agreement, 3) any other default under the facility by the Company or 4) the date an amended agreement is executed. Both parties have agreed to make their best efforts to negotiate the terms of an amended agreement, the purpose of which will be to restructure the current facility including the financial covenants. On June 12, 2002, the Company completed the sale of its majority ownership of GlobalSCAPE, our Internet e-commerce segment, for \$2.25 million resulting in a gain. A portion of the proceeds were used to make payment to NTFC in accordance with the forbearance agreement to release GlobalSCAPE as a co-borrower on the facility.

The Company's current liabilities also include approximately \$1.3 million of equipment purchased from Northern Telecom, a subsidiary of Nortel Networks in fiscal 2001. In June 2002, the Company reached an agreement with Nortel related to this payable. In return for a reduction of \$314,000

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in the price of the equipment and additional technical support related to the equipment, ATSI has agreed to make payments over a ten-month period beginning July 15, 2002 totaling approximately \$936,000.

The Company's current obligations also include approximately \$437,000 owed to the former owners of Grupo Intelcom, S.A. de C.V., the entity purchased by the Company in July 2000 and through which the Company obtained its Mexican long distance concession. Additionally, the Company has current notes payable of \$603,000.

We continue to focus on enhancing the capacity and efficiency of our international network backbone between the U.S. and Mexico, adding alternate carriers to transport our traffic outside of that backbone in Mexico, and changing the mix of our traffic to better utilize our network capabilities. A direct result of our producing positive cash flows from operations relates to the Company's focus on its core revenue stream and reducing the cash conversion cycle of its primary customers. To allow these trends to continue, the Company needs to expand its network and switch capacity in order to provide additional capacity to existing and potential customers.

The Company has limited availability to capital resources, and these resources may not be available to support our ongoing operations until such time as we are able to generate positive cash flows from operations. There is no assurance we will be able to achieve future revenue levels sufficient to support operations or recover our investment in property and equipment, goodwill and other intangible assets. These matters raise substantial doubt about our ability to continue as a going concern. Our ability to continue as a going concern is dependent upon the ongoing support of our stockholders and customers, our ability to obtain capital resources to support operations and our ability to successfully market our services.

Inflation/Foreign Currency

Inflation has not had a significant impact on the Company's operations. With the exception of revenues from the Company's communication centers and payphones, almost all of the Company's revenues are generated and collected in U.S. dollars. Integrated prepaid services from the Company's communication centers and payphones are provided at the time of the call in exchange for cash payment, so the Company does not maintain receivables on its books that are denominated in pesos. In an effort to reduce foreign currency risk, the Company attempts to convert pesos collected to U.S. dollars quickly and attempts to maintain minimal cash balances denominated in pesos. Some expenses related to

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certain services provided to the Company are incurred in foreign currencies, primarily Mexican pesos. The devaluation of the Mexican peso over the past several years has not had a material adverse effect on the Company's financial condition or operating results.

Market Risk

We are subject to several market risks. Specifically, we face commodity price risks, equity price risks and foreign currency exchange risk.

Commodity Price Risk

Certain of our businesses, namely network services, operate in an extremely price sensitive environment. The network services business over the past twelve months has seen significant reductions in the price per unit charged for transporting traffic. While we have been able to withstand these pricing

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pressures, certain of our competitors are much larger and better positioned to continue to withstand these price reductions. Our ability to further absorb these price reductions may be dependent on our ability to further reduce our costs of transporting this traffic.

Equity Price Risks

Until such time as we are able to consistently produce positive cash flows from operations, we will be dependent on our ability to continue to access debt and equity sources of capital. While recent history has shown us capable of raising equity sources of capital; future equity financings and the terms of those financings will be largely dependent on our stock price, our operations and the future dilution to our shareholders.

Foreign Currency Exchange Risk

We face two distinct risks related to foreign currency exchange risk; transaction risk and translation risk.

As previously discussed under the caption "Inflation", we face risks related to certain of our revenue streams, namely, integrated prepaid services from our own Mexican communication centers and payphones and the transacting of business in pesos as opposed to U.S. dollars. Historically, we have been able to minimize foreign currency exchange risk by converting from pesos to U.S. dollars quickly and by maintaining minimal cash balances denominated in pesos. As we grow our retail business in Mexico it is likely that we will face increasing foreign currency transaction risks.

Historically, we have recorded foreign currency translation gains/losses in our assets and liabilities due to the volatility of the peso exchange rate as compared to the U.S. dollar over time. We anticipate we will continue to experience translation gains/losses in our assets and liabilities, specifically in fixed assets which are accounted for at historical pesos amounts on the books of our Mexican subsidiaries but converted to U.S. dollars for consolidation purposes at current exchange rates.

PART II OTHER INFORMATION

Item 6 Exhibits and Reports on Form 8-K

(a) Exhibits:

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The exhibits listed below are filed as part of this report.

Exhibit Number

11 Computation of Earnings per Share (Exhibit to this Form 10-Q filed June 14, 2002)

(b) Current Reports on Form 8-K.

None.

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SIGNATURE

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

ATSI COMMUNICATIONS, INC.
(Registrant)

Date: June 14, 2002

By: /s/H. Douglas Saathoff

Name: H. Douglas Saathoff
Title: Chief Financial Officer

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