AMERICAN TELESOURCE INTERNATIONAL INC
Form 10-Q
March 16, 2001

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE
- ACT OF 1934
For the quarterly period ended January 31, 2001

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

AMERICAN TELESOURCE INTERNATIONAL, INC.
(Exact name of registrant as specified in its charter)

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

6000 Northwest Parkway, Suite 110
San Antonio, Texas 78249
(210) 558-6090
(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 X No
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The number of shares outstanding of the registrant's common stock at March 14, 2001 was 75,743,348

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AMERICAN TELESOURCE INTERNATIONAL, INC.
AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED JANUARY 31, 2001

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AMERICAN TELESOURCE INTERNATIONAL, INC.
AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share information)

	July 31, 2000	January 31, 2001 (unaudited)
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 1,550	$ 757
Accounts receivable, net of allowance of $ 757 and $ 769, respectively	3,186	2,698
Inventory	74	90
Prepaid expenses and other assets	631	781
Total current assets	5,441	4,326
PROPERTY AND EQUIPMENT (At cost):	19,388	20,727
Less - Accumulated depreciation and amortization	(8,330)	(10,370)
Net property and equipment	11,058	10,357
OTHER ASSETS, net		
Goodwill, net	4,901	4,831
Concession license, net	4,422	4,318
Trademarks, net	570	480
Other assets	502	432
Total assets	$ 26,894	$ 24,744

LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 3,931	$ 6,736
Accrued liabilities	2,350	2,254
Current portion of notes payable	544	456
Current portion of convertible long-term debt	289	565
Current portion of obligations under capital leases	3,411	3,639
Deferred revenue	167	577
Total current liabilities	10,692	14,227
LONG-TERM LIABILITIES:		
Obligations under capital leases, less current portion	2,506	1,923
Other long-term liabilities	56	74
Total long-term liabilities	2,562	1,997
MINORITY INTEREST	-	467
COMMITMENTS AND CONTINGENCIES:		
REDEEMABLE PREFERRED STOCK		
Series D Cumulative Preferred Stock, 3,000 shares authorized, 3,000 shares issued and outstanding at July 31, 2000 and 1,642 shares issued and outstanding at January 31, 2001, carrying value of $2,662,375 and $1,316,880 at July 31, 2000 and January 31, 2001, respectively	2,662	1,317
Series E Cumulative Preferred Stock, 10,000 shares authorized, no shares issued and outstanding at July 31, 2000, 2,500 shares issued and outstanding at January 31, 2001, carrying value of $1,573,309	-	1,573
STOCKHOLDERS' EQUITY:		
Preferred stock, $0.001 par value, 10,000,000 shares authorized, Series A Cumulative Convertible Preferred Stock, 50,000 shares authorized, 24,255 shares issued and outstanding at July 31, 2000, 14,255 shares issued and outstanding at January 31, 2001	-	-
Common stock, $0.001 par value, 100,000,000 shares authorized, 67,408,979 issued and outstanding at July 31, 2000, 72,166,769 issued and outstanding at January 31, 2001	67	72
Additional paid in capital	51,625	53,904
Accumulated deficit	(39,125)	(47,924)
Warrants outstanding	417	1,381
Notes due from officers	(1,108)	(1,108)
Deferred compensation	(119)	(98)
Other comprehensive loss	(779)	(1,064)
Total stockholders' equity	10,978	5,163
Total liabilities and stockholders' equity	$ 26,894	$ 24,744

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

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AMERICAN TELESOURCE INTERNATIONAL, INC.
AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(unaudited)

	Three months ended January 31, 2000	2001
OPERATING REVENUES:		
Telco services		
Network services	$ 6,891	$ 5,122
Integrated prepaid	1,520	1,505
Postpaid	987	169
Internet e-commerce	1,290	1,254
Total operating revenues	10,688	8,050
OPERATING EXPENSES:		
Cost of services	7,104	5,417
Selling, general and administrative	3,252	4,057
Bad debt expense	93	79
Depreciation and amortization	1,427	1,087
Total operating expenses	11,876	10,640
Operating loss	(1,188)	(2,590)
OTHER INCOME(EXPENSE):		
Interest income	2	33
Other income (expense)	-	444
Interest expense	(626)	(377)
Total other income (expense)	(624)	100
LOSS BEFORE INCOME TAX EXPENSE (BENEFIT)	(1,812)	(2,490)
INCOME TAX EXPENSE (BENEFIT)	-	(1)
MINORITY INTEREST	-	88
NET LOSS	($1,812)	($2,401)
LESS: PREFERRED DIVIDENDS	(791)	(233)
NET LOSS TO COMMON STOCKHOLDERS	($2,603)	($2,634)
BASIC AND DILUTED LOSS PER SHARE	($0.05)	($0.04)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	50,058	69,071

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

AMERICAN TELESOURCE INTERNATIONAL, INC.
AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(In thousands)

	For the three months ended January 31,	
	2000	2001
Net loss to common stockholders	($2,603)	($2,634)
Other comprehensive income (loss), net of tax:		
Foreign currency translation adjustments	(220)	(245)
Comprehensive loss to common stockholders	($2,823)	($2,879)

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

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AMERICAN TELESOURCE INTERNATIONAL, INC.
AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(unaudited)

	Six months ended 2000
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net loss	($3,759)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities-	
Depreciation and amortization	2,335
Amortization of debt discount	353
Deferred compensation	283
Minority interest	-
Provision for losses on accounts receivable	213
Changes in operating assets and liabilities	
(Increase) Decrease in accounts receivable	(863)
Increase in other assets-current and long-term	(555)
Increase in accounts payable	1,293
Increase (Decrease) in accrued liabilities	232
Decrease in deferred revenue	(47)

Net cash used in operating activities	(515)
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchases of property and equipment	(688)
Net cash used in investing activities	(688)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Proceeds from issuance of debt	106
Net decrease in short-term borrowings	(306)
Net increase from advanced funding arrangements	161
Payments on debt	(503)
Capital lease payments	(678)
Payments on long-term liabilities	(34)
Proceeds from issuance of preferred stock, net of issuance costs	1,821
Proceeds from issuance of common stock, net of issuance costs	920
Net cash provided by financing activities	1,487
Net increase (decrease) in cash	284
Cash, beginning of period	379
Cash, end of period	$ 663

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

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AMERICAN TELESOURCE INTERNATIONAL, INC.
AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(In thousands, except per share amounts)

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 January 31, 2001, the results of their operations for the three and six months ended January 31, 2000 and 2001, comprehensive loss for the three and six months ended January 31, 2000 and 2001, and cash flows for the six months ended January 31, 2000 and 2001. All adjustments are of a normal recurring nature. All significant intercompany 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, 2000 included in the Company's annual report on Form 10-K filed with the SEC on November 14, 2000. 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 September 2000, the Financial Accounting Standards Board ("FASB") ") issued Statement of Financial Accounting Standards (SFAS) No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", a replacement of FASB Statement No. 125. SFAS No. 140, effective after March 31, 2001 for reporting and disclosure proposes on fiscal years ending after December 15, 2000, provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities. Those standards are based on consistent application of a financial-components approach that focuses on control. Under that approach, after a transfer of financial assets, an entity recognizes the financial and servicing assets it controls and the liabilities it has incurred, derecognizes financial assets when control has been surrendered, and derecognizes liabilities when extinguished. This Statement provides consistent standards for distinguishing transfers of financial assets that are sales from transfers that are secured borrowings. We believe that SFAS No. 140 will not have a material effect on the financial condition or results of the Company once adopted.

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 January 31, 2001, the Company has incurred cumulative net losses of approximately $47.9 million. Further, the Company has a working capital deficit of approximately $9.9 million at January 31, 2001. Although the Company has capital resources available to it, these resources are limited and may not be available to support its ongoing operations until such time as the Company is able to maintain positive cash flow from operations. There is no assurance the Company will be able to achieve future revenue levels sufficient to support operations or recover its investments in property and equipment, goodwill and other

intangible assets. These matters raise substantial doubt about the Company's ability to continue as a going concern. The ability of the Company to continue as a going concern is dependent upon the ongoing support of its stockholders and customers, its ability to obtain capital resources to support operations and its ability to successfully market its services.

The Company is likely to require additional financial resources in the near term and could require additional financial resources in the long-term to support its ongoing operations. The Company has retained various financial advisers to assist it in refining its strategic growth plan, defining its capital needs and obtaining the funds required to meet those needs. The plan includes 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 long-term debt 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 maintain positive cash flow from operations. If the Company is 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 the Company until a successful level of operations is attained, the Company has limited additional sources of debt or equity capital and would likely be unable to continue operating as a going concern.

3. DEFERRED REVENUE

In November 2000, the Company settled an outstanding claim against one of its carrier services customers. The terms of the settlement called for the Company to receive $500,000 in cash, which has been recorded as other income in the consolidated financial statements. In addition to the $500,000 in cash, the settlement calls for an additional $500,000 to be applied to network services provided by ATSI to its customer. We have recorded the $500,000 as deferred revenue to be recorded as revenue as the customer's traffic is routed to ATSI's network. As of January 31, 2001, approximately $439,000 remains in deferred

revenue.

4. PREFERRED STOCK

In the quarter ended January 31, 2001, the holder of 10,000 shares of Series A Preferred Stock elected to convert its last 3,333 shares and accumulated dividends of approximately $27,000 into shares of common stock resulting in the issuance of 195,027 shares of common stock.

In addition, the holder of 3,000 shares of Series D Preferred Stock elected to convert 1,358 shares and accumulated dividends of approximately $73,000 into shares of common stock resulting in the issuance of 3,946,464 shares of common stock. As of January 31, 2001, 1,642 shares of Series D Preferred Stock remain outstanding.

5. SEGMENT REPORTING

In June 1997, the FASB issued SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information," which establishes standards for reporting information about operating segments in annual and interim financial statements. It also establishes standards for related disclosures about products and services, geographic areas and major customers. SFAS No. 131 supersedes SFAS No. 14, "Financial Reporting for Segments of a Business Enterprise." Generally, financial information is required to be reported on the basis that it is used internally for evaluating segment performance and deciding how to allocate resources to segments. SFAS No. 131 is effective for financial statements for

periods beginning after December 15, 1997. In an attempt to identify its reportable operating segments, the Company considered a number of factors or criteria. These criteria included segmenting based upon geographic boundaries only, segmenting based on the products and services provided, segmenting based on legal entity and segmenting by business focus. Based on these criteria or factors the Company has determined that it has three reportable operating segments: (1) U.S. Telco; (2) Mexico Telco; and (3) Internet e-commerce. The Company's Internet e-commerce subsidiary, GlobalSCAPE, Inc. and its operations can be differentiated from the telecommunication focus of the rest of the Company. Additionally, the Company believes that its U.S. and Mexican subsidiaries should be separate segments in spite of the fact that many of the products are borderless. Both the U.S. Telco and Mexican Telco segments include revenues generated from Integrated Prepaid, Postpaid, and Network Services. The Company has 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.

	For the three months ended		
U.S. Telco	January 31, 2000	January 31, 2001	Ja
External revenues	$ 7,622,248	$ 5,040,444	$ 1
Intercompany revenues	$ 763,192	$ 342,140	$
Total revenues	$ 8,385,440	$ 5,382,584	$ 1
EBITDA	($257,741)	($944,277)	
Operating loss	($622,018)	($1,440,697)	($
Net loss	($729,015)	($1,049,436)	($
Total assets	$ 11,413,817	$ 15,683,730	$ 1

Mexico Telco			
External revenues	$ 1,776,530	$ 1,755,505	$
Intercompany revenues	$ 631,032	$ 468,549	$
Total revenues	$ 2,407,562	$ 2,224,054	$
EBITDA	($229,359)	($517,173)	
Operating loss	($1,214,181)	($924,405)	($
Net loss	($1,400,242)	($1,146,910)	($
Total assets	$ 10,449,024	$ 8,766,249	$ 1

Internet e-commerce			
External revenues	$ 1,289,563	$ 1,254,048	$
Intercompany revenues	-	-	
Total revenues	$ 1,289,563	$ 1,254,048	$
EBITDA	$ 731,005	($35,992)	$
Operating income (loss)	$ 654,978	($161,797)	$
Net income (loss)	$ 643,055	($173,016)	$
Total assets	$ 1,816,530	$ 1,709,694	$

Other			
External revenues	-	-	
Intercompany revenues	($1,394,224)	($810,689)	($
Total revenues	($1,394,224)	($810,689)	($
EBITDA	($5,000)	($5,769)	
Operating loss	($7,160)	($62,841)	
Net loss	($1,116,325)	($264,707)	($
Total assets	$ 267,285	($1,415,501)	$

Total			
External revenues	$ 10,688,341	$ 8,049,997	$ 2
Intercompany revenues	-	-	
Total revenues	$ 10,688,341	$ 8,049,997	$ 2
EBITDA	$ 238,905	($1,503,211)	
Depreciation, Depletion and Amortization	($1,427,286)	($1,086,529)	($

Operating loss	($1,188,381)	($2,589,740)	($
Net loss to Common Stockholders	($2,602,527)	($2,634,069)	($
Total assets	$ 23,946,656	$ 24,744,172	$ 2

6. SUBSEQUENT EVENTS

On December 1, 2000, the Company elected to use its option to extend the maturity of the $565,000 convertible note to January 31, 2001. Subsequent to January 31, 2001, we negotiated an extension with the holder of the convertible note that allowed the Company to extend the maturity date until July 31, 2001. The note accrues interest at the rate of twelve percent (12%) per annum until paid in full July 31, 2001. The lender's options to elect conversion upon maturity remain unchanged.

On February 26, 2001, the Company and Genesis Communications International, Inc. announced that both parties mutually agreed to terminate the previously announced definitive agreement to combine both companies. Both parties cited the fact that certain conditions required to close the transaction had not been met. Also in response to significant changes that have occurred in the telecommunications marketplace since the original agreement and subsequent amendment were executed, both companies concluded that terminating the definitive agreement would be in the mutual best interest of the stockholders of each company. Although both companies mutually agreed to terminate the definitive agreement, both companies agreed to continue their existing business relationship.

On February 27, 2001, the Company announced that all seven proposals submitted for approval by its shareholders were approved at its Annual Meeting of Stockholders held February 26, 2001. The seven proposals approved by the ATSI stockholders are as follows:

1. The issuance of shares in the Genesis Merger. Although the shareholders approved the

issuance of shares for the acquisition of Genesis, both parties agreed to terminate the definitive agreement.
2. The issuance of shares upon conversion of preferred stock and exercise of warrants.
3. The amendment to the Certificate of Incorporation of the Company to increase the number of authorized shares of common stock from 100 million to 200 million shares.
4. The amendment to the Certificate of Incorporation of the Company to change its name to ATSI Communications, Inc.
5. The election of Arthur L. Smith and John R. Fleming as Class C members of the Company's Board of Directors, with their terms expiring at the Annual Meeting of Stockholders held in 2004.
6. The 2001 Incentive Stock Option Plan.
7. The ratification of the selection of Arthur Andersen LLP as independent public accountants for the fiscal year ending July 31, 2001.

Additional information regarding the seven proposals can be found in the Company's Proxy Statement as filed with the SEC on February 7, 2001.

In March 2001, the holder of the Company's Series E Preferred Stock converted 625 of the 2,500 shares outstanding and accumulated interest into common stock resulting in the issuance of 1,159,793 shares of common stock. In accordance with the terms of the Investment Option of the Series E Preferred Stock, the holder purchased an additional 927,834 shares of common stock for

$512,164. Additionally, the holder of the Company's Series E Preferred Stock purchased an additional 500 shares of its Series E Preferred Stock for cash proceeds of $500,000. Total cash proceeds to the Company of the investment by the holder of the Series E Preferred Stock was approximately $1,012,000.

In March 2001, the Company received commitments of approximately $800,000 in preferred stock funding.

In March 2001, the holder of 10,000 shares of Series A Preferred Stock elected to convert all their shares and accumulated dividends of approximately $125,000 into shares of common stock resulting in the issuance of 1,458,955 shares of common stock.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Quarterly Report on Form 10-Q contains certain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Specifically, all statements other than statements of historical facts included in the report regarding the Company's financial position, business strategy and plans and objectives of management of the Company for future operations are forward-looking statements. These forward-looking statements are based on the beliefs of the Company's management, as well as assumptions made by and information currently available to the Company's management. When used in this report, the words "anticipate," "believe," "could," "estimate," "expect" and "intend" and words or phrases of similar import, as they relate to the Company or Company's management, are intended to identify forward-looking statements. Such statements reflect the current view of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions related to certain factors including, without limitation, the inability to obtain capital, changes in the Mexican political or economic environment; the adoption by

Mexico of new laws or regulations, or changes effected by Mexico to existing laws affecting the communications industry generally or the Company specifically; increased or redirected competition efforts, targeting the Company's services or operation, by competitors; general economic conditions, customer relations, relationships with vendors, the interest rate environment, seasonality, the operation of the Company's network, the ability of the Company's direct sales force to successfully replace its independent marketing representatives or the failure of said direct sales force to produce anticipated results, transmission costs, product introductions and acceptance, the inability to continue to generate new sources of revenue, technological change, changes in industry practices, one-time events and other factors described herein ("cautionary statements"). Reference is made to the risks and uncertainties contained in the Company's annual report on Form 10-K. Although the Company believes that the expectations are reasonable, it can give no assurance that such expectations will prove to be correct. Based upon changing conditions, should any one or more of these risks or uncertainties materialize, or should any underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated, expected or intended. All subsequent written and oral forward-looking statements attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by the applicable cautionary statements.

General

Our mission is to employ leading-edge technologies for delivery of exceptional telecommunication services to underserved Latino markets in the U.S. and Latin America emphasizing convenience, accessibility, quality, reliability, and affordability, while continually seeking to add value through new and innovative products and services. Utilizing a framework of licenses, interconnection and service agreements, network facilities and retail

distribution channels (hereinafter collectively referred to as the "framework"), we are primarily focused on capturing market share in the international telecommunications corridor between the United States and Mexico. Even with poor phone-line penetration, our research indicates that Mexico and the U.S. may exchange more international traffic than any other two countries in the world within the next two years. As the regulatory environments allow, we also plan to establish framework in other Latin American countries as well. In addition to facilities we own or operate in the U.S. and Mexico, we currently own or have rights to use facilities in and have strategic relationships with carriers in Costa Rica, El Salvador, and Guatemala.

Utilizing the framework described above, we provide local, domestic long distance and international calls from our own public telephones and communication centers within Mexico, and provide similar services to some third party-owned communication centers, public telephones and hotels in Mexico. Consumers visiting a Company-owned communication center or public telephone may dial directly to the desired party in exchange for cash payment, or can charge the call to a U.S. address (collect, person-to-person, etc.) or calling card, or to a U.S. dollar-denominated credit card with the assistance of an operator.

Utilizing the same framework described above, we also serve as a facilities-based provider of network services for corporate clients and U.S. and Latin American telecommunications carriers. These customers typically lack transmission facilities into certain markets, or require additional capacity into certain markets. We currently provide these services to and from the United States, Mexico, and Costa Rica.

We also own approximately 73% 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. Utilizing CuteFTP as its flagship product, GlobalSCAPE's downloads of products increased from approximately 2.32 million for the quarter ended January 31, 2000 to approximately 3.91 million for the quarter ended January 31, 2001, respectively.

As discussed in Note 5 to our consolidated financial statements we have determined that we have three reportable operating 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, Postpaid and Integrated Prepaid Services. GlobalSCAPE, Inc. and its operations are accounted for exclusively as a part of the Internet e-commerce operating segment.

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 January 31, 2001. Additionally, we have had recurring negative cash flows from operations with the exception of the three-month periods ended January 31, 1998 and October 31, 1999. 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 half of fiscal 2001. However, we cannot guarantee 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 six-month periods ended January 31, 2000 and 2001.

	Three months ended January 31,				Six mont	
	2000		2001		2000	
			(unaudited)			
	$	%	$	%	$	%
Operating revenues:						
Telco Services						
Network services	$ 6,891	65%	$ 5,122	64%	$ 12,997	6
Integrated prepaid	1,520	14%	1,505	19%	2,922	1
Postpaid	987	9%	169	2%	2,162	1
Internet e-commerce	1,290	12%	1,254	15%	2,071	1
Total operating revenues	10,688	100%	8,050	100%	20,152	10
Cost of services	7,104	66%	5,417	67%	13,631	6
Gross margin	3,584	34%	2,633	33%	6,521	3
Selling, general and administrative expense	3,252	31%	4,057	50%	6,627	3
Bad debt expense	93	1%	79	1%	212	
Depreciation and amortization	1,427	13%	1,087	14%	2,335	1

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Operating loss	(1,188)	(11%)	(2,590)	(32%)	(2,653)	(1
Other, net	(624)	(6%)	100	1%	(1,106)	(
Net loss	(1,812)	(17%)	(2,490)	(31%)	(3,759)	(1
Income tax & minority interest, net	-	0%	89	1%	-	
Less: preferred dividends	(791)	(7%)	(233)	(3%)	(2,051)	(1
Net loss to common stockholders	($2,603)	(24%)	($2,634)	(33%)	($5,810)	(2

Three Months Ended January 31, 2001 Compared to Three Months Ended January 31, 2000

Operating revenues. Operating revenues decreased approximately $2.6 million, or 25%, primarily due to significant decreases in our network services and postpaid services revenues.

Network services, which represent sales to corporate and/or carrier

customers who utilize portions of the Company's international network to move communications traffic, decreased approximately $1.8 million, or 26% between quarters. This decline was principally due to a decline in the price per unit the Company charged for carrying communication traffic from quarter to quarter. The actual traffic processed increased approximately 12% from the quarter ended January 31, 2000 to the quarter ended January 31, 2001. Network services is a highly competitive and volatile industry with the key component being the price per unit. The price per unit declined between quarters as the Company carried significantly less non-equal access (NEA) traffic quarter to quarter. NEA traffic results in a higher revenue per unit as well as significantly higher costs per unit. During the quarter ended January 31, 2000, approximately 50% of the traffic carried was NEA traffic as compared to approximately 2% of NEA traffic carried during the quarter ended January 31, 2001.

Postpaid service revenues decreased approximately $818,000, or 83% between quarters. The decline was principally attributable to lower volumes of operator-assisted calls originating in Mexico and terminating in the U.S. Management continues to de-emphasize its postpaid services business as it focuses its efforts on the core services of the Company.

Our integrated prepaid and e-commerce services remained relatively flat between the quarters ended January 2000 and 2001.

Cost of Services. Cost of services decreased approximately $1.7 million, or 24%, between quarters and increased slightly as a percentage of revenues from 66% to 67%. The decrease in cost of services was principally attributable to the decline in the variable cost of our network services product. As mentioned previously, the mix of our carrier services product changed between quarters as the Company went from carrying a high percentage of NEA traffic for the quarter ended January 31, 2000 to a low percentage of NEA traffic for the quarter ended January 31, 2001. The increase in cost of sales, as a percentage of revenues, was due primarily to a decline in our network services gross margin between quarters. The decline in our network services gross margin led to an increase in the combined telco operations cost of services from 75% to 79% between the quarters.

Selling, General and Administrative (SG&A) Expense. SG&A expenses increased 25%, or approximately $805,000, between quarters. As a percentage of revenues, these expenses increased from 31% to 50% between quarters. Our e-commerce subsidiary accounted for approximately 87% or

$702,000 of the increase between quarters. This increase was a result of increased salaries and wages related to personnel growth, increased research and development (R&D) costs associated with the enhancing of its existing products as well as costs related to the subsidiary's relocation to its new office space, professional fees related to public filings and other matters, and travel to promote and market GlobalSCAPE's products. SG&A costs associated with our telco businesses slightly increased from approximately $2.8 million to $2.9 million between quarters or approximately 4%. The increase in SG&A, as a percentage of revenues, was principally attributable to the decline in revenues between quarters.

Depreciation and Amortization. Depreciation and amortization decreased approximately $341,000, or 24%, between quarters and remained relatively flat as a percentage of revenues. The decrease was primarily related to the Company fully amortizing acquisition costs as of July 31, 2000. The Company historically recognized approximately $66,000 per month related to this intangible asset. Additionally, during the quarter ended January 31, 2000, the Company fully depreciated approximately $165,000 of our fixed assets for which we believed there were no associated future benefits.

Operating Loss. Our operating loss increased approximately $1.4 million between quarters and increased as a percentage of revenues from 11% to 32%, due primarily to an increase in selling, general and administrative expenses.

Other Income (Expense). Other income (expense) improved approximately $724,000 between quarters from an expense of approximately $624,000 to income of approximately $100,000. This improvement was principally attributable to a $500,000 gain recognized from the settlement of a litigation case with one of our carrier customers. In addition, during the quarter ended January 31, 2000, debt discount expense was being recognized that was associated with our convertible notes and a note payable. These notes were fully converted in fiscal year 2000.

Preferred Dividends. During the second quarter of fiscal 2001, we recorded approximately $233,000 of non-cash dividends and beneficial conversion feature expense related to cumulative convertible preferred stock as compared to approximately $791,000 during the second quarter of fiscal 2000. As of December 31, 2000, the Company recognized the last amount of amortization expense related to the beneficial conversion feature.

Net loss. The net loss between quarters increased approximately $31,000 or 1% due primarily to decreased revenues and increased selling, general, and administrative expenses. This increase was somewhat offset by the improvement in other income, and the decrease in preferred stock expenses.

Six Months Ended January 31, 2001 Compared to Six Months Ended January 31, 2000

Operating revenues. Operating revenues decreased approximately $4.6 million, or 23%, principally due to declines in our network services and postpaid services. This decrease was offset to some extent by the increase in our Internet e-commerce business.

Network services decreased approximately $3.5 million, or 27% between periods. This decline is related to several changes within the industry, which has resulted in pricing pressures and much lower per-unit revenues for carrier-to-carrier services. Management believes the entrance of new alternative long distance providers into the Mexican market has resulted in several changes, most notably more fiber optic capacity, particularly in the crystal triangle made up of Mexico City, Guadalajara and

Monterrey; a steady increase in the calling options available within Mexico; and a decrease in the cost of long distance phone calls due to more competition. As a result, large increases in volumes have resulted in comparatively smaller revenue increases, and lower margins on network services. While the volume of traffic processed by the Company increased by approximately 10% between the periods, revenues actually decreased.

Postpaid service revenues decreased approximately $1.7 million, or 77% between periods. As a result of the industry changes made within Mexico mentioned above, callers now have a variety of ways to make calls from public telephones or cellular telephones, many of which are made on a prepaid basis at lower premiums than postpaid calls. As a result of the decreasing volumes of postpaid calls generated and processed by the Company, and lower margin associated with those calls, the Company stopped providing these services to most non-owned locations, closed its operator center in November 1999 and began utilizing the services of third-party owned operator centers. Management continues to de-emphasize its postpaid services business as it focuses its efforts on the core services of the Company.

Our Internet e-commerce services increased approximately $605,000, or 29% between periods. While downloads grew from nearly 4.3 million during the six-months ended January 2000 to approximately 6.6 million during the six-months ended January 2001, actual registrations declined from approximately 87,000 for the six months ended January 31, 2000 to approximately 82,000 for the six months ended January 31, 2001. Although registrations declined period to period, the revenue per registration increased as GlobalSCAPE sold fewer multi-seat licenses during the six months ended January 31, 2001 as compared to the same period in

the prior year.

Our integrated prepaid services remained relatively flat between the periods ended January 2000 and 2001.

Cost of Services. Cost of services decreased approximately $2.7 million, or 20% between periods, but increased as a percentage of revenues from 68% to 70% between periods. The decrease in cost of services was principally attributable to the decline in the variable cost of our network services product. The increase in cost of sales, as a percentage of revenues, was due primarily to the decline in our network services gross margin between the periods, which led to an increase in the combined telco operations cost of services from 75% to 84% between the periods.

Selling, General and Administrative (SG&A) Expense. SG&A expenses increased 40%, or approximately $2.7 million, between periods. As a percentage of revenues, these expenses increased from 33% to 60%, between periods. Our e-commerce subsidiary accounted for approximately 60% or $1.6 million of the increase between the periods. The majority of the subsidiary's increase relates to increased salaries and wages, professional fees related to the Form 10 and other SEC filings, R&D costs related to existing product enhancements and the development of new products, and compensation expense associated with the granting of stock options. SG&A costs associated with our telco businesses accounted for the remaining 40% increase, or $1.1 million, between periods. Approximately $914,000 of this increase was principally attributed to expenses recognized during the first quarter ended October 31, 2000. During the quarter ended October 31, 2000, the Company recorded and incurred expenses related to severance packages and professional fees related to SEC filings, strategic research services, and the recently terminated Genesis transaction.

Depreciation and Amortization. Depreciation and amortization decreased slightly from $2.3 million to $2.2 million or 4%, between periods. The principal reason for the decrease is related to the

Company fully amortizing acquisition cost during fiscal 2000. This decrease was offset somewhat by purchases of equipment during the period.

Operating Loss. Our operating loss increased approximately $4.4 million between periods and increased as a percentage of revenues from 13% to 45%, due to lower network service margins and increases in selling, general, and administrative expenses.

Other Income (Expense). Other income (expense) improved approximately $1.0 million or 90%, between periods. This improvement relates to approximately $495,000 of debt discount expense recognized in the period ended January 2000 associated with our convertible notes and a note payable that were fully converted in fiscal 2000, and a $500,000 gain recognized as a result of the settlement of a litigation case with one of our carrier customers.

Preferred Dividends. During the six months ending January 31, 2001, we recorded approximately $1.1 million of non-cash dividends and beneficial conversion feature expense related to cumulative convertible preferred stock. This compares with approximately $2.1 million of non-cash dividends and beneficial conversion feature expense during the six months ending January 31, 2000. As of December 31, 2000, the Company recognized its last month of amortization for the beneficial conversion feature expense. The net proceeds from preferred stock issuances were approximately $2.2 million for the six-month period ended January 2001.

Net loss. The net loss for the six months ended January 31, 2001 increased approximately $2.4 or 41%, between periods. The increase was principally attributed to lower carrier service margins and increases in selling, general and administrative expenses. This increase was somewhat offset by the improvement in other income and the decrease in preferred stock expenses.

Liquidity and Capital Resources

Due to lower margin revenues and the overall revenue decline during the three and six months ended January 31, 2001, the Company did not sufficiently cover our selling, general and administrative costs which resulted in negative cash flows from operations. The amount of cash used in our operations is a result of the net loss incurred during the period, the timing of cash receipts from our customers, as well as activities related to payments to our vendors. We have historically operated with negative cash flows and have sought to fund those losses and deficits through the issuance of debt and the completion of private equity placements.

For the six-months ended January 31, 2001, our net loss, after adjustments for non-cash items (depreciation and amortization, amortization of debt discount, deferred compensation, provision for losses on accounts receivable and minority interest) was approximately $4.4 million. Management of the operating assets and liabilities, which consists mainly of collections on accounts receivable and payments made on outstanding payables and accrued liabilities, produced positive cash flows of approximately $2.4 million, resulting in the negative operating cash flows for the period of $2.0 million. Accordingly, our accounts payable balance increased by approximately $2.3 million from July 31, 2000.

During the six-months ended January 31, 2001, the Company acquired approximately $604,000 in equipment which was not financed through capital lease or financing arrangements. Additional cash outflows included the payment of approximately $602,000 towards our capital lease obligations and an additional $417,000 towards note payables. As of January 31, 2001, the Company has an additional

$760,000 of equipment related to its infrastructure build-out included in its accounts payable balance. The Company expects that it will be able to finance this equipment through long-term capital lease arrangements resulting in a corresponding improvement in its working capital deficit.

For the quarter ended January 31, 2001, our net loss, after adjustments for non-cash items (depreciation and amortization, amortization of debt discount, deferred compensation, provision for losses on accounts receivable and minority interest) was approximately $1.2 million. Management of the operating assets and liabilities, which consists mainly of collections on accounts receivable and payments made on outstanding payables and accrued liabilities, produced negative cash flows of approximately $163,000, resulting in the negative operating cash flows for the period of $1.4 million. Accordingly, our combined accounts payable balance increased by approximately $921,000 between October 31, 2000 and January 31, 2001.

During the quarter ended January 31, 2001, the Company acquired approximately $308,000 in equipment which was not financed through capital lease or financing arrangements. Additional cash outflows included the payment of approximately $390,000 towards our capital lease obligations and an additional $59,000 towards note payables.

Until we are able to produce positive cash flows from operations on a recurring basis, and reduce or eliminate our working capital deficit, 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. Until then, our operating activities may result in net cash being used, or provided, during quarterly periods, regardless of our income statement results for the periods. As noted in our Form 10-K, 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.

In an effort to improve our working capital position, management reduced the Company's SG&A between the quarters ended October 2000 and January 2001 by approximately $1.2 million by reducing departmental overhead spending and the elimination of a number of personnel positions. Although management has made strides to reduce the working capital deficit, our accounts payable increased approximately $921,000 for the quarter. The net result of the Company's operating, investing and financing activities during the quarter was a working capital deficit at January 31, 2001 of approximately $9.9 million and cash on hand of approximately $757,000. This represents a $2.3 million and a $4.6 million increase in our working capital deficit from $7.6 million at October 31, 2000 and $5.3 million at July 31, 2000, respectively.

Included in the Company's current obligations are notes payable and convertible debt of approximately $456,000 and $565,000, respectively. The terms of the convertible debt that originally matured on November 30, 2000 gave the Company the option to extend the maturity date two additional thirty-day periods. The Company elected to use its option that extended the maturity date to January 31, 2001. Subsequent to January 31, 2001, the Company negotiated with the holder of the convertible debt to extend the maturity until July 31, 2001 under the same terms as before. The Company's current obligations also include the total obligation under its debt facility with NTFC Capital Corporation due to the Company's non-compliance with various covenants of the debt facility as of January 31, 2001. Although the Company does not anticipate NTFC Capital Corporation calling the amounts due under the

debt facility, the Company has classified the debt as current in accordance with accounting principles generally accepted in the U.S. Based upon our results before and after the period ended January 31, 2001, we will most likely be in default of these same covenants at the end of our next fiscal quarter April 30, 2001. As such, we have requested that NTFC review our current business plan, including expected results and capital requirements, in order to re-set the financial covenants applicable to the Company's capital lease obligation and prevent events of default from occurring on a quarterly basis going forward. Based on discussions with NTFC, management believes it is probable that NTFC will re-set the financial covenants after it has completed its review of this information, but can provide no assurance this will occur.

As planned, we continued to shift our focus away from traffic generated outside of our core market of Mexico, and focused on generating and transporting traffic over our own international network infrastructure in an effort to produce better cash flow results. The result was an increase in the volume of carrier services traffic transported over our network as compared to the prior year's quarter. Although the Company has emphasized a desire to transport a higher percentage of retail vs. wholesale traffic in order to produce better margins and cash flows, and had entered into a definitive agreement to purchase Genesis Communications International, Inc. in an effort to do so, the Company announced on February 26, 2001 that the agreement had been terminated. As such, the Company will most likely be dependent upon growth in its network services business in order to improve cash flow results in the near term. Although the Company has historically been subject to pricing pressures and declining per-unit revenues related to this business, through the management of the mix of traffic processed the Company was able to increase its revenue per unit during the quarter ended January 31, 2001 as compared to the quarter ended October 31, 2000. No assurance may be given that this trend will continue, however.

Given its dependency on network services business, in order for the Company to improve its financial performance going forward it must be able to expand its network capacity to allow for the processing of more traffic and continuously attempt to reduce both its variable and fixed costs of transporting this traffic. In January 2001, the Company announced that it had increased capacity on its fiber-based international network backbone; however, its ability to

transport additional international traffic for other carriers is also dependent on additional capacity being provided by other carriers within Mexico outside of its network backbone, as well as the Company's ability to extend its own network backbone under its Mexican long distance concession to connect to the local telecommunications network in Mexico. The Company's largest variable cost of processing traffic has historically been with other carriers in Mexico, primarily a single carrier within Mexico. In order to obtain additional capacity within Mexico and to lower its variable cost of processing this traffic within Mexico in the near term, the Company must obtain additional interconnection agreements with other long distance carriers within Mexico. This would provide additional capacity, as well as give the Company the ability to route its traffic on a least-cost basis. Longer term, the Company must focus on extending its own network infrastructure within Mexico in order to convert existing variable per-unit costs to fixed costs where possible. Any such network build-out is not expected to occur until the latter half of calendar 2001.

While there may be some equity funding requirements related to any such network build-out, the Company expects to finance the majority of its build-out needs through capital lease or debt facilities. In addition, the Company is actively exploring ways to capitalize on its ownership in GlobalSCAPE, and has engaged Roth Capital Partners, Inc. to assist it in doing so. The Company would like to liquidate, or leverage off of, its ownership in GlobalSCAPE in order to reduce, or eliminate, its current working capital deficit. Given the current and anticipated market conditions, we believe that it is most likely a private sale of all or part of our ownership of GlobalSCAPE that best helps us achieve our objective.

Inflation/Foreign Currency

Inflation has not had a significant impact on the Company's operations. With the exception of integrated prepaid 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 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.

Seasonality

The Company's integrated prepaid revenues are typically higher on a per phone and per communication center basis during January through July, the peak tourism months in Mexico.

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 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 2 Changes in Securities and Use of Proceeds

Our Registration Statement on Form S-3 (File No. 333-50008), on which we registered 19,568,940 shares of common stock, became effective on November 27, 2000. This common stock is issuable under the terms of our Series E Preferred Stock and a warrant for the purchase of 3,636,364 shares of common stock to RGC International Investors. Included in this Registration Statement are the terms of two warrants for the purchase of 75,000 and 100,000 shares of common stock to Jesup & Lamont Securities Corporation and Binkley LLC, issued in conjunction with the signing of our private equity line of credit in April 2000.

We did not receive any of the proceeds of the sale of common stock registered on this Form S-3. We received $2.5 million of proceeds upon the issuance of the Series E Preferred Stock in October 2000. We incurred expenses in connection with the issuance of the series E preferred stock and registration of the underlying common stock as follows (approximate amounts except for the SEC registration fees):

Legal fees:	$ 5,000.00
Registration fees:	6,309.30
Printing & Miscellaneous:	5,500.00
Total:	16,809.30

We used the remaining proceeds after payment of expenses for working

capital purposes.

Item 6 Exhibits and Reports on Form 8-K

(a) Exhibits:

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 March 16, 2001)

(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.

AMERICAN TELESOURCE INTERNATIONAL INC.
(Registrant)

Date: March 16, 2001

By: /s/ H. Douglas Saathoff

Name: H. Douglas Saathoff
Title: Chief Financial Officer

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