ADVANCED MATERIALS GROUP INC
Form 10-Q
July 15, 2002

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U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

ý **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the quarterly period ended May 31, 2002.

or

o **TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT**

For the transition period from to

Commission File No. 0-16401

ADVANCED MATERIALS GROUP, INC.

(Exact name of small business issuer as specified in its charter)

Nevada	**33-0215295**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20211 S. Susana Road, Rancho Dominguez, California 90221
(Address of principal executive offices)

(310) 537-5444
Issuer's telephone number

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or such shorter period that the issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ý Yes o No

Indicate the number of shares outstanding of each of the issuer's class of common equity, as of the latest practicable date:

COMMON STOCK, $.001 PAR VALUE, 8,671,272 SHARES AS OF JULY 13, 2002.

ADVANCED MATERIALS GROUP, INC.

FORM 10-Q

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PART I FINANCIAL INFORMATION

ITEM I CONSOLIDATED FINANCIAL STATEMENTS

ADVANCED MATERIALS GROUP, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended		Six Months Ended	
	May 31, 2002	May 31, 2001	May 31, 2002	May 31, 2001
Net sales	$ 9,258,000	$ 9,955,000	$ 17,918,000	$ 19,904,000
Cost of sales	8,378,000	8,874,000	16,239,000	17,755,000
Gross profit	880,000	1,081,000	1,679,000	2,149,000

	Three Months Ended		Six Months Ended	
Operating expenses:				
Selling, general and administrative	783,000	1,125,000	1,667,000	2,294,000
Depreciation and amortization	93,000	90,000	177,000	170,000
Restructuring costs		1,440,000		1,440,000
Total operating expenses	876,000	2,655,000	1,844,000	3,904,000
Income (loss) from operations	4,000	(1,574,000)	(165,000)	(1,755,000)
Other income (expense):				
Interest expense	(96,000)	(132,000)	(189,000)	(292,000)
Foreign exchange gain	18,000	25,000	21,000	14,000
Other, net	(26,000)	(28,000)	(41,000)	(44,000)
Total other expenses, net	(104,000)	(135,000)	(209,000)	(322,000)
Loss before income taxes	(100,000)	(1,709,000)	(374,000)	(2,077,000)
Income tax expense	(11,000)	(17,000)	(20,000)	(41,000)
Net loss	$ (111,000)	$ (1,726,000)	$ (394,000)	$ (2,118,000)
Basic and diluted loss per common share	$ (0.01)	$ (0.20)	$ (0.05)	$ (0.24)
Basic and diluted weighted average common shares outstanding	8,671,272	8,671,272	8,671,272	8,671,272

See accompanying notes to consolidated financial statements

ADVANCED MATERIALS GROUP, INC.

CONSOLIDATED BALANCE SHEETS

(Unaudited)

	May 31, 2002	November 30, 2001
ASSETS		
Current assets:		
Cash and cash equivalents	$ 660,000	$ 1,303,000
Accounts receivable, net	5,487,000	6,401,000
Inventories, net	3,582,000	3,551,000

	May 31, 2002		November 30, 2001
Prepaid expenses and other		318,000	308,000
Total current assets		10,047,000	11,563,000
Property and equipment, net		2,521,000	2,654,000
Goodwill, net		355,000	387,000
Other assets		173,000	168,000
Total assets	$	13,096,000	$ 14,772,000

LIABILITIES AND STOCKHOLDERS' EQUITY

		May 31, 2002		November 30, 2001
Current liabilities:				
Accounts payable	$	5,667,000	$	6,457,000
Accrued liabilities		643,000		838,000
Restructuring reserve,current		357,000		406,000
Deferred income		152,000		255,000
Line of credit		2,858,000		2,788,000
Current portion of long-term obligations		660,000		708,000
Total current liabilities		10,337,000		11,452,000
Convertible debentures		405,000		405,000
Deferred compensation, net of current protion		1,129,000		1,129,000
Restructuring reserve, net of current portion		488,000		647,000
Capital leases, net of current portion		226,000		234,000
Total liabilities		12,585,000		13,867,000
Commitments and contingencies				
Stockholders' equity:				
Preferred stock $.001 par value; 5,000,000 shares authorized no shares issued and outstanding				
Common stock $.001 par value; 25,000,000 shares authorized; 8,671,272 shares issued and outstanding at May 31, 2002 and November 30, 2001		9,000		9,000
Additional paid-in capital		7,083,000		7,083,000
Accumulated deficit		(6,581,000)		(6,187,000)
Total stockholders' equity		511,000		905,000
Total liabilities and stockholders' equity	$	13,096,000	$	14,772,000

See accompanying notes to consolidated financial statements

ADVANCED MATERIALS GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended	
	May 31, 2002	**May 31, 2001**
Cash flows from operating activities:		
Net loss	$ (394,000)	$ (2,118,000)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation	417,000	406,000
Amortization	32,000	32,000
Provision for bad debt	90,000	
Provision for obsolete inventory	24,000	262,000
Interest on deferred compensation	70,000	78,000
(Gain) loss on disposal of fixed assets	(13,000)	15,000
Changes in operating assets and liabilities:		
Accounts receivable	824,000	976,000
Inventories	(55,000)	1,051,000
Prepaid expenses and other	(15,000)	1,000
Accounts payable and accrued liabilities	(985,000)	(1,384,000)
Restructuring reserve	(208,000)	1,293,000
Deferred income	(103,000)	71,000
Net cash (used in)provided by operating activities	(316,000)	683,000
Cash flows from investing activities:		
Purchases of property and equipment	(182,000)	(378,000)
Proceeds from sale of fixed assets	13,000	
Increase in other assets		(66,000)
Net cash used in investing activities	(169,000)	(444,000)
Cash flows from financing activities:		
Net borrowings (repayments) under line of credit	70,000	(474,000)
Repayments of other long-term obligations	(228,000)	(131,000)
Net cash provided by (used in) financing activities	(158,000)	(605,000)
Net change in cash and cash equivalents	(643,000)	(366,000)
Cash and cash equivalents, beginning of period	1,303,000	1,101,000
Cash and cash equivalents, end of period	$ 660,000	$ 735,000

Supplemental disclosures of cash flow information

	Six Months Ended	
Cash paid during the period for:		
Interest	$ 193,000	$ 288,000
Income taxes	$	$

See accompanying notes to consolidated financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1) BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission and therefore do not include all information and footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America.

The unaudited consolidated financial statements do, however, reflect all adjustments, consisting of only normal recurring adjustments, which are, in the opinion of management, necessary to state fairly the financial position as of May 31, 2002 and November 20, 2001 and the results of operations and cash flows for the related interim periods ended May 31, 2002 and 2001. However, these results are not necessarily indicative of results for any other interim period or for the year. It is suggested that the accompanying consolidated financial statements be read in conjunction with the Company's Consolidated Financial Statements and accompanying notes thereto included in the Company's Annual Report on Form 10-K.

The Company has incurred substantial losses form operations, has a working capital deficit and has not been in compliance with minimum net income, minimum book net worth and debt service coverage ratio and therefore is in technical default under the compliance provisions of its bank line of credit and term loan. In order to fund present and future operations, the Company needs to cure its covenant violations with its lender or find a replacement lender with acceptable terms. While the Company is in the process of attempting to cure its line of credit violations, and has initiated plans to return to profitability, there are no assurances that the Company will be successful in completing these critical tasks. If the Company is unable to successfully complete these critical tasks, it may be forced to reduce its operations and/or liquidate inventory at amounts below current carrying value to generate the necessary working capital to fund its operations.

2) INVENTORIES

Inventories are stated at the lower of cost (determined on the first-in, first-out method) or market. Inventories consisted of the following:

	May 31, 2002	November 30, 2001
	(unaudited)	
Raw Materials	$ 1,883,000	$ 2,235,000
Work-in-process	285,000	209,000
Finished Goods	1,562,000	1,230,000
	3,730,000	3,674,000
Less allowance for obsolete inventory	(148,000)	(123,000)
	$ 3,582,000	$ 3,551,000

3) BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE

Basic and Diluted loss per share is computed in accordance with Statement of Financial Accounting Standards No. 128 ("SFAS No. 128"). In the May 31, 2002 computations, common

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equivalent shares are excluded from diluted loss per share as their effect is antidilutive. Basic and Diluted loss for the three and six months ended May 31, 2002 and 2001 are as follows:

	Three Months Ended		Six Months Ended	
	May 31, 2002	May 31, 2001	May 31, 2002	May 31, 2001
BASIC AND DILUTED EPS:				
Net loss	$ (111,000)	$ (1,726,000)	$ (394,000)	$ (2,118,000)
Denominator: Weighted average common shares outstanding	8,671,272	8,671,272	8,671,272	8,671,272
Basic and ditluted loss per share	$ (0.01)	$ (0.20)	$ (0.05)	$ (0.24)

4) SEGMENT REPORTING

The Company's foreign operations include both manufacturing and sales. The manufacturing facility is located in Ireland and the sales joint venture is located in Singapore. Both facilities began operations in fiscal 1998. All of the sales are made to unaffiliated customers. The following is a summary of selected financial information by entities within geographic areas for the second quarter and six months ended May 31, 2002 and 2001.

Three Months Ended May 31, 2002 and May 31, 2001

Revenue:

	AMI-US Operations	AMI-Singapore	AMI Ireland	Consolidated
2002	$ 3,633,000	$ 3,111,000	$ 2,514,000	$ 9,258,000
2001	$ 5,041,000	$ 2,738,000	$ 2,176,000	$ 9,955,000

Net income (loss):

	AMI-US Operations	AMI-Singapore	AMI Ireland	Consolidated
2002	$ (216,000)	$ 107,000	$ (2,000)	$ (111,000)
2001	$ (2,065,000)	$ 252,000	$ 87,000	$ (1,726,000)

Six Months Ended May 31, 2002 and May 31, 2001

Revenue:

	AMI-US Operations	AMI-Singapore	AMI Ireland	Consolidated
2002	$ 6,923,000	$ 6,252,000	$ 4,743,000	$ 17,918,000
2001	$ 10,394,000	$ 5,171,000	$ 4,339,000	$ 19,904,000

Net income (loss):

	AMI-US Operations	AMI-Singapore	AMI Ireland	Consolidated
2002	$ (621,000)	$ 269,000	$ (42,000)	$ (394,000)
2001	$ (2,783,000)	$ 462,000	$ 203,000	$ (2,118,000)

Assets: As of May 31, 2002 and November 30, 2001

	AMI-US Operations	AMI-Singapore	AMI Ireland	Consolidated
2002	$ 6,519,000	$ 2,835,000	$ 3,742,000	$ 13,096,000
2001	$ 8,040,000	$ 3,201,000	$ 3,531,000	$ 14,772,000

5) CONTINGENT LIABILITIES

Legal proceedings to which the Company is a party are discussed in Part 1 Legal Proceedings, in the latest Annual Report on form 10-K and in Part II, Item 1 of this Form 10-Q.

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

The following discussion should be read in conjunction with the consolidated financial statements and the related notes that appear elsewhere in this document.

This document contains forward-looking statements that involve risks and uncertainties that could cause the results of the Company and its consolidated subsidiaries to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include the Company's continuing need to timely develop, produce and deliver new products; the challenge of managing asset levels, including inventory and trade receivables; the difficulty of keeping expense growth at modest levels while increasing revenues and other risks described from time to time in the Company's filings with the Securities and Exchange Commission, including but not limited to the Annual Report on Form 10-K for the year ended November 30, 2001 and in "Factors That Could Affect Future Results" below.

Forward-looking statements reflect the current views of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated or expected.

Results of Operations

FY 02 Current Three Months Versus FY 01

Net sales for the second quarter ended May 31, 2002 were $9,258,000,versus $9,955,000 for the same period of fiscal 2001, a decrease of 7%. The decrease in net revenues for the second quarter of fiscal 2002 is primarily attributable to lower domestic sales prices and volumes relating to the slowdown in domestic economic conditions.

Cost of sales for the second quarters ended May 31, 2002 and 2001 were $8,378,000 and $8,874,000, respectively. Cost of sales as a percentage of net revenue was 91% for the second quarter of fiscal 2002, compared to 89% for the second quarter of fiscal 2001. Cost of sales as a percentage of net revenue increased for the second quarter of fiscal 2002 compared to the second quarter of fiscal 2001, primarily due to lower domestic sales prices and a reduction in the Company's share of the gross profit per its agreement with its strategic manufacturing partner in Singapore.

Selling, general and administrative expenses for the second quarter of fiscal 2002 and 2001 was $783,000 and $1,125,000, respectively. The decrease was due primarily to the closure of the Company's plant in Texas near the end of fiscal year 2001 and the Company's continued focus on reducing operating expenses and optimizing manufacturing processes in order to improve operating results.

Interest expense for the second quarter of fiscal 2002 and 2001 was $96,000 and $132,000, respectively. The decrease was primarily attributable to lower average loan balances and lower interest rates.

Net loss for the second quarter of fiscal 2002 was $111,000, compared to a net loss of $286,000 net of restructuring charges of $1,440,000 for the second quarter of 2001. Basic and diluted loss per share for the second quarter of fiscal 2002 was $0.01 per share on a weighted average of 8.7 million shares, compared to $0.20 on a weighted average of 8.7 million shares for the second quarter of fiscal 2001. The reduction in net loss was primarily attributable to reduced operating expenses for domestic operations.

FY 02 Six Months Versus FY 01

Net sales for the six months ended May 31, 2002 were $17,918,000 versus $19,904,000 for the same period of fiscal 2001. Net sales continue to slow due to domestic economic conditions.

Cost of sales for the six months ended May 31, 2002 and May 28, 2001 was $16,239,000 and $17,755,000, respectively. Cost of sales as a percentage of net revenue was 91% for the six months of fiscal 2002,compared to 89% for the six months of fiscal 2001. Cost of sales as a percentage of net revenue increased for the six months of fiscal 2002, compared to the six months of fiscal 2001 primarily due to lower sales prices and a decrease in the Companies share of the gross profit per its agreement with its strategic manufacturing partner in Singapore.

Selling, general and administrative expenses for the six months ended May 31, 2002 and 2001 were $1,667,000 and $2,294,000, respectively. The decrease was due primarily to the closure of the Company's plant in Texas near the end of fiscal year 2001 and the Company's continued focus on reducing operating expenses and optimizing manufacturing processes in order to improve operating results.

Interest expense for the six months of fiscal 2002 and 2001 was $189,000 and $292,000, respectively. The decrease is due to lower average loan balances and lower interest rates.

Net loss for the six months of fiscal 2002 and 2001 was $394,000 and $678,000 resepctively, excluding restructuring charges. Basic and diluted loss per share for the six months of fiscal 2002 was $0.05 per share on a weighted average of 8.7 million shares, compared to $0.24 on a weighted average of 8.7 million shares for the six months of fiscal 2001.

Segment Information

The following is a discussion of operating results for each of the Company's business segments. Quarterly financial data for each segment can be found in Note 4 to these consolidated financial statements. The reportable segments disclosed in this Form 10-Q are based on the Company's internal management responsibility.

FY 02 Current Three Months Versus FY 01

AMI-U.S. Operations

Net sales for the second quarter ended May 31, 2002 were $3,633,000, compared to net sales for the second quarter ended May 31, 2001 of $5,041,000. The decrease in net sales is primarily attributable to lower domestic sales prices and volumes relating to the slowdown in domestic economic conditions. The net loss for the second quarter ended May 31, 2002 was $216,000, compared to net loss for the second quarter of ended May 31, 2001 of $625,000, excluding restructuring charges of $1,440,000. The decrease in net loss is primarily attributable to the Company's continued focus on the reduction of operating expense ratios and optimization of manufacturing processes in order to improve profitability.

AMFSC-Singapore

Net sales for the second quarter ended May 31, 2002 were $3,111,000, compared to net sales for the second quarter ended May 31, 2001 of $2,738,000. The increase in net sales for the second quarter of fiscal 2002 is primarily attributable to higher volumes of component sales to computer printer manufacturers. Printer supply sales to key customer accounts have reflected continued growth in the installed base, growth in printing from the internet and increased usage of newly introduced products. Net income for the second quarter ended May 31, 2002 was $107,000, compared to net income for the second quarter ended May 31, 2001 of $252,000. The decrease in net income is primarily attributable to

the reduction in the Company's share of the gross profit per its agreement with its strategic manufacturing partner in Singapore.

AML-Ireland

Net sales for the second quarter ended May 31, 2002 was $2,514,000, compared to net sales for the second quarter ended May 31, 2001 of $2,176,000. The increase in net sales for the second quarter of fiscal 2002 is primarily attributable to higher volumes of component sales to computer printer manufacturers. Printer supply sales to key customer accounts reflected continued growth in the installed base, growth in printing from the Internet and increased usage of newly introduced products. Net loss for the second quarter ended May 31, 2002 was $2,000 compared to net income for the second quarter ended May 31, 2001 of $87,000. The decrease in net income is primarily due to lower prices for printer supply sales.

FY 02 Six Months Versus FY 01

AMI-U.S. Operations

Net sales for the six months ended May 31, 2002 was $6,923,000, compared to net sales for the six months ended May 31, 2001 of $10,394,000. The decrease in net sales is primarily attributable to lower domestic sales prices and volumes relating to the slowdown in domestic economic conditions. The net loss for the six months ended May 31, 2002 was $621,000, compared to net loss for the six months ended May 31, 2001 of $2,783,000, excluding restructuring charges the net loss was $1,343,000. The decrease in net loss excluding restructuring charges is primarily attributable to the Company's continued focus on the reduction of operating expense ratios and optimization of manufacturing processes in order to improve profitability.

AMFSC-Singapore

Net sales for the six months ended May 31, 2002 was $6,252,000, compared to net sales for the six months ended May 31, 2001 of $5,171,000. The increase in net sales for the six months of fiscal 2002 is primarily attributable to higher volumes of component sales to computer printer manufacturers. Printer supply sales to key customer accounts will reflect continued growth in the installed base, growth in printing from the internet and increased usage of newly introduced products. Net income for the six months ended May 31, 2002 was $269,000, compared to net income for the six months ended May 31, 2001 of $462,000. The decrease in net income is primarily attributable to the reduction in the Company's share of the gross profit per its agreement with its strategic manufacturing partner in Singapore.

AML-Ireland

Net sales for the six months ended May 31, 2002 was $4,742,000, compared to net sales for the six months ended May 31, 2001 of $4,339,000. The increase in net sales for the six months of fiscal 2002 is primarily attributable to higher volumes of component sales to computer printer manufacturers. Printer supply sales to key customer accounts reflected continued growth in the installed base, growth in printing from the internet and increased usage of newly introduced products. Net loss for the six months ended May 31, 2002 was $42,000, compared to net income for the six months ended May 31, 2001 of $203,000. The decrease in net income is primarily due to lower prices for printer supply sales.

Liquidity and Capital Resources

Cash and cash equivalents were $660,000 at May 31, 2002, compared with $1,303,000 at November 30, 2001. During the six months, cash flows from operating activities were used to fund operations, pay down short- and long-term debt and purchase property, plant and equipment.

Operating activities used $316,000 of cash during the second quarter of fiscal 2002, compared with generating $683,000 in the corresponding period in fiscal 2001. The decrease in cash generated from operating activities in fiscal 2002 resulted primarily from the pay down of accounts payable and accrued liabilities and the restructuring reserve.

Inventory at May 31, 2002 was $3,582,000, compared to $3,551,000 at November 30, 2001.

Net trade receivables at May 31, 2002 were $5,487,000, compared to $6,401,000 at November 30, 2001. The decrease is due to a reduction in domestic net sales and a decrease in terms for certain foreign sales.

Capital expenditures were $182,000 for the six months in 2002, compared to $378,000 for the corresponding period in fiscal 2001. The Company has instituted a Company-wide program to reduce non-essential capital expenditures, which are not specifically focused on revenue growth.

The Company uses short- and long-term borrowings to supplement internally generated cash flow. Short- and long-term borrowings in the six months of 2002 decreased by $158,000.

The Company had $660,000 of cash and cash equivalents at May 31, 2002. The Company has a $4,500,000 operating credit line with its primary lenders with approximately $2,858,000 currently outstanding as of May 31, 2002, which expires in February 2003. The Company has an outstanding term loan of $343,000 as of May 31, 2002 with the same bank. The term loan bears interest at prime plus 3.25% (8.25% at May 31, 2002). The Company anticipates that existing cash, cash from operations and existing lines of credit will supply sufficient cash for its short and long term projected needs for operations as long as the Company is successful in curing its covenant violations or finding a replacement lender with acceptable terms. (See discussion below).

At May 31, 2002, the Company has a working capital deficit and was not in compliance with minimum net income, minimum book net worth and debt service coverage ratio and therefore is in technical default under the compliance provisions of its bank line of credit and term loan. In order to fund present and future operations, the Company needs to cure its covenant violations with its lender or find a replacement lender with acceptable terms. While the Company is in the process of attempting to cure its line of credit violations, and has initiated plans to return to profitability, there are no assurances that the Company will be successful in completing these critical tasks. If the Company is unable to successfully complete these critical tasks, it may be forced to reduce its operations and/or liquidate inventory at amounts below current carrying value to generate the necessary working capital to fund its operations.

Factors That Could Affect Future Results

Competition The Company encounters aggressive competition in all areas of its business. It has numerous competitors, ranging from several comparable-size companies to many relatively small companies. The majority of the competitors are private, closely held companies. There is also a risk that a supplier to the Company could become a competitor. The Company competes primarily on the basis of performance, price, quality and customer service. Product life cycles are short, with numerous small one-time customer orders. To remain competitive, the Company must be able to quickly develop new products and enhance existing products in response to customer demands. In particular, management anticipates a continuing need to lower the prices of many of the Company's products to stay competitive and effectively manage financial returns with resulting reduced gross margins. In some of its markets, the Company may not be able to successfully compete against current and future competitors, and the competitive pressures faced could harm the business and prospects.

New Product Introductions If the Company cannot continue to rapidly develop and manufacture innovative products that meet customer requirements for performance, price, quality and customer service, it may lose market share and future revenue and earnings may suffer. The process of

developing new products and corresponding manufacturing processes is complex and uncertain. The customer decision-making process can be lengthy and some raw materials have extremely long lead times. These circumstances often lead to long delays in new product introductions. After a product is developed, the Company must be able to manufacture sufficient volumes quickly at low enough costs. To do this it must accurately forecast volumes and mix of products. Customer orders have also been subject to dramatic swings from customer provided forecasts. Thus, matching customers' demand and timing for particular products makes the process of planning production and managing inventory levels increasingly difficult.

Short Product Life Cycles The short life cycles of many of the Company's products pose a challenge to effectively manage the transition from existing products to new products. If the Company does not manage the transition effectively, the future revenue and earnings could suffer.

Among the factors that make a smooth transition from current products to new products difficult are delays in the customer decision-making process, development of manufacturing processes, long lead times for the delivery of raw materials and variations in product costs. The Company's future revenues and earnings could also suffer due to the timing and introduction of new product offerings, which compete directly or indirectly with its customers' products and new product offerings by its competitors.

Reliance on Suppliers The Company's manufacturing operations depend on its suppliers' ability to deliver quality raw materials and components in time for it to meet critical manufacturing and distribution schedules. The Company sometimes experiences a short supply of certain raw materials as a result of supplier out-of-stock situations or long manufacturing lead times. If shortages or delays exist, the Company's future operating results could suffer. Furthermore, it may not be able to secure enough raw materials at reasonable prices to manufacture new products in the quantities required to meet customer demand. Sudden or large raw materials price increases could also cause future operating results to suffer.

International Sales outside the United States make up more than 62% of the Company's revenues. Manufacturing for these products are also located outside of the United States. The Company's future earnings or financial position could be adversely affected by a variety of international factors, including:

Changes in a country or region's political or economic conditions,

Trade protection measures,

Import or export licensing requirements,

The overlap of different tax structures,

Unexpected changes in regulatory requirements,

Problems caused by the conversion of various European currencies to the Euro, and

Natural disasters.

Market Risk The majority of the Company's sales are denominated in U.S. dollars. All costs in Singapore and the majority of direct material costs in Ireland are also denominated in U.S. dollars. However, the Company is exposed to foreign currency exchange risk inherent in the sales commitments, anticipated sales and assets and liabilities denominated in currencies other than the U.S. dollar. See also "Item 7A. Quantitative and Qualitative Disclosures About Market Risk" in the Company's 2001 Annual Report on Form 10-K for more detailed information.

Earthquake The corporate offices and manufacturing division in California are located near major earthquake faults. The ultimate impact on the Company and its general infrastructure is unknown, but operating results could be materially affected in the event of a major earthquake. The Company is predominantly uninsured for losses and interruptions caused by earthquakes.

Environmental Some of the Company's operations use substances regulated under various federal, state and international laws governing the environment. It is our policy to apply strict standards for environmental protection to sites inside and outside the U.S., even when not subject to local government regulations. The Company has not been notified of any environmental infractions.

Profit Margin The Company's profit margins vary somewhat among its products and geographic markets. Consequently, the overall profitability in any given period is partially dependent on the product, customer and geographic mix reflected in that period's net sales.

Stock Price The Company's stock price, like that of any other small-cap company, can be volatile. Some of the factors that can affect the stock price are:

The Company's, its customer's or its competitor's announcement of new or discontinued products,

Quarterly increases or decreases in earnings,

Changes in revenue or earnings estimates by the investment community, and

Speculation in the press or investment community.

General market conditions and domestic or international macroeconomic factors unrelated to the Company's performance may also affect the stock price. For these reasons, investors should not rely on recent trends to predict future stock prices or financial results. In addition, following periods of volatility in a company's securities, securities class action litigation against a company is sometimes instituted. This type of litigation could result in substantial costs and the diversion of management time and resources.

Earnings Fluctuations Management cannot reliably predict future revenue and margin trends which may cause the Company to adjust its operations, which could cause period-to-period fluctuations in earnings.

The Company's common stock traded on the Nasdaq SmallCap Stock Market ("Nasdaq") under the symbol "ADMG" from June 23, 1993 until December 13, 2000. Effective as December 14, 2000, the Company's common stock was delisted from the Nasdaq and has traded on the NASD-regulated OTC Bulletin Board ("Bulletin Board") under the symbol "ADMG.OB."

ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

A discussion of the Company's exposure to, and management of, market risk appears in Item 2 of this Form 10-Q under the heading "Factors That Could Affect Future Results."

PART II OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits.

None

(b) Reports on Form 8-K
No reported 8-K developments submitted in quarter.

SIGNATURES

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

Dated: July 15, 2002 ADVANCED MATERIALS GROUP, INC.

By:	/s/ STEVE F. SCOTT	
	Steve F. Scott *President and CEO*	
	/s/ GAYLE ARNOLD	
	Gayle Arnold *Chief Financial Officer*	

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