MICROTEL INTERNATIONAL INC
Form 10-Q
May 15, 2003

U. S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

|X| QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended MARCH 31, 2003 or

| | TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______________ to ______________

Commission File Number 1-10346

MICROTEL INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in Its Charter)

DELAWARE	77-0226211
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

9485 HAVEN AVENUE, SUITE 100
RANCHO CUCAMONGA, CALIFORNIA 91730
(Address of Principal Executive Offices)

(909) 987-9220
(Registrant's Telephone Number, Including Area Code)

NOT APPLICABLE
(Former Name, Former Address And Former Fiscal Year, if Changed Since Last Report)

Indicate by check 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 registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes |X| No | |

Indicate by check whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes | | No |X|

As of May 9, 2003, there were 21,576,788 shares of the issuer's common stock, $0.0033 par value, outstanding.

PART I
FINANCIAL INFORMATION

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

MICROTEL INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF MARCH 31, 2003 AND DECEMBER 31, 2002
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)

ASSETS	March 31, 2003	December 31, 2002
Current assets:	(unaudited)	
Cash and cash equivalents	$ 29	$ 254
Accounts receivable, net of allowance for doubtful accounts of $163 and $130, respectively	5,179	5,356
Inventories	7,392	7,505
Prepaid and other current assets	430	343
Total current assets	13,030	13,458
Property, plant and equipment, net	392	588
Goodwill, net of accumulated amortization of $1,047 and $1,050, respectively	2,329	2,346
Other assets	527	394
	$ 16,278	$ 16,786
LIABILITIES, REDEEMABLE PREFERRED STOCK AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable	$ 2,733	$ 3,475
Current portion of long-term debt	256	318
Accounts payable	4,179	3,897
Accrued expenses	1,777	1,807
Total current liabilities	8,945	9,497
Long-term debt, less current portion	917	927
Other liabilities	329	348
Total liabilities	10,191	10,772
Convertible redeemable Series A Preferred Stock, $10,000 unit value. Authorized 200 shares; issued and outstanding 25 shares (aggregate liquidation preference of $250)	285	282
Stockholders' equity:		
Preferred stock, authorized 10,000,000 shares; Convertible Series B Preferred Stock, $0.01 par value; issued and outstanding 60,000 shares and 64,000 shares, respectively (aggregate liquidation preferences of $383 and $410, respectively)	374	400
Common stock, $0.0033 par value. Authorized 50,000,000 shares; issued and outstanding 21,577,000 and 21,535,000, respectively	71	71
Additional paid-in capital	24,926	24,900
Accumulated deficit	(19,000)	(19,042)
Accumulated other comprehensive loss	(569)	(597)
Total stockholders' equity	5,802	5,732
	$ 16,278	$ 16,786

See accompanying notes to condensed consolidated financial statements.

MICROTEL INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
THREE MONTHS ENDED MARCH 31, 2003 AND 2002
(UNAUDITED)

	Three months ended March 31, 2003	Three months ended March 31, 2002
	(in thousands, except per share amounts)	
Net sales	$ 5,668	$ 4,820
Cost of sales	3,527	3,291
Gross profit	2,141	1,529
Operating expenses:		
Selling, general and administrative	1,698	1,865
Engineering and product development	221	238
Income (loss) from operations	222	(574)
Other income (expense):		
Interest expense	(96)	(90)
Other income	(14)	4
Income (loss) before income taxes	112	(660)
Income tax expense	68	39
Net income (loss)	$ 44	$ (699)
Earnings (loss) per share:		
Net income (loss):		
Basic	$ 0.00	$ (0.03)
Diluted	$ 0.00	$ (0.03)

See accompanying notes to condensed consolidated financial statements.

MICROTEL INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
THREE MONTHS ENDED MARCH 31, 2003 AND 2002
(UNAUDITED)

	Three Months Ended March 31 2003	Three Months Ended March 31 2002
	(In Thousands)	
Net income (loss)	$ 44	$(699)
Other comprehensive income (loss) net of tax:		
Foreign currency translation adjustment	28	(38)

Comprehensive Income (loss)	$ 72	$(737)

See accompanying notes to condensed consolidated financial statements.

MICROTEL INTERNATIONAL, INC. AND SUBSIDIARIES
THREE MONTHS ENDED MARCH 31, 2003
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(UNAUDITED)
(IN THOUSANDS)

	Series B Convertible Preferred Stock		Common Stock		Additiona Paid-In Capital
	Shares	Amount	Shares	Amount	
Balance at December 31, 2002	64	400	21,535	71	24,900
Preferred Series B conversions	(7)	(26)	42	--	26
Foreign currency translation adjustment					
Accretion of redeemable preferred stock	--	--	--	--	--
Net profit	--	--	--	--	--
Balance at March 31, 2003	57	374	21,577	71	24,926

See accompanying notes to condensed consolidated financial statements.

MICROTEL INTERNATIONAL, INC. AND SUBSIDIARIES
THREE MONTHS ENDED MARCH 31, 2003 AND 2002
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three months ended March 3	
	2003	2002
	(in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 44	$(699)
Adjustments to reconcile net income (loss) to cash provided by operating activities:		
Depreciation and amortization	78	82
Provision for doubtful account	37	19
Provision for obsolete/slow moving inventory	67	119
Changes in operating assets and liabilities:		
Accounts receivable	136	482
Inventories	40	(165)

Other assets	(174)	47
Accounts payable and accrued expenses	240	394
Cash provided by operating activities	468	279
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net purchases of property, plant and equipment	(4)	(35)
Cash collected on note receivable	--	14
Cash (used in) investing activities	(4)	(21)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net (decrease) in notes payable and long-term debt	(814)	(432)
Cash (used in) financing activities	(814)	(432)
Effect of exchange rate changes on cash	125	(46)
Net (decrease) in cash and cash equivalents	(225)	(220)
Cash and cash equivalents at beginning of period	254	604
Cash and cash equivalents at end of period	$ 29	$ 384
Cash paid for:		
Income tax	$ 14	$ 9
Interest	$ 93	$ 92

See accompanying notes to condensed consolidated financial statements.

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MICROTEL INTERNATIONAL, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2003 AND 2002
(UNAUDITED)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION AND BUSINESS

MicroTel International, Inc. (the "Company") operates through three wholly-owned subsidiaries: CXR Telcom Corporation ("CXR Telcom"), CXR, S.A.S. ("CXR France") and XET Corporation, formerly XIT Corporation ("XET"). XET and its subsidiaries design, develop, manufacture and market digital and rotary switches and power supplies and subsystem assemblies. CXR Telcom and CXR France design, develop, manufacture and market transmission and network access products and communications test equipment. The Company conducts its operations out of various facilities in the United States, France, England and Japan and organizes itself in two product line segments: electronic components and communications equipment.

BASIS OF PRESENTATION

The accompanying unaudited condensed 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 generally accepted accounting principles.

The unaudited condensed 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 March 31, 2003 and December 31, 2002 and the results of operations and cash flows for the related interim periods ended March 31, 2003 and 2002. However, these results are not necessarily indicative of results for any other interim period or for the year. It is suggested that the accompanying condensed consolidated financial statements be read in conjunction with the Company's audited consolidated financial statements included in its 2002 annual report on Form 10-K.

STOCK-BASED COMPENSATION

In December 2002, the Financial Accounting Standards Board ("FASB") issued FASB Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure-An Amendment of SFAS 123." SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company has chosen to continue to account for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Bulletin Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. Accordingly, compensation expense for stock options is measured as the excess, if any, of the estimate of the market value of our stock at the date of the grant over the amount an employee must pay to acquire the stock. The Company has adopted the disclosure provisions of SFAS No. 148 for its financial reports. Because this standard involves disclosures only, the adoption of this standard did not have a material impact on the Company's results of operations, financial position or liquidity.

The following table sets forth the net income (loss), net income (loss) available for common stockholders and earnings (loss) per share amounts for the periods presented as if the Company had elected the fair value method of accounting for stock options for all periods presented:

	Three months ended March 31, 2003	Three months ended March 31, 2002

Net income (loss)		
As reported	$ 44,000	$ (699,000)
Pro forma	$ 31,000	$ (707,000)
Net income (loss) available for common stockholders (less accretion of preferred stock)		
As reported	$ 42,000	$ (702,000)
Pro forma	$ 29,000	$ (710,000)
Basic earnings (loss) per share		
As reported	$ 0.00	$ (0.03)
Pro forma	$ 0.00	$ (0.03)
Diluted earnings (loss) per share		
As reported	$ 0.00	$ (0.03)
Pro forma	$ 0.00	$ (0.03)

The above calculations include the effects of all grants in the periods presented. Because options often vest over several years and additional awards are made each year, the results shown above may not be representative of the effects on net income (loss) in future periods. The calculations were based on a Black-Scholes pricing model with the following assumptions: no dividend yield; expected volatility of 93%; risk-free interest rate of 2%-3%; expected lives of 7 years.

(2) EARNINGS (LOSS) PER SHARE

The following table illustrates the computation of basic and diluted earnings (loss) per share (in thousands, except per share amounts):

	Three months ende	
	2003	
	(in thousands, excep amounts)	
NUMERATOR:		
Net income (loss)	$ 44	
Less: accretion of the excess of the redemption value over the carrying value of redeemable preferred stock	(2)	
Income (loss) attributable to common stockholders	$ 42	$
DENOMINATOR:		
Weighted average number of common shares outstanding during the period	21,545	
Incremental shares from assumed conversions of warrants, options and preferred stock	1,862	
Adjusted weighted average shares	23,407	
Basic earnings (loss) per share	$ 0.00	$
Diluted earnings (loss) per share	$ 0.00	$

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MICROTEL INTERNATIONAL, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
MARCH 31, 2003 AND 2002
(UNAUDITED)

The computation of diluted loss per share for the three month period ended March 31, 2002 excludes the effect of incremental common shares attributable to the exercise of outstanding common stock options and warrants because their effect was antidilutive due to losses incurred by the Company or such instruments had exercise prices greater than the average market price of the common shares during the periods presented. As of March 31, 2002, there were 308,000 shares of common stock underlying options and warrants that were anti-dilutive and 2,751,000 shares of common stock underlying shares of convertible preferred stock.

(3) INVENTORIES

Inventories consist of the following.

	March 31, 2003	December 31, 2002
Raw materials	$ 2,798,000	$ 2,904,000
Work-in-process	2,904,000	2,988,000
Finished goods	1,690,000	1,613,000
	$ 7,392,000	$ 7,505,000

(4) REPORTABLE SEGMENTS

The Company has two reportable segments: electronic components and communications equipment. The electronic components segment operates in the United States, European and Asian markets and designs, manufactures and markets digital switches and power supplies. The communications equipment segment operates principally in the United States and European markets and designs, manufactures and distributes voice and data transmission and networking equipment and communications test instruments.

The Company evaluates performance based upon profit or loss from operations before income taxes, exclusive of nonrecurring gains and losses. The Company accounts for intersegment sales at prices negotiated between the individual segments.

The Company's reportable segments are comprised of operating entities offering the same or similar products to similar customers. Each segment is managed separately because each business has different customers, design, manufacturing and marketing strategies.

There were no differences in the basis of segmentation or in the basis of measurement of segment profit or loss from the amounts disclosed in the Company's audited consolidated financial statements included in its 2002 annual report on Form 10-K. Selected financial data for each of the Company's operating segments is shown below:

	Three months ended March 31, 2003	Three months ended March 31, 2002
Sales to external customers:		
Electronic Components	$ 3,471,000	$ 2,865,000
Communications Equipment	2,197,000	1,955,000
	$ 5,668,000	$ 4,820,000
Segment pretax profits (losses)		
Electronic Components	$ 674,000	$ 465,000
Communications Equipment	(132,000)	(659,000)
	$ 542,000	$ (194,000)

	March 31, 2003	December 31, 2002
Segment assets		
Electronic Components	$ 9,467,000	$ 9,445,000
Communications Equipment	6,768,000	6,773,000
	$16,235,000	$16,218,000

MICROTEL INTERNATIONAL, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
MARCH 31, 2003 AND 2002
(UNAUDITED)

The following is a reconciliation of the reportable segment income (loss) and assets to the Company's consolidated totals:

	Three months ended March 31, 2003	Three months ended March 31, 2002
Total income (loss) for reportable segments	$ 542,000	$ (194,000)
Unallocated amounts:		
Unallocated general corporate expenses	(430,000)	(466,000)
Consolidated income (loss) before income taxes	$ 112,000	$ (660,000)

	March 31, 2003	December 31, 2002
Assets		
Total assets for reportable segments	$ 16,235,000	$ 16,218,000
Other assets	43,000	568,000
Total consolidated assets	$ 16,278,000	$ 16,786,000

(5) NEW CXR FRANCE CREDIT FACILITY

As of March 31, 2003, CXR France had credit facilities with several lenders totaling up to approximately $716,000 in the aggregate. Each credit facility has a specified repayment term. However, each lender has the right to demand payment in full at any time prior to the scheduled maturity date of a particular credit facility. Because CXR France has experienced a substantial reduction in revenue, some of its lenders are contemplating, and others have made, reductions in the total available credit. Banque Hervet reduced availability to $78,000 from $159,000 effective December 31, 2002. On February 10, 2003, Societe Generale notified CXR France that CXR France had to pay back its credit line balance by April 30, 2003. As of March 31, 2003, that credit line balance was $161,000. As a result, the Company sought alternative financing sources in France to replace all of the current lenders to the Company's French operations. On April 8, 2003, CXR France obtained a credit facility from IFN Finance, a subsidiary of ABN AMRO Holdings, N.V. The new credit line is for a maximum of $1,307,000, based on the exchange rate in effect at March 31, 2003 for the conversion of euros into United States dollars. The facility is secured by accounts receivable and carries an annual interest rate of 1.6 percentage points above the French "T4M" rate, which was 2.758% as of March 31, 2003. Societe Generale has agreed to an alternative pay back schedule for the full balance currently owed so that $54,000 is due by May 31, 2003 and another $54,000 is due by June 30, 2003. Funds that become available under the new IFN Finance credit line as new accounts receivables develop will be used to retire the existing CXR France debt.

(6) NEW ACCOUNTING PRONOUNCEMENTS

New accounting pronouncements are discussed under the heading "Impacts of New Accounting Pronouncements" on page 12 of this report.

(7) INCOME TAXES

The effective tax rate for the three-month period ended March 31, 2003 differed from the federal statutory rate primarily due to certain domestic operating losses having been incurred without a tax benefit having been recorded.

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

The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and notes to financial statements included elsewhere in this document. This report and our condensed consolidated financial statements and notes to financial statements contain forward-looking statements, which generally include the plans and objectives of management for future operations, including plans and objectives relating to our future economic performance and our current beliefs regarding revenues we might earn if we are successful in implementing our business strategies. The forward-looking statements and associated risks may include, relate to or be qualified by other important factors, including, without limitation:

- the projected growth or contraction in the electronic components and communications equipment markets in which we operate;

- our business strategy for expanding, maintaining or contracting our presence in these markets;

- anticipated trends in our financial condition and results of operations; and

- our ability to distinguish ourselves from our current and future competitors.

We do not undertake to update, revise or correct any forward-looking statements.

The information contained in this document is not a complete description of our business or the risks associated with an investment in our common stock. Before deciding to buy or maintain a position in our common stock, you should carefully review and consider the various disclosures we made in this report, and in our other materials filed with the Securities and Exchange Commission that discuss our business in greater detail and that disclose various risks, uncertainties and other factors that may affect our business, results of operations or financial condition. In particular, you should review our annual report on Form 10-K for the year ended December 31, 2002, and the "Risk Factors" we included in that report.

Any of the factors described above could cause our financial results, including our net income (loss) or growth in net income (loss) to differ materially from prior results, which in turn could, among other things, cause the price of our common stock to fluctuate substantially.

OVERVIEW

Through our three wholly-owned operating subsidiaries, XET Corporation, CXR Telcom and CXR France, and through the divisions and subsidiaries of those subsidiaries, we design, develop, manufacture, assemble, and market products and services in the following two material business segments:

- Electronic Components
  - digital and rotary switches
  - electronic power supplies
  - subsystem assemblies

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- Communications Equipment
  - transmission and network access products
  - communications test instruments

Our sales are primarily in North America, Europe and Asia. Revenues are recorded when products are shipped if shipped FOB shipping point or when received by the customer if shipped FOB destination.

Sales to customers in the electronic components segment, primarily to defense and aerospace customers, defense contractors and industrial customers, were 59.1%, 46.1% and 44.1% of our total net sales during 2002, 2001 and 2000, respectively, and 61.2% of our total net sales during the quarter ended March 31, 2003. Sales of communications equipment and related services, primarily to telecommunications equipment customers, were 40.9%, 53.9% and 55.8% of our total net sales during 2002, 2001 and 2000, respectively, and 38.8% of our total net sales during the quarter ended March 31, 2003.

We experienced a 37.2% decline in our communications equipment segment sales during 2002. We believe this decline primarily was due to a general business downturn experienced by many of our telecommunications customers, the disruption caused by the French political elections in 2002 and our decision to discontinue the resale in Europe of test equipment not manufactured by us. As a result of the general business downturn, we experienced significant reductions in sales and gross profit as well as changes in our product mix. Consequently, we have shifted our overall focus toward growing our electronic components business. However, we also plan to continue working to improve the growth and performance of our communications equipment business, particularly customer premises transmission and network access products.

During the first quarter of 2003, our electronic components segment, which primarily serves defense and aerospace markets, improved its sales and profits as compared to the first quarter of 2002. Our communications equipment segment improved its sales and reduced its loss in the first quarter of 2003. The improvement was related to CXR France, which serves mainly our telecommunications premises equipment customer in Europe and the United States. CXR France's 42.0% increase in sales was partially offset by a 51.2% decline in sales at CXR Telcom in Fremont, California, which subsidiary mainly sells to telecommunications carrier companies in the United States. In the first quarter of 2003, we reduced costs at CXR Telcom by laying off a substantial portion of its work force and began to increase our sources of test equipment components from Asian manufacturers that produce the components for lower prices than we previously paid to our former suppliers.

We do not anticipate a further decline in our communications equipment segment sales in 2003 as compared to 2002. We believe that our communications transmission and network access equipment may actually realize a modest improvement in sales in 2003 as compared to 2002. We have reduced costs in our communications equipment segment and lowered the breakeven point both in our U. S. and French operations through various cost-cutting methods, such as using Asian contract manufacturers, reducing facility rent expense and downsizing our administrative office in Paris, France. We anticipate these cost-cutting efforts will improve our bottom line performance in this segment if we are able to achieve at least the same sales levels we achieved in 2002. However, we cannot predict the duration or severity of the telecommunications market downturn or the extent to which the downturn will continue to negatively affect our ability to sell our products and services to customers in the telecommunications

industry. A further reduction in sales would reduce our accounts receivable balances, which in turn would adversely affect our financial position by reducing cash availability under our lines of credit. As mentioned above, we have taken various actions, including staffing reductions as recently as February 2003, to reduce cash outlays of our communications equipment segment. However, if the downturn is long-lasting and more severe, we may need to continue to downsize or to restructure, sell or discontinue all or part of our communications equipment operations, which would negatively impact our business, prospects, financial condition, results of operations and cash flows.

CRITICAL ACCOUNTING POLICIES

Our significant accounting policies are described in the notes to the consolidated financial statements that are included in our annual report on Form 10-K for the year ended December 31, 2002. We believe our most critical accounting policies include inventory valuation, goodwill impairment and foreign currency translation.

INVENTORY VALUATION

We value our inventory at the lower of the actual cost to purchase or manufacture the inventory or the current estimated market value of the inventory. We regularly review inventory quantities on hand and record a provision for excess and obsolete inventory based primarily on our estimated forecast of product demand and production requirements for the next twelve months. Demand for our products can fluctuate significantly. A significant increase in the demand for our products could result in a short-term increase in the cost of inventory purchases, while a significant decrease in demand could result in an increase in the amount of excess inventory quantities on hand.

In addition, the communications equipment industry is characterized by rapid technological change, frequent new product development, and rapid product obsolescence that could result in an increase in the amount of obsolete inventory quantities on hand. Also, our estimates of future product demand may prove to be inaccurate, in which case we may have understated or overstated the provision required for excess and obsolete inventory. In the future, if our inventory is determined to be overvalued, we would be required to recognize such costs in our cost of goods sold at the time of such determination. Likewise, if our inventory is determined to be undervalued, we may have over-reported our costs of goods sold in previous periods and would be required to recognize additional operating income at the time of sale. Therefore, although we make every effort to ensure the accuracy of our forecasts of future product demand, any significant unanticipated changes in demand or technological developments could have a significant impact on the value of our inventory and our reported operating results.

IMPAIRMENT OF GOODWILL

We periodically evaluate acquired businesses for potential impairment indicators. Our judgments regarding the existence of impairment indicators are based on legal factors, market conditions and operational performance of our acquired businesses.

In assessing potential impairment of goodwill, we consider these factors as well as forecasted financial performance of the acquired businesses. If forecasts are not met, we may have to record additional impairment charges not previously recognized. In assessing the recoverability of our goodwill and other intangibles, we must make assumptions regarding estimated future cash flows and other factors to determine the fair value of those respective assets. If these estimates or their related assumptions change in the future, we may be required to record impairment charges for these assets that were not previously recorded. On January 1, 2002, we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," or SFAS No. 142, and were required to analyze our goodwill for impairment issues by June 30, 2002, and then at least annually after that date. During the year ended December 31, 2002 and the three months ended March 31, 2003, we did not record any impairment losses related to goodwill and other intangible assets.

FOREIGN CURRENCY TRANSLATION

We have foreign subsidiaries that together accounted for 62.1% of our net revenues, 72.3% of our assets and 74.7% of our total liabilities as of and for the year ended December 31, 2002, and 76.3% of our net revenues, 75.2% of our assets and 76.5% of our total liabilities as of and for the three months ended March 31, 2003.

In preparing our consolidated financial statements, we are required to translate the financial statements of our foreign subsidiaries from the currencies in which they keep their accounting records into United States dollars. This process results in exchange gains and losses which, under relevant accounting guidance, are either included within our statement of operations or as a separate part of our net equity under the caption "cumulative translation adjustment."

Under relevant accounting guidance, the treatment of these translation gains or losses depends upon our management's determination of the functional currency of each subsidiary. This determination involves consideration of relevant economic facts and circumstances affecting the subsidiary. Generally, the currency in which the subsidiary transacts a majority of its transactions, including billings, financing, payroll and other expenditures, would be considered the functional currency. However, management must also consider any dependency of the subsidiary upon the parent and the nature of the subsidiary's operations.

If management deems any subsidiary's functional currency to be its local currency, then any gain or loss associated with the translation of that subsidiary's financial statements is included in a cumulative translation adjustment. However, if management deems the functional currency to be United States dollars, then any gain or loss associated with the translation of these financial statements would be included within our statement of operations.

If we dispose of any of our subsidiaries, any cumulative translation gains or losses would be realized into our statement of operations. If we determine that there has been a change in the functional currency of a subsidiary to United States dollars, then any translation gains or losses arising after the date of the change would be included within our statement of operations.

Based on our assessment of the factors discussed above, we consider the functional currency of each of our international subsidiaries to be each subsidiary's local currency. Accordingly we had cumulative translation losses of $597,000 and $569,000, respectively, that were included as part of accumulated other comprehensive loss within our balance sheets at December 31, 2002 and March 31, 2003, respectively. During the year ended December 31, 2002 and the three months ended March 31, 2003, we included translation adjustments of gains of approximately $446,000 and $28,000, respectively, under accumulated other comprehensive income and loss.

If we had determined that the functional currency of our subsidiaries was United States dollars, these gains or losses would have decreased or increased our loss for the year ended December 31, 2002 and the three months ended March 31, 2003. The magnitude of these gains or losses depends upon movements in the exchange rates of the foreign currencies in which we transact business as compared to the value of the United States dollar. These currencies include the euro, the British pound and the Japanese yen. Any future translation gains or losses could be significantly higher than those we recorded for the year ended December 31, 2002 and the three months ended March 31, 2003.

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RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2003 COMPARED TO THREE MONTHS ENDED MARCH 31, 2002

The following table sets forth, for the periods indicated, certain statement of operations data expressed as a percentage of total net sales:

	Three months ended March 31, 2003	Three months ended March 31, 2002
Net sales	100.0%	100.0%
Cost of sales	62.2	68.3
Gross profit	37.8	31.7
Selling, general and administrative expenses	30.0	38.7
Engineering and product development expenses	3.9	4.9
Operating income (loss)	3.9	(11.9)
Interest expense	(1.7)	(1.9)
Other income	(0.2)	0.1
Income (loss) before income tax expense	2.0	(13.7)
Income tax expense	1.2	0.8
Net income (loss)	0.8%	(14.5)%

NET SALES. Net sales for the three months ended March 31, 2003 increased by $848,000 (18.2%) to $5,668,000 as compared to $4,820,000 for the three months ended March 31, 2002.

Net sales of our electronic components increased by $606,000 (21.2%) to $3,471,000 for the three months ended March 31, 2003 as compared to $2,865,000 for the three months ended March 31, 2002. Net sales of power supplies by XCEL Corporation, Ltd. increased by $636,000 (43.2%) to $2,109,000 for the three months ended March 31, 2003 as compared to $1,473,000 for the three months ended March 31, 2002 due to an increase in the number of products shipped under long-term programs. We anticipate that during the remainder of 2003 we will experience similar increases in sales of power supplies. Sales of digital switches manufactured by our Digitran Division decreased by $109,000 (8.1%) to $1,234,000 for the three months ended March 31, 2003 as compared to $1,343,000 for the three months ended March 31, 2002. The decline in sales of digital switches was a result of lower than expected orders, which we believe was primarily due to a temporary deferral of government orders that we believe will result in an increase in sales of digital switches in subsequent quarters of 2003. Sales of electronic subsystem assemblies were negligible in the current period and the comparable prior year period.

Net sales of our communications equipment products and services for the three months ended March 31, 2003 increased by $242,000 (12.4%) to $2,197,000 as compared to $1,955,000 for the three months ended March 31, 2002. The increase was the result of a substantial improvement in sales by CXR France of transmission and network access equipment, which improvement exceeded a decline in sales of test equipment by CXR France and CXR Telcom. Transmission and network access equipment sales increased by $637,000 (59.3%) to $1,712,000 for the three months ended March 31, 2003 as compared to $1,075,000 in the prior year period. Test equipment net sales for the three months ended March 31, 2003 decreased by $344,000 (54.2%) to $291,000 as compared to $635,000 for the three months ended March 31, 2002. The sales decrease resulted from a reduction in orders from telecommunication customers in the United States, which we believe was primarily due to the weak telecom market and CXR France's discontinuation of test equipment resales.

CXR France, our French subsidiary, produces all of our transmission products and network access equipment. Net sales of transmission products and network access equipment produced by CXR France increased by $637,000 (59.3%) to $1,712,000 for the three months ended March 31, 2003 as compared to $1,075,000 for the three months ended March 31, 2002 primarily because the prior year sales were negatively affected by the political elections in France, which we believe caused a slow down in purchasing activity in the first half of 2002. Total net sales by CXR France, including both test equipment and transmission and networking equipment, increased by $560,000 (42.0%) to $1,894,000 for the three months ended March 31, 2003 as compared to $1,334,000 for the three months ended March 31, 2002.

Net sales of our CXR HALCYON 704 series field test equipment decreased by $93,000 (39.7%) to $141,000 for the three months ended March 31, 2003 as compared to $234,000 for the three months ended March 31, 2002. Net sales of our T-Com central office test equipment product line declined by $81,000 (51.0%) to $78,000 for the three months ended March 31, 2003 as compared to $159,000 for the three months ended March 31, 2002.

Both the CXR HALCYON and T-COM product lines experienced these decreases in sales due to the continued slowdown in the capital expenditures of telecommunications service providers. The service providers are releasing their capital budgets later in the year and at reduced levels. We are responding to this industry downturn by reducing costs and developing a strategy to seek new business development in other industries that are not suffering from the telecommunications downturn, such as utilities, construction and government.

We believe that many of the United States telecom customers that CXR Telcom serves built networks to handle an anticipated demand for voice and data traffic that has not yet occurred. Consequently, many of these customers reduced their purchasing budgets for 2002 and 2003. This has had a negative impact on CXR Telcom's sales. We have seen recent improvement in orders at CXR Telcom but do not know if such improvement will be a continuing trend or only a temporary change.

GROSS PROFIT. Gross profit as a percentage of total net sales increased to 37.8% for the three months ended March 31, 2003 as compared to 31.7% for the comparable period in 2002. In dollar terms, total gross profit increased by $612,000 (40.0%) to $2,141,000 for the three months ended March 31, 2003 as compared to $1,529,000 for the comparable period in 2002.

Gross profit for our electronic components segment increased in dollar terms by $332,000 (32.0%) to $1,370,000 for the three months ended March 31, 2003 as compared to $1,038,000 for the three months ended March 31, 2002, and increased as a percentage of related net sales to 39.5% for the three months ended March 31, 2003 from 36.2% for the three months ended March 31, 2002. This increase primarily was the result of increases in the profit margins of both digital switches and power supplies due to changes in product mix for XET Corporation's Digitran Division switch production operations and increased production due to higher sales volumes lowering per unit costs for XCEL Power Systems' U.K. power supply production operations.

Gross profit for our communications equipment segment increased in dollar terms by $280,000 (57.0%) to $771,000 for the three months ended March 31, 2003 as compared to $491,000 for the comparable period in 2002, and increased as a percentage of net sales to 35.1% for the three months ended March 31, 2003 from 25.1% for the three months ended March 31, 2002. The increase in

gross profit as a percentage of net sales primarily was due to the increase in sales volume at CXR France and cost reduction, which helped reduce costs on a per unit basis. Cost reductions at CXR Telcom were not sufficient to offset the effect of CXR Telcom's decline in sales, and CXR Telcom ended the first quarter of 2003 with a negative gross profit. Based on recent orders, we expect CXR Telcom to improve its gross profit in subsequent quarters of 2003.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses decreased by $167,000 (9.0%) to $1,698,000 for the three months ended March 31, 2003 as compared to $1,865,000 for the three months ended March 31, 2002. Selling, general and administrative expenses also decreased as a percentage of total net sales, to 30.0% of net sales during the three months ended March 31, 2003 from 38.7% of net sales during the comparable period in 2002. The decrease in selling, general and administrative expenses was due to several factors. Selling expenses were reduced by $96,000 in our communications equipment segment, and administrative costs were reduced by $135,000 in our communications equipment segment primarily due to staff reductions at CXR Telcom and CXR France. These reductions were partially offset by an $83,000 increase in administrative expenses in our electronic components segment which was partially due to an increase in the reserve for doubtful accounts and miscellaneous other items.

ENGINEERING AND PRODUCT DEVELOPMENT EXPENSES. Engineering and product development expenses consist primarily of research and product development activities of our communications equipment segment. These expenses decreased slightly to $221,000 for the three months ended March 31, 2003 as compared to $238,000 for the three months ended March 31, 2002.

OTHER INCOME AND EXPENSE. Interest expense increased by $6,000 (6.7%) to $96,000 for the three months ended March 31, 2003 from $90,000 for the three months ended March 31, 2002. Other expense was $14,000 for the three months ended March 31, 2003 as compared to $4,000 for the three months ended March 31, 2002 primarily due to currency exchange rate fluctuations.

INCOME TAX EXPENSE. Income tax expense for the three months ended March 31, 2002 was $68,000 as compared to $39,000 for the comparable prior year period. The majority of the increase related to the recording by XCL of a provision for U.K. income tax that was required because XCL is expected to produce greater taxable income for 2003 than in 2002 and has consumed its net operating loss carryforwards.

NET INCOME (LOSS). The net income for the three months ended March 31, 2003 was $44,000 as compared to the net loss of $699,000 for the three months ended March 31, 2002 . The largest contribution to this positive change was the increase in net sales of CXR France in our communications equipment segment, which improved its operating income by $442,000. We continue to closely monitor costs throughout our operations and have reduced costs through staffing reductions in our communications equipment operations in the United States and France and through various other cost-cutting methods, such as using contract manufacturers, reducing facility rent expense and phasing out our administrative office in Paris, France. These actions have substantially reduced the sales volume required to turn a profit at both CXR Telcom and CXR France.

LIQUIDITY AND CAPITAL RESOURCES

During the three months ended March 31, 2003 and the year ended December 31, 2002, we funded our operations primarily through revenue generated from our operations and through our lines of credit with Wells Fargo Business Credit, Inc. and various foreign banks. As of March 31, 2003, we had working capital of $4,085,000, an accumulated deficit of $19,000,000, an accumulated other comprehensive loss of $569,000, cash and cash equivalents of $29,000, and $5,179,000 of accounts receivable. As of December 31, 2002, we had working capital of $3,961,000, an accumulated deficit of $19,042,000, an accumulated other comprehensive loss of $597,000, cash and cash equivalents of $254,000, and $5,356,000 of accounts receivable.

Cash provided by our operating activities totaled $468,000 for the three months ended March 31, 2003 as compared to cash provided by our operating activities of $279,000 for the three months ended March 31, 2002. This $189,000 increase in cash provided by operations during the three months ended March 31, 2003 primarily resulted from accounts receivable collections and increases in accounts payable balances.

Cash used in our investing activities totaled $4,000 for the three months ended March 31, 2003 as compared to $21,000 for the three months ended March 31, 2002. Included in the results for the three months ended March 31, 2002 are $35,000 of fixed asset purchases.

Cash used in our financing activities totaled $814,000 for the three months ended March 31, 2003 as compared to $432,000 for the three months ended March 31, 2002, primarily due to repayments of bank debt.

On August 16, 2000, our subsidiaries, CXR Telcom and XET Corporation, together with MicroTel acting as guarantor, obtained a credit facility from Wells Fargo Business Credit, Inc. In April 2002, the maturity date of the facility was extended by two years to August 16, 2005. Since April 17, 2002, the facility has provided for a revolving loan of up to $3,000,000 secured by inventory and accounts receivable and a term loan in the amount of $687,000 secured by machinery and equipment. On March 31, 2003, the interest rate was the prime rate (then 4.25%) plus 1%, subject to a minimum interest charge of $13,500 per month. The balance outstanding at March 31, 2003 was $697,000 on the revolving loan and $86,000 on the term loan, and we had available to us $148,000 of additional borrowings under the revolving loan. The credit facility contains restrictive financial covenants that are set by mutual agreement each year. At March 31, 2003, no covenants had been established for 2003.

As of March 31, 2003, our foreign subsidiaries had credit facilities, including lines of credit and term loans, with Venture Finance PLC, a subsidiary of the global Dutch ABN AMRO Holdings N.V. financial institution, in England, Banc National de Paris, Societe Generale and Banque Hervet in France and Johan Tokyo Credit Bank and Johnan Shinkin Bank in Japan. At March 31, 2003, the balances outstanding under our U.K., France and Japan credit facilities were $2,105,000, $716,000 and $78,000, respectively.

XCEL Japan Ltd. , or XJL, obtained a term loan on November 29, 2002 from the Johnan Shinkin Bank. The loan is amortized over five years and carries an annual interest rate 3.25%. The balance of the loan on March 31, 2003 was $78,000 using the exchange rate in effect at that date for conversion of Japanese yen into United States dollars.

Our U.K. subsidiary, XCEL Power Systems, Ltd., or XPS, obtained a credit facility with Venture Finance PLC as of November 12, 2002, which facility expires on November 15, 2005. Using the exchange rate in effect at March 31, 2003 for the conversion of British pounds into United States dollars, the new facility is for a maximum of $2,370,000 and includes a $553,000 unsecured cash flow loan, a $126,000 term loan secured by fixed assets and the remainder is a loan secured by accounts receivable and inventory. The interest rate is the base rate of Venture Finance PLC (4% at March 31, 2003) plus 2%, and is subject to a minimum rate of 4% per annum. There are no financial performance covenants applicable to this credit facility.

As of March 31, 2003, CXR France had credit facilities with several lenders totaling up to approximately $716,000 in the aggregate. Each credit facility has a specified repayment term. However, each lender has the right to demand payment in full at any time prior to the scheduled maturity date of a particular credit facility. Because CXR France has experienced a substantial reduction in revenue, some of its lenders are contemplating, and others have made, reductions in the total available credit. Banque Hervet reduced availability to $78,000 from $159,000 effective December 31, 2002. On February 10, 2003, Societe Generale notified CXR France that CXR France had to pay back its credit line balance by April 30, 2003. As of March 31, 2003, that credit line balance was $161,000. As a result, we sought alternative financing sources in France to replace all of the current lenders to our French operations. On April 8, 2003, CXR France obtained a credit facility from IFN Finance, a subsidiary of ABN AMRO Holdings, N.V. The new credit line is for a maximum of $1,307,000, based on the exchange rate in effect at March 31, 2003 for the conversion of euros into United States dollars. The facility is secured by accounts receivable and carries an annual interest rate of 1.6 percentage points above the French "T4M" rate, which was 2.758% as of March 31, 2003. Societe Generale has agreed to an alternative pay back schedule for the full balance currently owed so that $54,000 is due by May 31, 2003 and another $54,000 is due by June 30, 2003. Funds that become available under the new IFN Finance credit line as new accounts receivables develop will be used to retire the existing CXR France debt.

Our backlog was $11,815,000 as of March 31, 2003 as compared to $14,800,000 as of March 31, 2002. Our backlog as of March 31, 2003 was 95.9% related to our electronic components business, which business tends to provide us with long lead-times for our manufacturing processes due to the custom nature of the products, and 4.1% related to our communications equipment business, which business tends to deliver standard products from stock as orders are received. The amount of backlog orders represents revenue that we anticipate recognizing in the future, as evidenced by purchase orders and other purchase commitments received from customers, but on which work has not yet been initiated or with respect to which work is currently in progress. However, there can be no assurance that we will be successful in fulfilling such orders and commitments in a timely manner or that we will ultimately recognize as revenue the amounts reflected as backlog.

During the three months ended March 31, 2003 and the year ended December 31, 2002, 38.8% and 40.9% of our total net sales, respectively, were generated by our communications equipment segment. We experienced a 12.4% increase in our communications equipment segment sales for the three months ended March 31, 2003 as compared to the three months ended March 31, 2002. This increase was net of a 54.2% decline in sales of test equipment. The test equipment decline was due to our discontinuation of test equipment resales in Europe and the general telecommunications downtown in the United States. We cannot predict the duration or severity of the telecommunications market downturn or the extent to which the downturn will continue to negatively affect our ability to sell our products and services to customers in the telecommunications industry. A further reduction in sales could reduce our total accounts receivable balances, which in turn would have an adverse effect on our financial position by reducing the amount of cash available under our lines of credit.

We took various actions to reduce costs in 2002. These actions were intended to reduce the cash outlays of our telecommunications equipment segment to match its revenue rate. Also, in February 2003, we reduced the staffing level by 50% at CXR Telcom, which we anticipate will reduce costs at an annualized rate of approximately $360,000. This savings is in addition to the approximate $325,000 annualized savings we have begun to realize from moving CXR Telcom into a lower cost facility in November 2002. We also have contracted with Asian manufacturers for production of test equipment components at lower prices than we previously paid to our former suppliers.

The following table outlines payments due from us or our subsidiaries under our lines of credit and other significant contractual obligations over the next five years, exclusive of interest. The symbol "P" represents the prime rate, and the symbol "B" represents the lender's base rate.

CONTRACTUAL OBLIGATIONS AT MARCH 31, 2003	PAYMENTS DUE BY PERIOD (IN THOUSANDS)					
	2003	2004	2005	2006	2007	THERE-
Line of Credit (Domestic)	$ 697	$ --	$ --	$ --	$ --	$ --
Average Interest Rate	P+1%					
Line of Credit (U.K.)	$1,437	$ --	$ --	$ --	$ --	$ --
Average Interest Rate	B+2%					
Overdraft (France)	$ 599	$ --	$ --	$ --	$ --	$ --
Average Interest Rate	5.5% -7.2%					
Term Loan (Domestic)	$ 72	$ 8	$ 5	$ --	$ --	$ --
Average Interest Rate	P+1%					
Term Loan (U.K.)	$ 21	$ 45	$ 602	$ --	$ --	$ --
Average Interest Rate	B+2%					
Term Loan (France)	$ 50	$ 56	$ 10	$ --	$ --	$ --
Average Interest Rate	5.2% -5.6%					
Term Loan (Japan)	$ 13	$ 17	$ 17	$ 16	$ 15	$ --
Average Interest Rate	3.25%					
Capitalized Lease Obligations	$ 90	$ 98	$ 35	$ 3	$ --	$ --
Operating Leases	$ 475	$ 562	$ 382	$ 6	$ --	$ --
	$3,454	$ 786	1,051	25	$ 15	$ --

In conjunction with our cost reductions, we believe that current and future available capital resources, revenues generated from operations, and other existing sources of liquidity, including the credit facilities we and our subsidiaries have, will be adequate to meet our anticipated working capital and capital expenditure requirements for at least the next twelve months. If, however, our capital requirements or cash flow vary materially from our current projections or if unforeseen circumstances occur, we may require additional financing. Deteriorating global economic conditions may cause prolonged declines in investor confidence in and accessibility to capital markets. Our failure to raise capital, if needed, could restrict our growth, limit our development of new products or hinder our ability to compete.

EFFECTS OF INFLATION

The impact of inflation and changing prices has not been significant on the financial condition or results of operations of either our company or our operating subsidiaries.

IMPACTS OF NEW ACCOUNTING PRONOUNCEMENTS

In August 2001, the Financial Accounting Standards Board, or the FASB, issued FASB Statement No. 143, "Accounting for Asset Retirement Obligations," or SFAS No. 143. This statement addresses financial and reporting obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. It applies to all entities and legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or normal operation of long-lived assets, except for certain obligations of lessees. This statement is effective for financial statements issued for fiscal years beginning after June 15, 2002. Our management has determined that the adoption of SFAS No. 143 has not had a material effect on our financial position or results of operations.

In October 2001, the FASB issued FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," or SFAS No. 144. SFAS No. 144 requires that long-lived assets be measured at the lower of carrying amount or fair value less cost to sell, whether reported in continuing operations or in discontinued operations. Therefore, discontinued operations will no longer be measured at net realizable value or include amounts for operating losses that have not yet occurred. SFAS No. 144 is effective for our consolidated financial statements beginning January 1, 2002. The implementation of SFAS No. 144 did not have a material impact on our consolidated financial position or results of operations.

In April 2002, the FASB issued FASB Statement No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections," or SFAS No. 145. This statement rescinds SFAS No. 4, "Reporting Gains and Losses from Extinguishment of Debt" and amends SFAS No. 64, "Extinguishments of Debt Made to Satisfy Sinking Fund Requirements." Under SFAS No. 4, all gains and losses from extinguishment of debt were required to be aggregated and, if material, classified as an extraordinary item, net of the related income tax effect. With the elimination of SFAS No. 4, gains and losses from extinguishment of debt are to be classified as extraordinary items only if they meet the criteria for extraordinary items in APB Opinion No. 30, "Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions." Applying the provisions of APB Opinion No. 30 will distinguish transactions that are part of an entity's recurring operations from those that are unusual or infrequent or that meet the classification of an extraordinary item. SFAS No. 145 also rescinds SFAS No. 44, "Accounting for Intangible Assets of Motor Carriers," and amends SFAS No. 13, "Accounting for Leases," to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. SFAS No. 145 also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings or describe their applicability under changed conditions. The adoption of the provisions of SFAS No. 145 during 2002 did not have any impact on our financial position or results of operations.

In June 2002, the FASB issued FASB Statement No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," or SFAS No. 146. SFAS No. 146 addresses accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)." SFAS No. 146 requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value when the liability is incurred. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002, with early application encouraged. We do not expect the adoption of this statement to have a material effect on our financial statements.

In November 2002, the FASB issued FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others," or FIN 45. FIN 45 requires a guarantor to recognize a liability, at the inception of the guarantee, for the fair value of obligations it has undertaken in issuing the guarantee and also include more detailed disclosures with respect to guarantees. FIN 45 is effective for guarantees issued or modified after December 31, 2002 and requires the additional disclosures for interim or annual periods ended after December 15, 2002. The initial recognition and measurement provisions of FIN 45 have not had an impact on our results of operations or financial position.

In December 2002, the FASB issued FASB Statement No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure-An Amendment of SFAS 123," or SFAS No. 148. SFAS No. 148 amends SFAS No. 123 to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. We have chosen to continue to account for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Bulletin Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. Accordingly, compensation expense for stock options is measured as the excess, if any, of the estimate of the market value of our stock at the date of the grant over the amount an employee must pay to acquire the stock. We have adopted the annual disclosure provisions of SFAS No. 148 for our financial reports for the year ended December 31, 2002 and have also adopted the interim disclosure provisions for our financial reports beginning with the quarter ended March 31, 2003. Because this standard involves disclosures only, the adoption of SFAS No. 148 did not impact our results of operations, financial position or liquidity.

In January 2003, the FASB issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities - An Interpretation of ARB No. 51," or FIN 46. FIN 46 requires that if an entity has a controlling financial interest in a variable interest entity, the assets, liabilities and results of activities of the variable interest entity should be included in the consolidated financial statements of the entity. FIN 46 requires that its provisions are effective immediately for all arrangements entered into after January 31, 2003. For arrangements entered into prior to January 31, 2003, the FIN 46 provisions are required to be adopted at the beginning of the first interim or annual period beginning after June 15, 2003. We do not expect that the provisions of FIN 46 will have a material impact on our results of operations or financial position.

EURO CONVERSION

Our operating subsidiaries located in France and the U.K. had combined net sales from operations approximating 72.2% and 58.7%, respectively, of our total net sales for the three months ended March 31, 2003 and the year ended December 31, 2002. Net sales from the French subsidiary participating in the euro conversion were approximately 33.4% and 25.8%, respectively, of our net sales for the three months ended March 31, 2003 and the year ended December 31, 2002. We continue to review the impact of the euro conversion on our operations.

Our European operations took steps to ensure their capability of entering into euro transactions. No material changes to information technology and other systems are necessary to accommodate these multiple currency transactions because such systems already were capable of using multiple currencies.

While it is difficult to assess the competitive impact of the euro conversion on our European operations, at this time we do not foresee any material impediments to our ability to compete for orders from customers requesting pricing using the new exchange rate. Since we have no significant direct sales between our United States and European operations, we regard exchange rate risk as nominal.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

We have established and acquired international subsidiaries that prepare their balance sheets in the relevant foreign currency. In order to be included in our consolidated financial statements, these balance sheets are converted, at the then current exchange rate, into United States dollars, and the statements of operations are converted using weighted average exchange rates for the applicable period. Accordingly, fluctuations of the foreign currencies relative to the United States dollar could have an effect on our consolidated financial statements. Our exposure to fluctuations in currency exchange rates has increased as a result of the growth of our international subsidiaries. However, because historically the majority of our currency exposure has related to financial statement translation rather than to particular transactions, we do not intend to enter into, nor have we historically entered into, forward currency contracts or hedging arrangements in an effort to mitigate our currency exposure.

A substantial portion of our notes payable and long-term debt have variable interest rates based on the prime interest rate and/or the lender's base rate, which exposes us to risk of earnings loss due to changes in such interest rates. Our annual report on Form 10-K for the year ended December 31, 2002 contains information about our debt obligations that are sensitive to changes in interest rates under "Item 7A. Quantitative and Qualitative Disclosures About Market Risk." There were no material changes in those market risks during the three months ended March 31, 2003.

ITEM 4. CONTROLS AND PROCEDURES.

Our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively) have concluded, based on their evaluation as of May 5, 2003 ("Evaluation Date"), that the design and operation of our "disclosure controls and procedures" (as defined in Rules 13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934, as amended ("Exchange Act")) are effective to ensure that information required to be disclosed by us in the reports filed or submitted by us under the Exchange Act is accumulated, recorded, processed, summarized and reported to our management, including our principal executive officer and our principal financial officer, as appropriate to allow timely decisions regarding whether or not disclosure is required.

There were no significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the Evaluation Date, nor were there any significant deficiencies or material weaknesses in our internal controls. As a result, no corrective actions were required or undertaken.

PART II
OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

We are not a party to any material pending legal proceedings.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS.

RECENT SALES OF UNREGISTERED SECURITIES

In March 2003, we issued 41,663 shares of common stock to one investor upon conversion of 4,166.3 shares of our Series B Preferred Stock.

Exemption from the registration provisions of the Securities Act of 1933 for the transaction described above is claimed under Section 4(2) of the Securities Act of 1933, among others, on the basis that such transaction did not involve any public offering and the purchaser was sophisticated with access to the kind of information registration would provide.

DIVIDENDS

To date we have not paid dividends on our common stock. Our line of credit with Wells Fargo Business Credit, Inc. prohibits the payment of cash dividends on our common stock. The certificates of designations related to our Series A Preferred Stock and Series B Preferred Stock provide that shares of those series of preferred stock are not entitled to receive cash dividends. We currently intend to retain future earnings to fund the development and growth of our business and, therefore, do not anticipate paying cash dividends on our common stock within the foreseeable future. Any future payment of dividends on our common stock will be determined by our board of directors and will depend on our financial condition, results of operations, contractual obligations and other factors deemed relevant by our board of directors.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

ITEM 5. OTHER INFORMATION.

None.

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

(a) Exhibits

Number	Description
10.1	Waiver of Default Agreement dated March 28, 2003 between XET Corporation, CXR Telcom Corporation and Wells Fargo Business Credit, Inc. (1)
99.1	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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(1) Filed as an exhibit to our annual report on Form 10-K for the year ended December 31, 2002 and incorporated herein by reference.

(b) Reports on Form 8-K

None.

SIGNATURES

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

MICROTEL INTERNATIONAL, INC.

Dated: May 14, 2003

By: /S/ CARMINE T. OLIVA

Carmine T. Oliva, Chairman of the Board, Chief Executive Officer (principal executive officer) and President

By: /S/ RANDOLPH D. FOOTE

Randolph D. Foote, Chief Financial Officer (principal financial and accounting officer)

CERTIFICATIONS

I, Carmine T. Oliva, certify that:

1. I have reviewed this quarterly report on Form 10-Q of MicroTel International, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 14, 2003

/s/ CARMINE T. OLIVA

Carmine T. Oliva,
Chief Executive Officer (principal executive officer)

I, Randolph D. Foote, certify that:

1. I have reviewed this quarterly report on Form 10-Q of MicroTel International, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 14, 2003

/s/ RANDOLPH D. FOOTE

Randolph D. Foote,
Chief Financial Officer (principal financial officer)

EXHIBITS FILED WITH THIS REPORT ON FORM 10-Q

Number	Description
99.1	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act Of 2002