

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **2003-02-10** | Period of Report: **2002-12-31**  
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FILER

**SMTEK INTERNATIONAL INC**

CIK: **26987** | IRS No.: **330213512** | State of Incorporation: **DE** | Fiscal Year End: **0702**  
Type: **10-Q** | Act: **34** | File No.: **001-08101** | Film No.: **03546507**  
SIC: **3672** Printed circuit boards

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10 - Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the quarterly period ended: DECEMBER 31, 2002

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number: 1-8101

Exact Name of Registrant as  
Specified in Its Charter: SMTEK INTERNATIONAL, INC.

DELAWARE 33-0213512  
State or Other Jurisdiction of I.R.S. Employer  
Incorporation or Organization: Identification No.

Address of Principal Executive Offices: 200 Science Drive  
Moorpark, CA 93021

Registrant's Telephone Number: (805) 532-2800

Indicate by check mark whether the registrant: (1) has filed all reports  
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of  
1934 during the preceding 12 months (or for such shorter period that the  
registrant was required to file such reports), and (2) has been subject to  
such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as  
defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes  No

The registrant had 2,284,343 shares of common stock outstanding as of

February 7, 2003.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SMTEK INTERNATIONAL, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)  
(In thousands except share amounts)

<TABLE>

<CAPTION>

|   | December 31,<br>2002 | June 30,<br>2002 |
|---|----------------------|------------------|
|   | -----                | -----            |
| ASSETS  |                      |                  |
| <S>   | <C>                  | <C>              |
| Current assets:   |                      |                  |
| Cash and cash equivalents   | \$ 628               | \$ 816           |
| Accounts receivable, less allowance for doubtful<br>accounts of \$175 and \$380, as of December 31,<br>2002 and June 30, 2002, respectively | 12,155               | 12,351           |
| Inventories, net  | 10,082               | 11,223           |
| Prepaid expenses  | 1,061                | 863              |
|   | -----                | -----            |
| Total current assets  | 23,926               | 25,253           |
|   | -----                | -----            |
| Property, equipment and improvements, net of<br>accumulated depreciation and amortization   | 8,115                | 8,809            |
| Other assets  | 330                  | 772              |
|   | -----                | -----            |
|   | \$ 32,371            | \$ 34,834        |
|   | =====                | =====            |
| LIABILITIES AND STOCKHOLDERS' EQUITY  |                      |                  |
| Current liabilities:  |                      |                  |
| Current portion of bank lines of credit payable   | \$ 8,131             | \$ 3,223         |
| Current portion of long-term debt   | 3,235                | 2,527            |
| Accounts payable  | 8,343                | 8,652            |
| Other accrued liabilities   | 7,099                | 4,936            |
|   | -----                | -----            |
| Total current liabilities   | 26,808               | 19,338           |
|   | -----                | -----            |
| Long-term liabilities:  |                      |                  |
| Long-term bank lines of credit payable  | -                    | 4,005            |
| Long-term debt  | 4,618                | 6,066            |
| Other long-term liabilities   | 710                  | -                |
|   | -----                | -----            |
| Total long-term liabilities   | 5,328                | 10,071           |
|   | -----                | -----            |
| Commitments and contingencies   |                      |                  |
| Stockholders' equity:   |                      |                  |
| Preferred stock, \$1 par value; 1,000,000 shares<br>authorized; no shares issued or outstanding   | -                    | -                |

|   |           |           |
|---|-----------|-----------|
| Common stock, \$.01 par value; 3,750,000 shares<br>authorized; 2,284,343 issued and outstanding at<br>December 31, 2002 and June 30, 2002 | 23        | 23        |
| Additional paid-in capital  | 37,028    | 37,028    |
| Accumulated deficit   | (36,697)  | (31,616)  |
| Accumulated other comprehensive loss  | (119)     | (10)      |
|   | -----     | -----     |
| Total stockholders' equity  | 235       | 5,425     |
|   | -----     | -----     |
|   | \$ 32,371 | \$ 34,834 |
|   | =====     | =====     |

</TABLE>

See accompanying notes to unaudited condensed consolidated financial statements.

SMTEK INTERNATIONAL, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
AND OTHER COMPREHENSIVE INCOME (LOSS) (Unaudited)  
(In thousands except per share amounts)

<TABLE>  
<CAPTION>

|   | Three Months Ended<br>December 31, |          | Six Months Ended<br>December 31, |          |
|---|------------------------------------|----------|----------------------------------|----------|
|   | 2002                               | 2001     | 2002                             | 2001     |
|   | -----                              | -----    | -----                            | -----    |
| <S>   | <C>                                | <C>      | <C>                              | <C>      |
| Revenues  | \$17,299                           | \$19,594 | \$38,035                         | \$39,228 |
| Cost of goods sold                              | 16,501                             | 17,632   | 35,540                           | 35,262   |
|   | -----                              | -----    | -----                            | -----    |
| Gross profit                                    | 798                                | 1,962    | 2,495                            | 3,966    |
|   | -----                              | -----    | -----                            | -----    |
| Operating expenses:                             |                                    |          |                                  |          |
| Administrative and selling                      | 4,357                              | 2,438    | 6,526                            | 4,146    |
| Goodwill amortization                           | -                                  | 9        | -                                | 19       |
|   | -----                              | -----    | -----                            | -----    |
| Total operating expenses                        | 4,357                              | 2,447    | 6,526                            | 4,165    |
|   | -----                              | -----    | -----                            | -----    |
| Operating loss                                  | (3,559)                            | (485)    | (4,031)                          | (199)    |
|   | -----                              | -----    | -----                            | -----    |
| Non-operating income (expense):                 |                                    |          |                                  |          |
| Interest expense, net                           | (330)                              | (291)    | (654)                            | (563)    |
| Other income, net                               | 12                                 | 26       | 30                               | 54       |
|   | -----                              | -----    | -----                            | -----    |
| Total non-operating expense, net                | (318)                              | (265)    | (624)                            | (509)    |
|   | -----                              | -----    | -----                            | -----    |
| Loss from operations before income taxes        | (3,877)                            | (750)    | (4,655)                          | (708)    |
| Income tax provision                            | 1                                  | 12       | 6                                | 27       |
|   | -----                              | -----    | -----                            | -----    |
| Loss from operations                            | (3,878)                            | (762)    | (4,661)                          | (735)    |
|   | -----                              | -----    | -----                            | -----    |
| Change in accounting principle,<br>net of taxes | -                                  | -        | (420)                            | -        |
|   | -----                              | -----    | -----                            | -----    |

|   |            |           |            |           |
|---|------------|-----------|------------|-----------|
| Net loss  | \$ (3,878) | \$ (762)  | \$ (5,081) | \$ (735)  |
|   | =====      | =====     | =====      | =====     |
| Other comprehensive income (loss):                        |            |           |            |           |
| Foreign currency translation adjustments                  | (2)        | 2         | (72)       | 44        |
| Change in unrealized gain/(loss) on forward contracts     | (20)       | -         | (37)       | -         |
|   | -----      | -----     | -----      | -----     |
| Comprehensive loss  | \$ (3,900) | \$ (760)  | \$ (5,190) | \$ (691)  |
|   | =====      | =====     | =====      | =====     |
| Basic and diluted loss per share:                         |            |           |            |           |
| Loss from operations                                      | \$ (1.70)  | \$ (0.33) | \$ (2.04)  | \$ (0.32) |
| Change in accounting principle                            | -          | -         | (0.18)     | -         |
|   | =====      | =====     | =====      | =====     |
| Basic and diluted loss per share                          | \$ (1.70)  | \$ (0.33) | \$ (2.22)  | \$ (0.32) |
|   | =====      | =====     | =====      | =====     |
| Shares used in computing basic and diluted loss per share | 2,284      | 2,284     | 2,284      | 2,284     |
|   | =====      | =====     | =====      | =====     |

</TABLE>

See accompanying notes to unaudited condensed consolidated financial statements.

SMTEK INTERNATIONAL, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
(In thousands)

|   | Six Months Ended<br>December 31, |          |
|---|----------------------------------|----------|
|   | 2002                             | 2001     |
|   | -----                            | -----    |
| Cash flows from operating activities:   |                                  |          |
| Net loss  | \$ (5,081)                       | \$ (735) |
| Adjustments to reconcile net loss to net cash provided by operating activities:         |                                  |          |
| Depreciation and amortization   | 1,301                            | 1,215    |
| Loss on sale of assets  | 6                                | -        |
| Facility consolidation costs  | 1,815                            | -        |
| (Increase) decrease in accounts receivable  | 440                              | (469)    |
| Decrease in costs and estimated earnings in excess of billings on uncompleted contracts | -                                | 3,692    |
| (Increase) decrease in inventories  | 1,195                            | (1,045)  |
| Increase (decrease) in accounts payable   | (381)                            | 515      |
| Increase (decrease) in other accrued liabilities  | 1,834                            | (510)    |
| Other, net  | (314)                            | (518)    |
|   | -----                            | -----    |
| Net cash provided by operating activities   | 815                              | 2,145    |
|   | -----                            | -----    |

|   |        |          |
|---|--------|----------|
| Cash flows from investing activities:               |        |          |
| Capital expenditures                                | (907)  | (2,717)  |
| Purchase of Century Thailand, net of cash received  | -      | (129)    |
|   | -----  | -----    |
| Net cash used in investing activities               | (907)  | (2,846)  |
|   | -----  | -----    |
| Cash flows from financing activities:               |        |          |
| Proceeds from (payments of) bank lines of credit    | 749    | (60)     |
| Proceeds from long-term debt                        | -      | 2,452    |
| Payments of long-term debt                          | (810)  | (798)    |
| Proceeds from the exercise of stock options         | -      | 7        |
|   | -----  | -----    |
| Net cash provided by (used in) financing activities | (61)   | 1,601    |
|   | -----  | -----    |
| Effect of exchange rate changes on cash             | (35)   | 5        |
|   | -----  | -----    |
| Increase (decrease) in cash and cash equivalents    | (188)  | 905      |
| Cash and cash equivalents at beginning of period    | 816    | 224      |
|   | -----  | -----    |
| Cash and cash equivalents at end of period          | \$ 628 | \$ 1,129 |
|   | =====  | =====    |
| Supplemental cash flow information:                 |        |          |
| Interest paid                                       | \$ 501 | \$ 426   |
| Income taxes paid                                   | -      | 40       |
| Non-cash investing activities:                      |        |          |
| Other obligations                                   | -      | 2        |

See accompanying notes to unaudited condensed consolidated financial statements

SMTEK INTERNATIONAL, INC. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
Six Months Ended December 31, 2002 and 2001

NOTE 1 - DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

SMTEK International, Inc. (the "Company," "we," "us" or "our") is an electronics manufacturing services ("EMS") provider to original equipment manufacturers ("OEMs") primarily in the industrial and instrumentation, medical, telecommunications, security, financial services automation and aerospace and defense industries. We provide integrated solutions to OEMs across the entire product life cycle, from design to manufacturing to end-of-life services, for the worldwide low-to-medium volume, high complexity segment of the EMS industry.

We have seven wholly owned subsidiaries: SMTEK, Inc. (dba SMTEK Moorpark), located in Moorpark, California; Technetics, Inc. (dba SMTEK San Diego), located in Poway, California (see discussion in the next paragraph);

Jolt Technology, Inc. (aka SMTEK Fort Lauderdale), located in Fort Lauderdale, Florida; SMTEK Europe Limited, located in Craigavon, Northern Ireland; SMTEK New England, located in Marlborough, Massachusetts; SMTEK Santa Clara, located in Santa Clara, California; and SMTEK International Thailand Limited, located in Ayutthya, Thailand.

On November 19, 2002, we announced that we are consolidating our Poway facility into our other California operations in Moorpark and Santa Clara. This transition is expected to be completed by the quarter ending March 2003.

We have experienced and may continue to experience an adverse effect on our operating results and in our financial condition, especially if current economic conditions continue for an extended period of time, despite our cost reduction measures and efficiency improvements at our operating facilities. We are focused on the consolidation and streamlining of operations so as to reduce our excess capacity to better match market conditions. Recent actions taken and strategies being pursued are as follows:

- Transitioning the San Diego facility and evaluating further opportunities of consolidation, transition or sale of other facilities.
- Continuing focus on cost reductions related to pertinent production levels and reductions in administrative costs.
- Focusing our marketing efforts in the solicitation of customers in noneconomically affected industries.

We remain dependent on our lines of credit for operations and growth. Our domestic line of credit agreement is set to mature in September 2003. We can provide no assurance that the agreement will be renewed or that any renewal would occur on commercially reasonable terms. We may have to explore alternative financing if the bank does not renew our line of credit.

We may require additional financing to satisfy our debt obligations. However, there can be no assurance that we will be able to obtain additional debt or equity financing when needed, or on acceptable terms. Any additional debt or equity financing may involve substantial dilution to our stockholders, restrictive covenants or high interest costs. The failure to raise needed funds on sufficiently favorable terms could have a material adverse effect on our business, operating results, and financial condition.

Although management believes our cash resources, cash from operations and available borrowing capacity on our working capital lines of credit are sufficient to fund operations, if we cannot refinance the domestic line of credit upon its maturity or find alternative financing/funding of this obligation, there is no assurance that we will continue as a going concern.

All significant intercompany transactions and accounts have been eliminated in consolidation. In the opinion of the Company's management, the accompanying condensed consolidated financial statements reflect all adjustments (consisting of normal recurring accruals) necessary to present fairly our financial position, results of operations and cash flows as of and for the periods presented.

We utilize a 52-53 week fiscal year ending on the Friday closest to June 30, which for fiscal year 2002 fell on June 28, 2002. In the accompanying condensed consolidated financial statements, the 2002 fiscal year end is shown as June 30 and the interim period end for both years is shown as December 31 for clarity of presentation. The actual interim periods ended on December 27, 2002 and December 28, 2001.

Certain notes and other information are condensed or omitted from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these condensed financial statements should be read in conjunction with our 2002 Annual Report on Form 10-K as filed with the Securities and Exchange Commission on September 26, 2002.

NOTE 2 - CHANGE IN ACCOUNTING PRINCIPLE

We adopted Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets," as of July 1, 2002. SFAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment, at least annually, in accordance with the provisions of SFAS No. 142. SFAS No. 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." In accordance with SFAS No. 142, during the December 2002 quarter we completed our initial assessment of impairment and determined that our goodwill was fully impaired and have recognized an impairment loss of \$420,000, net of taxes, in the condensed consolidated statement of operations as a change in accounting principle, effective July 1, 2002. The effect of the change in accounting principle to the quarter ended September 30, 2002 is as follows (dollars in thousands except per share amounts):

|  | Three months ended<br>September 30, 2002<br>----- |
|--|---|
| Net loss as originally reported              | \$ (783)  |
| Change in accounting principle, net of taxes | (420)   |
|  | -----   |
| Net loss as restated                         | \$(1,203)   |
|  | =====   |
| Basic and diluted loss per share:            |   |
| Net loss as originally reported              | \$ (0.34)   |
| Change in accounting principle               | (0.18)  |
|  | -----   |
| Net loss as restated                         | \$ (0.52)   |
|  | =====   |

Goodwill amortization of \$9,000 and \$19,000 was recognized in the three and six months ended December 31, 2001, respectively. Unaudited pro forma results of operations for the three and six months ended December 31, 2001, as if the change in accounting principle occurred at the beginning of the period reported, are as follows (dollars in thousands, except for per share amounts):

<TABLE>

<CAPTION>

|                                  | Three Months Ended<br>December 31, |           | Six Months Ended<br>December 31, |           |
|----------------------------------|------------------------------------|-----------|----------------------------------|-----------|
|                                  | 2002                               | 2001      | 2002                             | 2001      |
| <S>                              | <C>                                | <C>       | <C>                              | <C>       |
| Net loss                         | \$ (3,878)                         | \$ (753)  | \$ (5,081)                       | \$ (716)  |
|                                  | =====                              | =====     | =====                            | =====     |
| Basic and diluted loss per share | \$ (1.70)                          | \$ (0.33) | \$ (2.22)                        | \$ (0.31) |
|                                  | =====                              | =====     | =====                            | =====     |

</TABLE>

NOTE 3 - ACQUISITION OF THE ASSETS OF CENTURY ELECTRONICS MANUFACTURING, INC.

On October 24, 2001, we completed a transaction to purchase certain assets, but not assume any liabilities, of Century Electronics Manufacturing, Inc. ("Century"), an EMS company that filed for bankruptcy. As part of this transaction, we also purchased substantially all of the common stock of Century's subsidiary in Thailand. The aggregate purchase price of this transaction was approximately \$3.2 million in cash and was funded by our existing bank lines of credit.

Specifically, we purchased from Century certain equipment and machinery for approximately \$1.4 million and inventory for approximately \$900,000. We have and will continue to utilize some of the purchased assets at our other locations. We negotiated new facility leases in Marlborough, Massachusetts and Santa Clara, California and began operations in Marlborough and Santa Clara in connection with the purchase of these assets.

As part of the Century agreement we purchased the common stock of the Century subsidiary in Thailand ("Century Thailand") for approximately \$900,000. The acquisition of the Thailand subsidiary provides us with a low cost manufacturing facility in Southeast Asia. The acquisition of Century Thailand was accounted for using the purchase method of accounting and, accordingly, the statements of condensed consolidated operations include the results of the Thailand subsidiary from the date of acquisition. The assets acquired and liabilities assumed were recorded at fair value as determined by us based on information currently available. A summary of the assets acquired and the liabilities assumed in the acquisition is as follows (in thousands):

|                        |         |
|------------------------|---------|
| Estimated fair values: |         |
| Assets acquired        | \$1,392 |
| Liabilities assumed    | 476     |
|                        |         |
| Purchase price         | \$ 916  |
| Less cash received     | 787     |
|                        | -----   |
| Net cash paid          | \$ 129  |
|                        | =====   |

Unaudited pro forma results of operations for the three and six months ended December 31, 2001, as if the acquisition of the Thailand subsidiary had occurred at the beginning of the period reported, follow (dollars in thousands). The unaudited pro forma results are not necessarily indicative of

the results which would have occurred if the business combination had occurred on the date indicated:

|                   | Three Months Ended<br>December 31, 2001<br>----- | Six Months Ended<br>December 31, 2001<br>----- |
|-------------------|--|--|
| Revenue           | \$19,608<br>=====                                | \$40,548<br>=====                              |
| Net loss          | \$ (788)<br>=====                                | \$ (672)<br>=====                              |
| Loss per share:   |  |  |
| Basic and diluted | \$ (0.35)<br>=====                               | \$ (0.29)<br>=====                             |

NOTE 4 - EARNINGS PER SHARE

Basic earnings (loss) per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in our earnings (losses).

Common stock equivalents used in the determination of diluted earnings per share include the effect, when such effect is dilutive, of our outstanding employee stock options and the 8-1/2% Convertible Subordinated Debentures (which are convertible into 7,435 shares of common stock at \$212.50 per share of common stock). The following is a summary of the calculation of basic and diluted earnings per share (dollars in thousands, except per share data):

<TABLE>

<CAPTION>

|          | Three Months Ended<br>December 31,<br>----- |                   | Six Months Ended<br>December 31,<br>----- |                   |
|----------|---|-------------------|---|-------------------|
|          | 2002<br>-----                               | 2001<br>-----     | 2002<br>-----                             | 2001<br>-----     |
| <S>      | <C>   | <C>               | <C>                                       | <C>               |
| Net loss | \$ (3,878)<br>=====                         | \$ (762)<br>===== | \$ (5,081)<br>=====                       | \$ (735)<br>===== |

Weighted average shares:

|  |           |           |           |           |
|--|-----------|-----------|-----------|-----------|
| Basic weighted average<br>number of common shares<br>outstanding | 2,284,343 | 2,284,343 | 2,284,343 | 2,283,693 |
| Dilutive effect of<br>outstanding common<br>stock equivalents    | -         | -         | -         | -         |
|  | -----     | -----     | -----     | -----     |

Diluted weighed average  
number of common

|                                  |           |           |           |           |
|----------------------------------|-----------|-----------|-----------|-----------|
| shares outstanding               | 2,284,343 | 2,284,343 | 2,284,343 | 2,283,693 |
|                                  | =====     | =====     | =====     | =====     |
| Basic and diluted loss per share | \$ (1.70) | \$ (0.33) | \$ (2.22) | \$ (0.32) |
|                                  | =====     | =====     | =====     | =====     |

</TABLE>

Because we had a net loss for the three and six months ended December 31, 2002, there were no common stock equivalents which had a dilutive effect on earnings per share. However, if we had reported net income rather than a loss for the three and six months ended December 31, 2002, the additional diluted shares outstanding would have been 3,704 and 3,002 for the three and six months ended December 31, 2002, respectively. Further, options to purchase approximately 657,200 of common stock at prices ranging from \$1.05 to \$10.00 which were outstanding at December 31, 2002, would not have been included in the computation of diluted earnings per share for the three and six months ended December 31, 2002, because the exercise prices of these options were greater than the average market price of the common stock. If we had reported net income rather than a loss for the three and six months ended December 31, 2001, the additional diluted shares outstanding would have been 87,213 and 132,497 for the three and six months ended December 31, 2001, respectively. Options to purchase approximately 157,800 shares of common stock at prices ranging from \$5.80 to \$10.00 were outstanding at December 31, 2001, but were not included in the computation of diluted earnings per share for the three and six months ended December 31, 2001, because the exercise prices of these options were greater than the average market price of the common stock.

Convertible subordinated debentures aggregating \$1,580,000, due in 2008 and convertible at a price of \$212.50 per share at any time prior to maturity, were outstanding during the three and six months ended December 31, 2002 and 2001, but were not included in the computation of diluted earnings per share because the effect would be antidilutive.

#### NOTE 5 - REVENUE RECOGNITION

All of our subsidiaries recognize revenues and cost of sales upon shipment of products. We ship products FOB shipping point and accordingly, title and risk of ownership pass to the customer upon shipment.

Prior to June 30, 2002, the Moorpark facility historically generated a significant portion of its revenue through long-term contracts with suppliers of electronic components and products. Consequently, this operating unit historically used the percentage of completion method to recognize revenues and cost of sales. Percentage of completion was determined on the basis of costs incurred to total estimated costs. Contract costs include direct material and direct labor costs and those indirect costs related to the assembly process, such as indirect labor, supplies, tools, repairs and depreciation costs. Selling and administrative costs were charged to expense as incurred. In the period in which it was determined that a loss would result from the performance of a contract, the entire amount of the estimated loss was charged to cost of goods sold. Other changes in contract price and estimates of costs and profits at completion were recognized prospectively. The asset "costs and estimated earnings in excess of billings on uncompleted contracts" represented revenues recognized in excess of amounts billed.

During fiscal 2002, our Moorpark facility entered into sales contracts consistent with our other locations, and as such, recognized revenue on these new arrangements upon shipment of products rather than on a percentage of completion method. As a result, during most of fiscal 2002, the Moorpark facility was recognizing revenue upon shipment of product as well as under the percentage of completion method. Since June 30, 2002, no sales contracts have been accounted for using the percentage of completion method of accounting.

#### NOTE 6 - INVENTORIES

Inventories consist of the following (in thousands):

|                   | December 31,<br>2002 | June 30,<br>2002 |
|-------------------|----------------------|------------------|
|                   | -----                | -----            |
| Raw materials     | \$ 6,587             | \$ 7,553         |
| Work in process   | 3,288                | 3,174            |
| Finished goods    | 207                  | 496              |
|                   | -----                | -----            |
|                   | \$10,082             | \$11,223         |
|                   | =====                | =====            |
| Total inventories |                      |                  |

#### Note 7 - PROPERTY, EQUIPMENT AND IMPROVEMENTS

Property, equipment and improvements consist of the following (in thousands):

|  | December 31,<br>2002 | June 30,<br>2002 |
|--|----------------------|------------------|
|  | -----                | -----            |
| Buildings and improvements                     | \$ 4,076             | \$ 3,980         |
| Plant equipment                                | 17,172               | 16,243           |
| Office and other equipment                     | 3,091                | 2,941            |
| Less accumulated depreciation and amortization | (16,224)             | (14,355)         |
|  | -----                | -----            |
| Total property, equipment and improvements     | \$ 8,115             | \$ 8,809         |
|  | =====                | =====            |

#### NOTE 8 - CREDIT AGREEMENTS

At December 31, 2002, borrowings under our working capital facility for our domestic operating units amounted to \$5.2 million. This credit facility is collateralized by accounts receivable, inventory and equipment for our domestic operating units and matures September 25, 2003. At December 31, 2002, the weighted average interest rate on the line of credit was 4.91%. The line of credit agreement contains certain financial covenants, with which we were not in compliance at December 31, 2002. However, the terms of our line of credit have been amended as of February 5, 2003. Under the new terms, our line of credit is at \$8.5 million, bears interest at either the bank's prime rate (4.25% at December 31, 2002) plus 1.00% or a Eurodollar-base rate (1.37%

at December 31, 2002) plus 3.75%, and the covenants have been amended. We are currently and expect to be in compliance with the amended bank covenants. Our available borrowing capacity as of December 31, 2002, after giving effect to the amendment, was approximately \$1.8 million.

In addition, during fiscal 2002, we borrowed \$1.6 million on our equipment line of credit to finance our capital expenditures. This advance has a maturity date of October 24, 2006. At December 31, 2002, the balance outstanding was \$945,000 and the weighted average interest rate was 4.87%. Under the amended credit facility terms, interest is at either the bank's prime rate plus 1.00% or at a Eurodollar-base rate plus 3.75%. Additional advances under our equipment line of credit will not be available to us until a review by the bank at a future date.

We also have a credit facility agreement with Ulster Bank Markets for our Northern Ireland operating company. This agreement consists of an accounts receivable revolver, with maximum borrowings equal to the lesser of 75% of eligible receivables or 2,500,000 British pounds sterling (approximately \$4,025,000 at December 31, 2002), of which 500,000 British pounds sterling (approximately \$805,000 at December 31, 2002) consists of an overdraft facility, and bears interest at the bank's base rate (4.00% at December 31, 2002) plus 2.00%. At December 31, 2002, borrowings outstanding under this credit facility amounted to approximately \$2.9 million, of which the overdraft facility was fully utilized, and there was nominal available borrowing capacity. The credit facility agreement matures on November 30, 2003.

We also have a mortgage note secured by real property at Northern Ireland with an outstanding balance of \$732,000 at December 31, 2002. At December 31, 2002, we were in arrears and we are currently seeking to negotiate a payment plan.

#### NOTE 9 - BUSINESS SEGMENT AND GEOGRAPHIC INFORMATION

We operate in a single business segment - the EMS industry. Our revenues and long-lived assets, net of accumulated depreciation, by geographic area are as follows (in thousands):

|                  | Three Months Ended<br>December 31, |          | Six Months Ended<br>December 31, |          |
|------------------|------------------------------------|----------|----------------------------------|----------|
|                  | 2002                               | 2001     | 2002                             | 2001     |
| Revenues:        |                                    |          |                                  |          |
| United States    | \$14,526                           | \$16,590 | \$31,358                         | \$34,532 |
| Northern Ireland | 1,842                              | 2,655    | 4,991                            | 4,347    |
| Thailand         | 931                                | 349      | 1,686                            | 349      |
|                  | -----                              | -----    | -----                            | -----    |
| Total revenues   | \$17,299                           | \$19,594 | \$38,035                         | \$39,228 |
|                  | =====                              | =====    | =====                            | =====    |
|                  | December 31,                       | June 30, |                                  |          |
|                  | 2002                               | 2002     |                                  |          |
|                  | -----                              | -----    |                                  |          |

|                         |         |         |
|-------------------------|---------|---------|
| Long-lived assets:      |         |         |
| United States           | \$6,262 | \$7,487 |
| Northern Ireland        | 1,672   | 1,549   |
| Thailand                | 181     | 193     |
|                         | -----   | -----   |
| Total long-lived assets | \$8,115 | \$9,229 |
|                         | =====   | =====   |

#### NOTE 10 - FOREIGN CURRENCY FORWARD CONTRACTS

It is our policy not to enter into derivative financial instruments for speculative purposes. We may, from time to time, enter into foreign currency forward exchange contracts in an effort to protect us from adverse currency rate fluctuations on foreign currency commitments entered into in the ordinary course of business. These commitments are generally for terms of less than one year. The foreign currency forward exchange contracts are executed with banks believed to be creditworthy and are denominated in currencies of major industrial countries. In accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," all derivative financial instruments are measured at fair value and are recognized as either assets or liabilities in the balance sheet. The accounting treatment of changes in fair value is dependent upon whether or not a derivative financial instrument is designated as a hedge and, if so, the type of hedge. Changes in fair value are recognized in current results of operations for fair value hedges and in other comprehensive income for cash flow hedges. Derivative financial instruments not qualifying for hedge accounting treatment under SFAS No. 133 are recognized as assets or liabilities with gains or losses recognized in current results of operations. At December 31, 2002, we did not have any open forward foreign currency contracts.

#### NOTE 11 - COMMITMENTS AND CONTINGENCIES - ENVIRONMENTAL MATTERS

Since the early 1990s, we have been, and continue to be, involved in certain remediation and investigative studies regarding soil and groundwater contamination at the site of a former printed circuit board manufacturing plant in Anaheim, California. One of our former subsidiaries, Aeroscientific Corp., leased the Anaheim facility. Under the terms of a cost sharing agreement entered into in July 1993, the remaining remediation costs are currently being shared on a 50-50 basis with the landlord. There is no environmental insurance coverage for this remediation. At December 31, 2002, we had a reserve of \$416,000 for future remediation costs. Management, based in part on consultations with outside environmental engineers and scientists, believes that this reserve is adequate to cover its share of future remediation costs at this site. However, the future actual remediation costs could differ significantly from the estimates and our portion could exceed the amount of our reserve. Our liability for remediation in excess of our reserve could have a material adverse impact on our business, financial condition, results of operations and cash flows.

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

THIS QUARTERLY REPORT ON FORM 10-Q, INCLUDING THE DISCLOSURES BELOW, CONTAINS FORWARD-LOOKING STATEMENTS THAT INVOLVE SUBSTANTIAL RISKS AND UNCERTAINTIES. WHEN USED HEREIN, THE TERMS "ANTICIPATES," "EXPECTS," "ESTIMATES," "BELIEVES," "WILL" AND SIMILAR EXPRESSIONS, AS THEY RELATE TO US OR OUR MANAGEMENT, ARE INTENDED TO IDENTIFY SUCH FORWARD-LOOKING STATEMENTS. FORWARD-LOOKING STATEMENTS IN THIS REPORT OR HEREAFTER INCLUDED IN OTHER PUBLICLY AVAILABLE DOCUMENTS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ("SEC"), REPORTS TO THE STOCKHOLDERS OF SMTEK INTERNATIONAL, INC., A DELAWARE CORPORATION (THE "COMPANY," "WE," "US" OR "OUR") AND OTHER PUBLICLY AVAILABLE STATEMENTS ISSUED OR RELEASED BY US INVOLVE KNOWN AND UNKNOWN RISKS, UNCERTAINTIES AND OTHER FACTORS WHICH COULD CAUSE OUR ACTUAL RESULTS, PERFORMANCE (FINANCIAL OR OPERATING) OR ACHIEVEMENTS TO DIFFER FROM THE FUTURE RESULTS, PERFORMANCE (FINANCIAL OR OPERATING) OR ACHIEVEMENTS EXPRESSED OR IMPLIED BY FORWARD-LOOKING STATEMENTS. THESE RISKS INCLUDE, BUT ARE NOT LIMITED TO, THE RISKS SET FORTH HEREIN AND IN OTHER DOCUMENTS FILED WITH THE SEC, EACH OF WHICH COULD ADVERSELY AFFECT OUR BUSINESS AND THE ACCURACY OF THE FORWARD-LOOKING STATEMENTS CONTAINED HEREIN. FUTURE EXPECTED RESULTS ARE BASED UPON MANAGEMENT'S BEST ESTIMATES BASED UPON CURRENT CONDITIONS AND THE MOST RECENT RESULTS OF OPERATIONS. OUR ACTUAL RESULTS, PERFORMANCE OR ACHIEVEMENTS MAY DIFFER MATERIALLY FROM THOSE EXPRESSED OR IMPLIED BY SUCH FORWARD-LOOKING STATEMENTS.

THE FOLLOWING DISCUSSION AND ANALYSIS SHOULD BE READ IN CONJUNCTION WITH THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND RELATED NOTES INCLUDED ELSEWHERE IN THIS REPORT.

#### UPDATE OF RISK FACTORS

The following updates the risk factors identified in our 2002 Annual Report on Form 10-K which was filed with the SEC on September 26, 2002.

#### Our Debt Agreements Contain Certain Financial Covenants That Must Be Met.

As a result of consolidating our San Diego facility and the related costs incurred during the second quarter of 2003, we were in violation of certain covenants on our domestic line of credit agreement as of December 31, 2002. In February 2003, the bank either removed or amended the related restricted covenants in an amendment to the credit agreement which enabled us to regain compliance with the terms of the credit agreement. If we are unable to comply with the terms of our revised financial covenants, our lender may declare a default and immediately accelerate the due date of our outstanding loans. If we are unable to repay our outstanding loans when asked to do so by the lender, the lender may exercise any one or more of the remedies available to it, including foreclosing on the assets pledged to support the facility, which includes virtually all of our assets.

Our domestic line of credit agreement is set to mature in September 2003. Our borrowings on this line of credit at December 31, 2002 amounted to \$5.2 million. We can provide no assurance that the agreement will be renewed or that any renewal would occur on commercially reasonable terms. We remain dependent on our line of credit for operations and growth and may have to

explore alternative financing if the bank does not renew our line of credit or if amounts outstanding become immediately payable as a result of future covenant violations.

We also have a mortgage note secured by real property at Northern Ireland with an outstanding balance of \$732,000 at December 31, 2002. At December 31, 2002, we were in arrears and we are currently seeking to negotiate a payment plan.

We may require additional financing to satisfy our debt obligations. However, there can be no assurance that we will be able to obtain additional debt or equity financing when needed, or with acceptable terms. Any additional debt or equity financing may involve substantial dilution to our stockholders, restrictive covenants or high interest costs. The failure to raise needed funds on sufficiently favorable terms could have a material adverse effect on our business, operating results and financial condition.

Although management believes our cash resources, cash from operations and available borrowing capacity on our working capital lines of credit are sufficient to fund operations, if we cannot refinance the domestic line of credit upon its maturity or find alternative financing/funding of this obligation, there is no assurance that we will continue as a going concern.

Our Stock Price Has Been And Continues To Be Volatile. Based Upon Any Number of Factors, We May Face Delisting Proceedings From Nasdaq.

The market price for our common stock continues to be volatile due to various factors. These factors include, but are not limited to:

- our public stock float being relatively small and thinly traded;
- announcements by us or our competitors of new contracts or technological innovations;
- fluctuations in our quarterly and annual operating results;
- continued losses in each quarter;
- acquisition-related announcements; and
- general market conditions.

In addition, in recent years, our stock price has experienced significant price fluctuations for a variety of reasons, both internal to us and due to external conditions.

Under Nasdaq rules, if our stock trades below \$1.00 per share for 30 consecutive days, or if we are below \$2.5 million in shareholders' equity, we face delisting proceedings from Nasdaq. Our common stock has traded below \$1.00 per share for 30 consecutive days starting in October 2002. It has traded below \$1.00 per share for much of the time since October 2002. Further, we are now below \$2.5 million in shareholders' equity. Therefore, we are not in compliance with two Nasdaq Small Cap Market criteria for continued listing.

In November 2002, we received a deficiency notice from Nasdaq relating to our stock trading below \$1.00 per share for 30 consecutive days. The notice indicated that we have until May 2003 in which to show 10 consecutive trading days where the closing minimum bid is \$1.00 per share or more. We have not yet satisfied that requirement at this time. However, even if we met this criterion at any time before May 2003, we are still likely to be delisted if we continue to fail to meet the \$2.5 million minimum level of stockholders' equity criterion that Nasdaq has established. While we have not yet received any deficiency or other similar notice from Nasdaq with reference to our failure to meet the criterion of having \$2.5 million in stockholders' equity, we expect to receive a notice from Nasdaq in this regard after the filing of this Form 10-Q.

If we are delisted from the Nasdaq Small Cap Market, we may be transferred to the over-the-counter market on the NASD Electronic Bulletin Board or to the "pink sheets" maintained by the National Quotation Bureau, Inc. There is also a risk that we will not continue to be listed at all. Non-prominent trading markets are generally considered to be less efficient than markets such as Nasdaq or other national exchanges, and may cause us difficulty in obtaining future financing. If our stock is no longer traded in a prominent trading market, or at all, it may be difficult for you to sell shares that you own, and the price of the stock may be negatively affected.

For companies whose securities are traded in the Over-The-Counter Market, it is more difficult: (i) to obtain accurate quotations and (ii) to obtain coverage for significant news events because major wire services, such as the Dow Jones News Service, generally do not publish press releases about such companies.

#### DESCRIPTION OF THE BUSINESS

SMTEK International, Inc. (the "Company," "we," "us" or "our") is an electronics manufacturing services ("EMS") provider to original equipment manufacturers ("OEMs") primarily in the industrial and instrumentation, medical, telecommunications, security, financial services automation and aerospace and defense industries. We provide integrated solutions to OEMs across the entire product life cycle, from design to manufacturing to end-of-life services, for the worldwide low-to-medium volume, high complexity segment of the EMS industry.

We have seven wholly owned subsidiaries: SMTEK, Inc. (dba SMTEK Moorpark), located in Moorpark, California; Technetics, Inc. (dba SMTEK San Diego), located in Poway, California (see discussion in next paragraph); Jolt Technology, Inc. (aka SMTEK Fort Lauderdale), located in Fort Lauderdale, Florida; SMTEK Europe Limited, located in Craigavon, Northern Ireland; SMTEK New England, located in Marlborough, Massachusetts; SMTEK Santa Clara, located in Santa Clara, California; and SMTEK International Thailand Limited, located in Ayutthya, Thailand.

On November 19, 2002, we announced that we are consolidating our Poway facility into our other California operations in Moorpark and Santa Clara. As a result, we will record during fiscal year 2003 a one-time charge of

approximately \$2.3 million to \$3.0 million for severance and other costs related to facilities consolidation. As of December 31, 2002, costs of approximately \$2.2 million, related to the consolidation, have been recognized in the condensed consolidated statement of operations. This transition is expected to be completed by the quarter ending March 2003.

#### CRITICAL ACCOUNTING POLICIES

In response to SEC Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies," we have identified our most critical accounting policies that require significant management judgment or involve complex estimates upon which our financial status depends. The consolidated condensed financial statements and related notes within this Quarterly Report on Form 10-Q contain information that is pertinent to our accounting policies and to management's discussion and analysis and should also be read in conjunction with our 2002 Annual Report on Form 10-K as filed with the SEC on September 26, 2002. The information that follows describes specific disclosures about our accounting policies regarding risks, estimates, subjective decisions, or assessments under which materially different results of operations and financial condition could have been reported had different assumptions been used or different conditions existed.

REVENUE AND COST RECOGNITION--We recognize revenues and cost of sales upon shipment of products. Prior to June 30, 2002, our Moorpark subsidiary historically generated a significant portion of its revenue through long-term contracts with suppliers of electronic components and products. Consequently, this operating unit historically used the percentage of completion method to recognize revenues and cost of sales. Percentage of completion was determined on the basis of costs incurred to total estimated costs. Contract costs include direct material and direct labor costs and those indirect costs related to the assembly process, such as indirect labor, supplies, tools, repairs and depreciation costs. Selling and administrative costs were charged to expense as incurred. In the period in which it was determined that a loss would result from the performance of a contract, the entire amount of the estimated loss was charged to cost of goods sold. Other changes in contract price and estimates of costs and profits at completion were recognized prospectively. A change in our estimate of costs to complete may have resulted in lower earnings than currently recorded. A portion of the asset "costs and estimated earnings in excess of billings on uncompleted contracts" represented revenues recognized in excess of amounts billed.

During fiscal 2002, our Moorpark facility entered into sales contracts consistent with our other locations, and as such, recognized revenue on these new arrangements upon shipment of products rather than on a percentage of completion method. As a result, during most of fiscal 2002, the Moorpark facility was recognizing revenue upon shipment of products as well as under the percentage of completion method. Since June 30, 2002, no sales contracts have been accounted for using the percentage of completion method of accounting.

ACCOUNTS RECEIVABLE--We perform ongoing credit evaluations of our customers and adjust credit limits based upon each customer's payment history and current credit worthiness, as determined by credit information available at that time. We continuously monitor collections and payments from our

customers and we maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. If the condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

INVENTORIES--Inventories are stated at the lower of cost or net realizable value, with cost determined principally by use of the first-in, first-out method. We write down inventory for slow-moving and obsolete inventory based on assessments of future demands, market conditions and customers who may be experiencing financial difficulties. If these factors are less favorable than those projected, additional inventory write downs may be required.

LONG-LIVED ASSETS--Property, equipment and improvements are stated at cost. Depreciation and amortization are computed on the straight-line method. The principal estimated useful lives are: buildings - 20 years; improvements - 5 to 10 years; and plant, office and other equipment - 3 to 7 years. Property, equipment and improvements acquired by our Northern Ireland operating unit are recorded net of capital grants received from the Industrial Development Board for Northern Ireland. Goodwill represents the excess of acquisition cost over the fair value of net assets of a purchased business, and has been amortized over 5 to 15 years through June 30, 2002. Amortization of goodwill ceased on July 1, 2002 when we adopted Statement of Financial Accounting Standards ("SFAS") No. 142. As a result of implementing SFAS No. 142, we determined that our goodwill was fully impaired and recognized an impairment loss of \$420,000, net of taxes, in the condensed consolidated statement of operations, effective July 1, 2002. The recoverability of long-lived assets is evaluated whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable, and if future undiscounted cash flows expected to result from the use of such assets are believed insufficient to recover the carrying value of the asset, the carrying value is written down to fair value in the period the impairment is identified. Factors we consider important which could trigger an impairment review include, but are not limited to, the following:

- the asset's ability to continue to generate income;
- loss of legal ownership or title to the asset;
- significant changes in our strategic business objectives and utilization of the asset;
- the impact of significant negative industry or economic trends; or
- significant decrease in the market value of the asset.

## RESULTS OF OPERATIONS

We utilize a 52-53 week fiscal year ending on the Friday closest to June 30, which for fiscal year 2002 fell on June 28, 2002. In the accompanying condensed consolidated financial statements, the 2002 fiscal year end is shown as June 30 and the interim period end for both years is shown as December 31 for clarity of presentation. The actual interim periods ended on December 27,

2002 and December 28, 2001.

Consolidated revenues for the three and six months ended December 31, 2002 were \$17.3 million and \$38.0 million, respectively, compared to \$19.6 million and \$39.2 million for the three and six months ended December 31, 2001, respectively. The decrease in revenues was mainly due to the current downward economic and EMS market trends in the United States, slightly offset by an increase in revenues generated at our three new facilities. Starting in the third quarter of fiscal 2001, existing customers began to defer shipments, and some cancelled orders.

Consolidated gross profit for the three and six months ended December 31, 2002 was \$798,000 (4.6% of sales) and \$2.5 million (6.6% of sales), respectively, compared to \$2.0 million (10.0% of sales) and \$4.0 million (10.1% of sales) for the three and six months ended December 31, 2001, respectively. Gross profit for the three and six months ended December 31, 2001 was positively impacted by the benefit received from inventory used during the period that was purchased at a discount from Century Electronics Manufacturing, Inc. ("Century"). Excluding the positive impact from these reduced inventory costs, we estimate that the consolidated gross profit for the three and six months ended December 31, 2001 would have been approximately \$1.2 million (6.0% of sales) and \$3.2 million (8.1% of sales), respectively. The decrease in gross profit and gross profit margin, excluding the purchase benefit, was due to an increase in fixed costs, primarily due to our new facilities and lower revenues, partially offset by a decrease in headcount and decrease in material costs.

Administrative and selling expenses were \$4.4 million and \$6.5 million for the three months and six months of December 31, 2002, respectively, compared to \$2.4 million and \$4.1 million for the three and six months of December 31, 2001, respectively. The increase in administrative and selling expenses included the recognition, during the second quarter of 2003, of approximately \$1.6 million in expenses related to the closing of our San Diego facility. These costs are detailed as follows: \$1.0 million loss related to the lease of the building, \$370,000 related to write-off of leasehold improvements and \$200,000 related to severance and other related costs. In the second quarter of 2003, we also recognized a \$600,000 loss related to the lease at our former Thousand Oaks facility. Also contributing to the increase in expenses for the six months ended December 31, 2002 were costs incurred by our three new facilities that were created upon the completion of the Century transaction in mid-October 2001.

Total non-operating expense was \$318,000 and \$624,000 for the three and six months ended December 31, 2002, respectively, compared to \$265,000 and \$509,000 for the three and six months ended December 31, 2001, respectively. The primary reason for this increase was due to the increase in interest expense as a result of higher levels of debt outstanding during the three and six months ended December 31, 2002 as compared to the three and six months ended December 31, 2001. The increased debt level is a result of the acquisition costs of the new facilities and from supporting their working capital requirements.

We had an income tax provision of \$1,000 and \$6,000 for the three and six months ended December 31, 2002, respectively, as compared to \$12,000 and \$27,000 for the three and six months ended December 31, 2001, respectively.

The income tax provision for the three and six months ended December 31, 2002 was lower than that for the three and six months ended December 31, 2001, due mainly to minimum state and federal taxes that were incurred.

Net loss from operations was \$3.9 million and \$4.7 million for the three and six months ended December 31, 2002, or \$1.70 and \$2.04 loss per diluted share, respectively, compared to net loss from operations of \$762,000 and \$735,000 for the three and six months ended December 31, 2001, or \$0.33 or \$0.32 loss per diluted share, due mainly to lower gross profit and higher administrative and selling expenses and non-operating expense.

#### CHANGE IN ACCOUNTING PRINCIPLE

We adopted SFAS No. 142, "Goodwill and Other Intangible Assets," as of July 1, 2001. SFAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment, at least annually, in accordance with the provisions of SFAS No. 142. SFAS No. 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." In accordance with SFAS No. 142, during the December 2002 quarter we completed our initial assessment of impairment and determined that our goodwill was fully impaired and have recognized an impairment loss of \$420,000, net of taxes, in the condensed consolidated statement of operations as a change in accounting principle, effective July 1, 2002.

#### RECENT ACCOUNTING PRONOUNCEMENTS

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 replaces SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." The primary objectives of SFAS No. 144 were to develop one accounting model, based on the framework established in SFAS No. 121, for long-lived assets to be disposed of by sale and to address other significant implementation issues. While SFAS No. 144 supersedes SFAS No. 121, it retains many of the fundamental provisions of SFAS No. 121. SFAS No. 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001. We have adopted SFAS No. 144 as of July 1, 2002.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 requires recognition of a liability for a cost associated with an exit or disposal activity when the liability is incurred, as opposed to when the entity commits to an exit plan under previous guidance. SFAS No. 146 is effective for exit or disposal activities initiated after December 31, 2002. We believe that the adoption of SFAS No. 146 will not have a material impact on our results of operations or financial position.

#### LIQUIDITY AND CAPITAL RESOURCES

Our primary sources of liquidity are our cash and cash equivalents,

which amounted to \$628,000 at December 31, 2002, and amounts available under our bank lines of credit, which provided approximately \$1.8 million of availability in excess of current borrowings at December 31, 2002, after giving effect to the amendment to the credit agreement discussed below. During the six months ended December 31, 2002, cash and cash equivalents decreased by \$188,000. This decrease resulted from purchases of equipment of \$907,000 and financing activities of \$61,000, partially offset by cash provided by operations of \$815,000.

Net cash provided by operating activities of \$815,000 for the six months ended December 31, 2002 was attributable primarily to facility consolidation costs of \$1.8 million, a decrease in inventories of \$1.2 million and an increase in accrued liabilities of \$1.8 million offset by our net loss before depreciation and amortization of \$3.8 million.

Net cash used in investing activities was \$907,000 for the six months ended December 31, 2002 compared to \$2.8 million for the six months ended December 31, 2001. The cash used was for the purchase of capital expenditures mainly for production purposes.

Net cash used in financing activities was \$61,000 for the six months ended December 31, 2002 compared to net cash provided by financing activities of \$1.6 million for the six months ended December 31, 2001. At December 31, 2002, we had approximately \$1.8 million available to borrow under our bank lines of credit, after giving effect to the amendment to the credit agreement discussed below.

At December 31, 2002, borrowings under our working capital facility for our domestic operating units amounted to \$5.2 million. This credit facility is collateralized by accounts receivable, inventory and equipment for our domestic operating units and matures September 25, 2003. At December 31, 2002, the weighted average interest rate on the line of credit was 4.91%. The line of credit agreement contains certain financial covenants, with which we were not in compliance at December 31, 2002. However, the terms of our line of credit have been amended as of February 5, 2003. Under the new terms, our line of credit is at \$8.5 million, bears interest at either the bank's prime rate (4.25% at December 31, 2002) plus 1.00% or a Eurodollar-base rate (1.37% at December 31, 2002) plus 3.75%, and the covenants have been amended. We are currently and expect to be in compliance with the amended bank covenants. Our available borrowing capacity as of December 31, 2002, after giving effect to the amendment, was approximately \$1.8 million.

In addition, during fiscal 2002 we borrowed \$1.6 million on our equipment line of credit to finance our capital expenditures. This advance has a maturity date of October 24, 2006. At December 31, 2002, the balance outstanding was \$945,000 and the weighted average interest rate was 4.87%. Under the amended credit facility terms, interest is at either the bank's prime rate plus 1.00% or at a Eurodollar-base rate plus 3.75%. Additional advances under our equipment line of credit will not be available to us until a review by the bank at a future date.

We also have a credit facility agreement with Ulster Bank Markets for our Northern Ireland operating company. This agreement consists of an accounts receivable revolver, with maximum borrowings equal to the lesser of 75% of eligible receivables or 2,500,000 British pounds sterling

(approximately \$4,025,000 at December 31, 2002), of which 500,000 British pounds sterling (approximately \$805,000 at December 31, 2002) consists of an overdraft facility, and bears interest at the bank's base rate (4.00% at December 31, 2002) plus 2.00%. At December 31, 2002, borrowings outstanding under this credit facility amounted to approximately \$2.9 million, of which the overdraft facility was fully utilized, and there was nominal available borrowing capacity. The credit facility agreement matures on November 30, 2003.

We also have a mortgage note secured by real property at Northern Ireland with an outstanding balance of \$732,000 at December 31, 2002. At December 31, 2002, we were in arrears and we are currently seeking to negotiate a payment plan.

We anticipate that additional expenditures of as much as \$125,000 may be made during the remainder of fiscal 2003, primarily to improve production efficiency at our subsidiaries. A substantial portion of these capital expenditures is expected to be financed by our line of credit or other notes/leases payable.

At December 31, 2002, the ratio of current assets to current liabilities was 0.9 to 1.0 compared to 1.3 to 1.0 at June 30, 2002. At December 31, 2002, we had \$2.9 million of negative working capital compared to \$5.9 million of working capital at June 30, 2002. At December 31, 2002, we had long-term borrowings of \$4.6 million compared to \$10.1 million at June 30, 2002. The decreases in the working capital and long-term debt is due to the reclassification of our domestic line of credit of \$5.2 million from long-term debt to current liabilities as this matures in less than 12 months. In addition, contributing to the decrease in working capital is an increase in lease reserves recognized in the second quarter of 2003.

As more fully described in Note 6 to the notes to our consolidated financial statements in our June 30, 2002 Form 10-K, at December 31, 2002, we have a federal tax assessment liability of approximately \$1.1 million and a related accrued interest liability of approximately \$1.3 million, which reflect the results of a settlement with the IRS Appeals Division in December 2001. We are currently seeking an installment payment plan with the IRS.

We have experienced and may continue to experience an adverse effect on our operating results and our financial condition, especially if current economic conditions continue for an extended period of time, despite our cost reduction measures and efficiency improvements at our operating subsidiaries. We are focused on the consolidation and streamlining of operations so as to reduce our excess capacity to better match market conditions. Recent actions taken and strategies being pursued are as follows:

- Transitioning the San Diego facility and evaluating further opportunities of consolidation, transition or sale of other facilities.
- Continuing focus on cost reductions related to pertinent production levels and reductions in administrative costs.
- Focusing our marketing efforts in the solicitation of customers in noneconomically affected industries.

For further discussion, see section entitled "Risk Factors That May Affect Your Decision to Invest in Us" in our 2002 Form 10-K, which was filed with the SEC on September 26, 2002 and to the discussion in this Form 10-Q under the heading "Update of Risk Factors."

We remain dependent on our lines of credit for operations and growth. Our domestic line of credit agreement is set to mature in September 2003. We can provide no assurance that the agreement will be renewed or that any renewal would occur on commercially reasonable terms. We may have to explore alternative financing if the bank does not renew our line of credit.

We may require additional financing to satisfy our debt obligations. However, there can be no assurance that we will be able to obtain additional debt or equity financing when needed, or on acceptable terms. Any additional debt or equity financing may involve substantial dilution to our stockholders, restrictive covenants or high interest costs. The failure to raise needed funds on sufficiently favorable terms could have a material adverse effect on our business, operating results, and financial condition.

Although management believes our cash resources, cash from operations and available borrowing capacity on our working capital lines of credit are sufficient to fund operations, if we cannot refinance the domestic line of credit upon its maturity or find alternative financing/funding of this obligation, there is no assurance that we will continue as a going concern.

#### ENVIRONMENTAL MATTERS

Since the early 1990s, we have been, and continue to be, involved in certain remediation and investigative studies regarding soil and groundwater contamination at the site of a former printed circuit board manufacturing plant in Anaheim, California. One of our former subsidiaries, Aeroscientific Corp., leased the Anaheim facility. Under the terms of a cost sharing agreement entered into in July 1993, the remaining remediation costs are currently being shared on a 50-50 basis with the landlord. There is no environmental insurance coverage for this remediation. At December 31, 2002, we had a reserve of \$416,000 for future remediation costs. Management, based in part on consultations with outside environmental engineers and scientists, believes that this reserve is adequate to cover its share of future remediation costs at this site. However, the future actual remediation costs could differ significantly from the estimates and our portion could exceed the amount of our reserve. Our liability for remediation in excess of our reserve could have a material adverse impact on our business, financial condition, results of operations and cash flows.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our financial instruments include cash and cash equivalents, accounts receivable and short-term and long-term debt. At December 31, 2002, the carrying amount of long-term debt (including the current portion thereof but excluding bank lines of credit) was \$7.9 million and the fair value was \$7.4 million. The carrying values of our other financial instruments approximated

their fair values. The fair value of our financial instruments is estimated based on quoted market prices for the same or similar issues. A change in interest rates of one percent would result in an annual impact on interest expense of approximately \$110,000.

It is our policy not to enter into derivative financial instruments for speculative purposes. We may, from time to time, enter into foreign currency forward exchange contracts in an effort to protect us from adverse currency rate fluctuations on foreign currency commitments entered into in the ordinary course of business. These commitments are generally for terms of less than one year. The foreign currency forward exchange contracts are executed with banks believed to be creditworthy and are denominated in currencies of major industrial countries. In accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," all derivative financial instruments are measured at fair value and are recognized as either assets or liabilities in the balance sheet. The accounting treatment of changes in fair value is dependent upon whether or not a derivative financial instrument is designated as a hedge and, if so, the type of hedge. Changes in fair value are recognized in current results of operations for fair value hedges and in other comprehensive income for cash flow hedges. Derivative financial instruments not qualifying for hedge accounting treatment under SFAS No. 133 are recognized as assets or liabilities with gains or losses recognized in current results of operations. At December 31, 2002, we did not have any open forward foreign currency contracts.

Our operations consist of investments in foreign operating units. Our foreign subsidiaries represent approximately 18% of our revenues and 26% of our total assets. As a result, our financial results have been and may continue to be affected by changes in foreign currency exchange rates.

#### ITEM 4. CONTROLS AND PROCEDURES

Within the 90 days prior to the filing date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these internal controls subsequent to the date of their most recent evaluation.

#### PART II. OTHER INFORMATION

##### ITEM 1. LEGAL PROCEEDINGS

In the ordinary course of business, we experience various types of

claims which sometimes result in litigation or other legal proceedings. We do not anticipate that any of these claims or proceedings that are currently pending will have a material adverse effect on us.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

This information is set forth in this report under the captions "Update of Risk Factors - Our Debt Agreements Contain Financial Covenants That Must Be Met" and "Management's Discussion and Analysis - Liquidity" and is incorporated herein by reference.

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

At the 2002 Annual Meeting of Stockholders, held on November 12, 2002, James P. Burgess was elected as Class I director. Directors whose terms of office continued after the meeting were Kimon Amenogiannis, Clay M. Biddinger, Oscar B. Marx, III and Steven M. Waszak. There were 2,284,343 shares of common stock outstanding and entitled to vote at this meeting. Following is a summary of the results of voting:

|  | Votes For<br>----- | Votes<br>Against or<br>Withheld<br>----- |
|--|--------------------|--|
| Election of James P. Burgess as director | 2,094,964          | 66,588                                   |

### ITEM 5. OTHER INFORMATION

#### PRE-APPROVAL OF NON-AUDIT SERVICES

In accordance with Section 10A of the Securities Exchange Act of 1934, as amended by Section 202 of the Sarbanes-Oxley Act of 2002, the members of the Audit Committee approved non-audit, tax-related services by our auditors during this reported fiscal quarter.

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

#### a. Exhibits:

10.1 Amendment No. 4 to Credit Agreement, dated February 5, 2003, between the Company and Comerica Bank.

99.1 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

#### b. Reports on Form 8-K:

On October 14, 2002, the Board of Directors and the Audit Committee dismissed KPMG LLP as our principal independent auditors and engaged PricewaterhouseCoopers LLP as our principal independent auditors.

SIGNATURE

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.

February 7, 2003  
Date

/s/ Edward J. Smith  
Edward J. Smith  
Chief Executive Officer and  
President (Principal Executive  
Officer)

/s/ Kirk A. Waldron  
Kirk A. Waldron  
Senior Vice President and Chief  
Financial Officer (Principal  
Financial Officer)

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Edward J. Smith, certify that:

1. I have reviewed this quarterly report on Form 10-Q of SMTEK 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: February 7, 2003

/s/ Edward J. Smith  
Edward J. Smith  
Chief Executive Officer and President  
SMTEK International, Inc.

#### CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Kirk A. Waldron, certify that:

1. I have reviewed this quarterly report on Form 10-Q of SMTEK 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: February 7, 2003

/s/ Kirk A. Waldron

Kirk A. Waldron

Senior Vice President and Chief Financial Officer

SMTEK International, Inc.

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Exhibit 10.1

AMENDMENT NO. 4 TO CREDIT AGREEMENT AND WAIVER

This Amendment dated as of the 5th day of February, 2003 by and between Smttek International, Inc., a Delaware corporation ("Company") and Comerica Bank, a Michigan banking corporation, ("Bank").

WITNESSETH:

WHEREAS, Company and Bank entered into a Credit Agreement dated September 25, 2001, as amended by an Amendment dated December 21, 2001, an Amendment dated May 1, 2002 and an Amendment dated September 24, 2002 ("Agreement").

WHEREAS, Company and Bank desire to amend the Agreement and waive Company's violation of certain covenants, in each case as expressly set forth herein.

NOW, THEREFORE, the Company and the Bank agree as follows:

1. Each of the following definitions set forth in Section 1 of the Agreement is deleted in its entirety and the following is inserted in its place:

"`Applicable Eurodollar Margin' shall mean before the occurrence of the Availability Event, three and three-quarters percent (3-3/4%) and after the occurrence of the Availability Event, four and one quarter percent (4-1/4%)."

"`Applicable L/C Commission Rate' shall mean before the occurrence of the Availability Event, three and three-quarters percent (3-3/4%) per annum and after the occurrence of the Availability Event, four and one quarter percent (4-1/4%)."

"`Applicable Prime Margin' shall mean, before the occurrence of the Availability Event, one percent (1%) and after the occurrence of the Availability Event, one and one-half percent (1-1/2%)."

"`Borrowing Base' shall mean (a) on any date of determination prior to the occurrence of the Availability Event, the sum of (i) eighty five percent (85%) of Eligible Accounts plus (ii) the lesser of (x) thirty percent (30%) of Eligible Inventory and (y) \$3,000,000, and (b) on any date of determination following the occurrence of the Availability Event, the sum of (i) eighty five percent (85%) of Eligible Accounts plus (ii) the lesser of (x) twenty percent (20%) of Eligible Inventory and (y) \$2,000,000."

2. The following definition is inserted in Section 1 in its appropriate alphabetical order:

"`Availability Event' shall be deemed to have occurred if Availability is below \$1,000,000 for five (5) calendar days (whether or not consecutive) during any thirty (30) calendar day period."

3. The definition of "Daily Reporting Event" is deleted from Section 1 in

its entirety.

4. The last sentence of Section 2.6 is deleted in its entirety, and the following is inserted in its place:

"Company shall pay to Bank annually in advance a per annum fee equal to the Applicable L/C Commission Rate of the amount of each standby Letter of Credit and of each commercial letter of credit."

5. Section 8.1(c)(iv) of the Agreement is amended to read in its entirety as follows:

"(iv) a borrowing base report, each in form acceptable to Bank; provided however, at all times after the occurrence of the Availability Event, updated borrowing base reports shall be due each Business Day."

6. Section 8.11 of the Agreement is amended to read in its entirety as follows:

"Maintain as of the end of each fiscal quarter an Adjusted Tangible Net Worth of not less than the following amounts during the periods specified below:

|                                      |           |            |
|--------------------------------------|-----------|------------|
| March 31, 2003 through June 29, 2003 | \$400,000 |            |
| June 30, 2003 and thereafter         |           | \$600,000" |

7. Section 8.12 of the Agreement is amended to read in its entirety as follows:

"8.12 Reserved."

8. Section 8.14 of the Agreement is amended to read in its entirety as follows:

"Maintain for the fiscal quarter ending June 30, 2003, Net Income of not less than \$450,000."

9. Section 8.15 of the Agreement is amended to read in its entirety as follows:

"Not allow the loss for the fiscal quarter ending March 31, 2003 to be more than \$1,275,000."

10. Sections 2.1 and 2.6 of the Agreement are amended to change each reference therein to "Eleven Million Dollars (\$11,000,000)" to "Eight Million Five Hundred Thousand Dollars (\$8,500,000)".

11. Following the occurrence of the Availability Event, (a) the remittance basis provisions of Sections 3.2 and 3.3 of the Security Agreements from Company and the Guarantors in favor of the Bank shall apply and any failure by Company or any of the Guarantors to comply with such remittance basis provisions shall be an Event of Default under the Agreement, (b) Company's ability to use Bank's "Sweep to Loan" system shall be terminated, and (c) Company shall pay Bank, in advance and on the first day of each month, a monthly collateral monitoring fee of \$750 (such fee for the month during which the Availability Event occurs to be paid on a pro-rata basis on the first day of the next succeeding month).

12. Company has notified Bank that it has violated the provisions of Section(s) 8.11 (Adjusted Total Net Worth), 8.12 (Total Debt to Adjusted Net Worth) and 8.15 (Year to Date Net Loss) of the Credit Agreement for the period ending December 31, 2002. Bank hereby waives such covenant violations for such periods. This waiver shall not act as a consent or waiver of any other transaction, act or omission, whether related or unrelated thereto, including any noncompliance with such covenant for any period other than the periods described above. This waiver shall not extend to or affect any obligation, covenant, agreement or default not expressly waived hereby.

13. Company hereby represents and warrants that, after giving effect to the amendments contained herein, (a) execution, delivery and performance of this Amendment and any other documents and instruments required under this Amendment or the Agreement are within Company's corporate powers, have been duly authorized, are not in contravention of law or the terms of Company's Certificate of Incorporation or Bylaws, and do not require the consent or approval of any governmental body, agency, or authority; and this Amendment and any other documents and instruments required under this Amendment or the Agreement, will be valid and binding in accordance with their terms; (b) the continuing representations and warranties of Company set forth in Sections 7.1 through 7.5 and 7.7 through 7.12 (after, in the case of Section 7.9, giving effect to the formation of Smtex Santa Clara, Inc. and Smtex New England, Inc.) of the Agreement are true and correct on and as of the date hereof with the same force and effect as made on and as of the date hereof; (c) the continuing representations and warranties of Company set forth in Section 7.6 of the Agreement are true and correct as of the date hereof with respect to the most recent financial statements furnished to the Bank by Company in accordance with Section 8.1 of the Agreement; and (d) no event of default, or condition or event which, with the giving of notice or the running of time, or both, would constitute an event of default under the Agreement, has occurred and is continuing as of the date hereof.

14. This Amendment shall be effective upon (i) execution of this Amendment by Company and Bank, (ii) execution of the attached Affirmation by the Guarantors, (iii) execution and delivery to Bank of the Revolving Credit Note the form of which is attached hereto as Exhibit A and (iv) payment by Company to Bank of a non-refundable amendment fee in the amount of \$15,000.

15. Except as modified hereby, all of the terms and conditions of the Agreement shall remain in full force and effect.

WITNESS the due execution hereof on the day and year first above written.

COMERICA BANK

SMTEK INTERNATIONAL, INC.

By: /s/ Beth A. Brockmann

By: /s/ Kirk A. Waldron

Its: Vice President

Its: CFO

#### AFFIRMATION

The undersigned Guarantors acknowledge the foregoing amendment and ratify and confirm their obligations under their Guaranties dated September 25, 2001 and October 18, 2001, which Guaranties remain in full force and

effect in accordance with their respective terms.

SMTEK, INC.

By: /s/ Kirk A. Waldron  
Signature of Kirk A. Waldron  
Its: Treasurer

JOLT TECHNOLOGY, INC.

By: /s/ Kirk A. Waldron  
Signature of Kirk A. Waldron  
Its: Treasurer

TECHNETICS, INC.

By: /s/ Kirk A. Waldron  
Signature of Kirk A. Waldron  
Its: Treasurer

SMTEK SANTA CLARA, INC.

By: /s/ Kirk A. Waldron  
Signature of Kirk A. Waldron  
Its: Treasurer

SMTEK NEW ENGLAND, INC.

By: /s/ Kirk A. Waldron  
Signature of Kirk A. Waldron  
Its: Treasurer

REVOLVING CREDIT NOTE

\$8,500,000            Detroit, Michigan  
February 5, 2003

On or before the Revolving Credit Maturity Date FOR VALUE RECEIVED, SMTEK International, Inc., a Delaware corporation (herein called "Company") promises to pay to the order of COMERICA BANK, a Michigan banking corporation (herein called "Bank") at its Main Office at 500 Woodward Avenue, Detroit, Michigan, in lawful money of the United States of America the indebtedness or so much of the sum of Eight Million Five Hundred Thousand Dollars (\$8,500,000) as may from time to time have been advanced and then be outstanding hereunder pursuant to the Credit Agreement dated as of September 25, 2001, made by and between Company and Bank (as the same may be amended or modified from time to time, herein called "Agreement"), together with interest thereon as hereinafter set forth.

Each of the Advances hereunder shall bear interest at the Applicable Interest Rate from time to time applicable thereto under the Agreement or as otherwise determined thereunder, and interest shall be computed, assessed and payable as set forth in the Agreement.

This Note is a note under which advances, repayments and readvances may be made from time to time, subject to the terms and conditions of the Agreement. This Note evidences borrowing under, is subject to, is secured in accordance with, and may be matured under, the terms of the Agreement, to which reference is hereby made. As additional security for this Note, Company grants Bank a lien on all property and assets including deposits and other credits of the Company, at any time in possession or control of or owing by Bank for any purpose.

Company hereby waives presentment for payment, demand, protest and notice of dishonor and nonpayment of this Note and agrees that no obligation hereunder shall be discharged by reason of any extension, indulgence or forbearance granted by any holder of this Note to any party now or hereafter liable hereon. Any transferees of, or endorser, guarantor or surety paying this Note in full shall succeed to all rights of Bank, and Bank shall be under no further responsibility for the exercise thereof, or the loan evidenced hereby. Nothing herein shall limit any right granted by Bank by other instrument or by law.

All capitalized terms used but not defined herein shall have the meanings ascribed to them in the Agreement.

This Note replaces by renewal and reduces that certain \$11,000,000 Revolving Credit Note dated May 1, 2002 made by Company payable to Bank.

SMTEK INTERNATIONAL, INC.

By: /s/ Kirk A. Waldron  
Its: CFO

Exhibit 99.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of SMTEK International, Inc. (the "Company") on Form 10-Q for the period ended December 31, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Kirk A. Waldron, Senior Vice President and Chief Financial Officer of the Company, certify, to the best of my knowledge, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities and Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Kirk A. Waldron  
KIRK A. WALDRON  
Senior Vice President,  
Chief Financial Officer  
SMTEK International, Inc.

February 7, 2003  
Date

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of SMTEK International, Inc. (the "Company") on Form 10-Q for the period ended December 31, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Edward J. Smith, Chief Executive Officer and President of the Company, certify, to the best of my knowledge, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities and Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Edward J. Smith  
EDWARD J. SMITH  
Chief Executive Officer  
President  
SMTEK International, Inc.

February 7, 2003  
Date

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