ADVO INC
Form 10-Q
May 14, 2002

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

(Mark One)

(X) Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended MARCH 30, 2002

or

( ) Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ------------------ to -----------------

Commission file number 1-11720

ADVO, INC.

(Exact name of registrant as specified in its charter)

Delaware	06-0885252
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
One Univac Lane, P.O. Box 755, Windsor, CT	06095-0755
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number including area code: (860) 285-6100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

As of April 27, 2002 there were 20,069,100 shares of common stock outstanding.

ADVO, INC.
INDEX TO QUARTERLY REPORT

ON FORM 10-Q

QUARTER ENDED MARCH 30, 2002

Part I - Financial Information

ADVO, INC.
CONSOLIDATED BALANCE SHEETS (UNAUDITED)
(In thousands, except share data)

ASSETS	March 30, 2002	September 29, 2001
Current assets:		
Cash and cash equivalents	$ 10,593	$ 17,728
Accounts receivable, net	115,053	119,388
Inventories	2,832	2,840
Prepaid expenses and other current assets	8,120	7,282
Investment in deferred compensation plan	13,379	11,493
Deferred income taxes	11,145	11,319

Total current assets	161,122	170,050
Property, plant and equipment	256,748	246,936
Less accumulated depreciation and amortization	(137,354)	(126,455)
Net property, plant and equipment	119,394	120,481
Goodwill	21,600	21,525
Other assets	13,003	10,264
TOTAL ASSETS	$ 315,119	$ 322,320
LIABILITIES		
Current liabilities:		
Current portion of long-term debt	$ 15,000	$ 11,250
Notes payable - short term	1,715	2,390
Accounts payable	30,451	37,759
Accrued compensation and benefits	23,646	21,531
Deferred compensation plan	13,379	11,493
Other current liabilities	38,095	44,678
Total current liabilities	122,286	129,101
Long-term debt	157,250	173,750
Notes payable - long term	--	1,715
Deferred income taxes	10,173	9,852
Other liabilities	5,030	4,949
STOCKHOLDERS' EQUITY		
Series A Convertible preferred stock, $.01 par value (Authorized 5,000,000 shares, none issued)	--	--
Common stock, $.01 par value (Authorized 40,000,000 shares, issued 30,464,213 and 30,317,994 shares, respectively)	305	303
Additional paid-in capital	200,785	197,222
Accumulated earnings	39,830	19,321
	240,920	216,846
Less common stock held in treasury, at cost	(217,295)	(208,620)
Accumulated other comprehensive loss	(3,245)	(5,273)
Total stockholders' equity	20,380	2,953
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	$ 315,119	$ 322,320

See Accompanying Notes.

ADVO, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(In thousands, except per share data)

	Six months ended		Three months ended	
	March 30, 2002	March 31, 2001	March 30, 2002	March 31, 2001
REVENUES	$561,369	$569,324	$274,433	$271,783
Costs and expenses:				
Cost of sales	409,217	413,346	201,786	200,346
Selling, general and administrative	107,835	105,164	53,445	50,194
Provision for bad debts	4,112	3,017	1,987	1,924
OPERATING INCOME	40,205	47,797	17,215	19,319
Interest expense	6,864	9,177	3,349	4,538
Other expense, net	787	221	493	103
Income before income taxes	32,554	38,399	13,373	14,678
Provision for income taxes	12,045	14,208	4,948	5,431
NET INCOME	$ 20,509	$ 24,191	$ 8,425	$ 9,247
BASIC EARNINGS PER SHARE	$ 1.03	$ 1.20	$ .42	$ .46
DILUTED EARNINGS PER SHARE	$ 1.01	$ 1.17	$ .42	$ .45
Weighted average basic shares	19,939	20,105	19,950	20,183
Weighted average diluted shares	20,281	20,650	20,276	20,713

See Accompanying Notes.

ADVO, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In thousands)

	Six months ended March 30, 2002	Six months ended March 31, 2001
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 28,633	$ 13,313
Cash flows from investing activities:		
Acquisition of property, plant and equipment	(13,370)	(16,537)
Proceeds from disposals of property, plant and equipment	301	94
Distributions from equity affiliates	44	--
Acquisitions/joint ventures, net of cash acquired	(450)	(9,255)
NET CASH USED BY INVESTING ACTIVITIES	(13,475)	(25,698)
Cash flows from financing activities:		
Revolving line of credit - net	(9,000)	6,000
Payments on long-term debt	(3,750)	--
(Decrease) increase in note payable - net	(2,391)	4,030
Proceeds from exercise of stock options	1,522	4,523
Purchase of common stock for treasury	(8,674)	(3,976)
NET CASH (USED) PROVIDED BY FINANCING ACTIVITIES	(22,293)	10,577
Decrease in cash and cash equivalents	(7,135)	(1,808)
Cash and cash equivalents at beginning of period	17,728	6,003
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 10,593	$ 4,195
Noncash activities:		
Change in fair value of interest rate swap liabilities	2,028	(3,129)
Change in noncash portion of deferred compensation plan	1,967	(1,197)

See Accompanying Notes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included.

Operating results for the six month period ended March 30, 2002 are not necessarily indicative of the results that may be expected for the fiscal year ending September 28, 2002. For further information, refer to the consolidated financial statements and footnotes thereto included in ADVO's annual report on Form 10-K for the fiscal year ended September 29, 2001. Certain reclassifications have been made in the fiscal 2001 financial statements to conform with the fiscal 2002 presentation.

2. SUMMARY OF ACCOUNTING POLICIES

Long-lived assets

In August 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("Statement") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", which addresses financial accounting and reporting for the impairment or disposal of long-lived assets and for the disposal of a segment of a business. The Company expects to adopt Statement No. 144 in fiscal 2003 and does not expect such adoption to have a material effect on the Company's financial position or results of operations.

3. GOODWILL AND OTHER INTANGIBLE ASSETS

Effective October 1, 2001, the Company adopted Statement No. 142, "Goodwill and Other Intangible Assets". Under Statement No. 142, goodwill and intangible assets that have indefinite useful lives are no longer subject to amortization. Accordingly, the Company ceased amortization of all goodwill upon adoption. Intangible assets that have a finite life continue to be amortized over their useful lives.

Statement No. 142 also requires that goodwill be tested for impairment at least annually. Impairment exists when the carrying amount of goodwill exceeds its fair market value. The Company performed the impairment tests upon the adoption of Statement No. 142 on October 1, 2001. Fair value was determined using the discounted cash flow methodology. The Company has determined that no impairment of goodwill exists.

The following table reflects actual results of operations for the six month and three month periods ended March 30, 2002 and pro-forma results of operations for the six month and three month periods ended March 31, 2001 had the Company applied the non-amortization provisions of Statement No. 142 in those periods:

ADVO, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(In thousands, except per share data)	Six months ended March 30, 2002	Six months ended March 31, 2001	Three months ended March 30, 2002	Three months ended March 31, 2001
Reported net income	$ 20,509	$ 24,191	$ 8,425	$ 9,247
Add: Goodwill amortization, net of tax	--	439	--	234
Adjusted net income	$ 20,509	$ 24,630	$ 8,425	$ 9,481
Reported basic earnings per share	$ 1.03	$ 1.20	$ .42	$ .46
Add: Goodwill amortization, net of tax	--	.02	--	.01
Adjusted basic earnings per share	$ 1.03	$ 1.22	$ .42	$ .47
Reported diluted earnings per share	$ 1.01	$ 1.17	$ .42	$ .45
Add: Goodwill amortization, net of tax	--	.02	--	.01
Adjusted diluted earnings per share	$ 1.01	$ 1.19	$ .42	$ .46

Intangible assets that continue to be subject to amortization are included in other assets and consist primarily of customer based intangibles with a gross carrying value of $4.0 million and accumulated amortization of $3.4 million at March 30, 2002.

Amortization expense for the quarter and six months ended March 30, 2002 was $0.1 million and $0.2 million, respectively. Amortization expense is estimated to be $0.2 million for the remainder of fiscal 2002, $0.3 million for fiscal 2003. Subsequent to fiscal 2003, all intangible assets are expected to be fully amortized.

4. COMPREHENSIVE INCOME

Comprehensive income for a period encompasses net income and all other changes in a company's equity other than from transactions with the company's owners. The Company's comprehensive income was as follows:

(In thousands)	Six months ended March 30, 2002	Six months ended March 31, 2001	Three months ended March 30, 2002	Three months ended March 31, 2001
Net income	$ 20,509	$ 24,191	$ 8,425	$ 9,247

Other comprehensive income (loss):				
Unrealized gain (loss) on derivative instruments	2,028	(3,129)	1,362	(1,552)
Total comprehensive income	$ 22,537	$ 21,062	$ 9,787	$ 7,695

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ADVO, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

5. EARNINGS PER SHARE

Basic earnings per share excludes the effect of common stock equivalents, such as stock options, and is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution that could occur if common stock equivalents, such as stock options, were exercised.

	Six months ended		Three months ended	
	March 30, 2002	March 31, 2001	March 30, 2002	March 31, 2001
(In thousands, except per share data)				
Net income	$20,509	$24,191	$ 8,425	$ 9,247
Weighted average basic shares	19,939	20,105	19,950	20,183
Effect of dilutive securities:				
Stock options	310	508	305	494
Restricted stock	32	37	21	36
Dilutive potential common shares	342	545	326	530
Weighted average diluted shares	20,281	20,650	20,276	20,713
Basic earnings per share	$ 1.03	$ 1.20	$ .42	$ .46
Diluted earnings per share	$ 1.01	$ 1.17	$ .42	$ .45

ADVO, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This section should be read in conjunction with the consolidated financial statements of the Company and the notes thereto.

RESULTS OF OPERATIONS

REVENUES Revenues for the second quarter of fiscal 2002 were $274.4 million, representing a 1.0% increase over the second quarter of fiscal 2001. Contributing to this result were increases in the Company's core shared mail business, notably the continued extension of newspaper partnerships and second-in-home dates, and incremental revenues of $1.8 million associated with the acquisition of the New Jersey Shoppers Guide ("NJ Shopper") in the third quarter of the previous fiscal year. The increase in shared mail revenue was primarily due to pricing gains, in part as a result of the postal rate increases effective in the prior year, partially offset by shifts in product mix and weights.

For the year-to-date period ended March 30, 2002, the Company's revenues were $561.4 million reflecting a 1.4% decrease from the prior year period. This decrease was primarily driven by volume declines which took place in the first quarter of fiscal 2002, and to a lesser degree, shifts in product mix and weights. Partially offsetting these year-to-date declines were pricing gains, due in part to the postal rate increases in the prior year. Also offsetting the revenue decline for the first six months of fiscal 2002 was a 7.3% year over year revenue increase in the Company's A.N.N.E. (ADVO National Network Extension) brokered distribution program and $3.9 million of incremental revenues associated with the Company's acquisition of the NJ Shopper in the third quarter of fiscal 2001.

Revenue per thousand pieces remained relatively constant for the three months ended March 30, 2002 at $38.53 versus $38.66 for the same period in fiscal 2001. Revenue per thousand pieces was $39.48 for the six months ended March 30, 2002, representing a 0.4% increase over the comparable period in the prior year. Average pieces per package were 7.63 for the second quarter and 7.84 for the six months ended March 30, 2002, decreasing 3.4% and 4.6%, respectively, from the prior year due to the dilutive effect of the second in-home date mailings. Conversely, these mailings contributed to the increase in shared mail packages delivered to 856.3 million packages and 1,655.9 million packages for the three and six months ended March 30, 2002, representing a 5.9% and 3.6% increase, respectively, over the prior year period. Also, total shared mail pieces distributed increased 2.3% and decreased 1.2% for the second quarter and first half of fiscal 2002, respectively, compared to the same periods in fiscal 2001.

OPERATING EXPENSES Cost of sales as a percentage of revenue was 73.5% for the second quarter of fiscal 2002 decreasing 0.2 percentage points when compared to the same period in the prior year. The decrease was primarily the result of continued improvements and efficiencies in the branch operations of the Company and lower print costs. In absolute terms, cost of sales increased $1.4 million for the three months ended March 30, 2002 when compared to the same period in the prior year. The increase was due to higher distribution costs partially offset by lower print and paper costs and branch efficiencies. Distribution costs, consisting primarily of postage costs, increased for the second quarter of fiscal 2002. This net increase was the result of the postal rate increase in the prior fiscal year and higher postage costs resulting from the 5.9% increase in shared mail packages delivered in the second quarter of fiscal 2002.

Cost of sales as a percentage of revenue for the first half of fiscal 2002 increased 0.3 percentage points to 72.9% when compared to the first half of fiscal 2001. This increase primarily resulted from underweight postage costs incurred as a result of the decline in average pieces per package due to the expected dilutive effect of the second in-home date initiatives. In absolute terms, cost of sales decreased $4.1 million for the first six months of fiscal 2002 versus 2001. The decrease was caused primarily by lower print costs due to volume declines and lower paper prices. Also contributing to the decrease were lower production costs, particularly temporary labor cost reductions associated with the year over year 1.2% decrease in shared mail pieces processed and improved branch efficiencies. Offsetting these decreases in cost of sales were higher postage costs resulting from the postal rate increase in the prior year and the 3.6% increase in shared mail packages distributed during the first half of fiscal 2002.

For the three and six month periods ended March 30, 2002, selling, general and administrative costs, including the provision for bad debts, increased $3.3 million and $3.8 million, respectively, when compared to the same periods in the prior year. As a percentage of revenue, these costs increased 1.0 and 0.9 percentage points for the three and six months ended March 30, 2002 versus the comparable periods in fiscal 2001. The increase in selling, general and administrative costs for the second quarter and year-to-date periods was due to incremental security costs incurred when the Company established at the beginning of the fiscal year an executive level Office of Safety and Security designed to ensure the safety of the Company's operations for its associates, clients and consumers. The increase in selling, general and administrative costs was also affected by lower incentive wages in the prior year versus the current year. Also impacting year-to-date selling, general and administrative expenses were the organizational realignment costs incurred during the first quarter of fiscal 2002. These increases were offset by reductions in spending due to strict fixed cost controls implemented throughout the organization.

OPERATING INCOME The Company reported operating income of $17.2 million for the second quarter of fiscal 2002 compared to $19.3 million for the second quarter of fiscal 2001. For the first half of fiscal 2002, operating income was $40.2 million versus $47.8 million for the same period in the prior year.

INTEREST EXPENSE Interest expense decreased $1.2 million and $2.3 million for the three and six month periods ended March 30, 2002, respectively. The decreases were due to lower market rates of interest and a decrease in the average outstanding debt balance.

INCOME TAXES The effective income tax rate was 37% for both the three and six months ended March 30, 2002 and March 31, 2001.

EARNINGS PER SHARE Diluted earnings per share was $0.42 for the second quarter of fiscal 2002 versus $0.45 for the same period of the prior year. On a year-to-date basis, diluted earnings per share was $1.01 for the current period versus $1.17 in the comparable prior year period.

FINANCIAL CONDITION

Working capital decreased $2.1 million from September 29, 2001 to March 30, 2002. The change in working capital was the result of decreases in current assets and current liabilities of $8.9 million and $6.8 million, respectively.

The change in current assets was due in part to a decrease in cash and cash equivalents as a result of scheduled debt repayments, treasury stock purchases made under the Company's buyback program and the timing of vendor payments. A decrease in accounts receivable, due to improved collections, also contributed to the decrease in current assets.

The decrease in current liabilities was attributed to the following: decreases in accounts payable due to the timing of vendor payments, decreases in other current liabilities relating to the timing of customer advance payments and the change in the fair value of interest rate swap liabilities. Offsetting these decreases were increases in taxes payable associated with the timing of payments, increases in accrued compensation and benefits due to higher incentive compensation and increases in the current portion of long term debt due to scheduled debt payments.

Stockholders' equity of $20.4 million at March 30, 2002 reflects an increase of $17.4 million from September 29, 2001. The increase was primarily attributable to net income of $20.5 million. Other increases in equity were derived from employee related stock activity of $3.6 million and a $2.0 million reduction in the fair value of derivative instruments. These increases were offset by treasury stock purchases of $8.7 million. The treasury stock purchases consisted of $7.3 million made on the open market associated with the Company's buyback program and $1.4 million pursuant to elections by employees to satisfy withholding requirements under the Company's restricted stock and stock option plans.

PROPERTY, PLANT AND EQUIPMENT

Investments in property, plant and equipment for the six month period ended March 30, 2002 were $13.4 million. Software development for the order management, order fulfillment and targeting solutions systems, as well as, upgrades to the human resource/payroll systems, deployment of computer hardware and renovations at certain of the Company's facilities account for the majority of the capital expenditures. The Company expects its capital expenditures for the entire year to be approximately $35.0 million.

LIQUIDITY

The Company's main source of liquidity continues to be funds generated from operating activities. In addition, the Company has available unused credit commitments of $116.5 million that may be used to fund operating activities.

The net cash provided by operating activities was $28.6 million for the six months ended March 30, 2002 versus $13.3 million for the six months ended March 31, 2001. The year over year increase resulted primarily from the change in accounts receivable due to improved collections and the change in accrued compensation and benefits as a result of the incentive payment which was made in fiscal 2001 for which no comparable payment was made in the current fiscal year.

Cash and cash equivalents for the first six months of fiscal 2002 decreased $7.1 million to $10.6 million. The decrease was comprised of net cash used for investing and financing activities of $13.5 million and $22.3 million, respectively, offset partially by net cash provided by operating activities of $28.6 million.

Investing activities made during the first half of fiscal 2002 primarily consisted of $13.4 million for the capital expenditures detailed above. Investing activities for the first half of the prior fiscal year included $16.5 million of capital expenditures and $9.3 million for acquisitions and joint ventures, most notably for the $8.3 million acquisition of MMSI, net of cash acquired, and including subsequent contingent consideration paid in the second quarter of fiscal 2001.

Net cash used for financing activities was $22.3 million for the year-to-date period ended March 30, 2002 versus net cash provided by financing activities of $10.6 million in the same prior year period. In the current year, financing activities consisted of debt payments of $12.8 million which included net payments on the revolver and scheduled principal payments on the term loan, payment of a $2.4 million note resulting from the acquisition of MMSI in the prior year, and $8.7 million of treasury stock purchases offset by $1.5 million of proceeds from stock option exercises. In the prior year, financing activities included net borrowings of $6.0 million, a $4.0 million note payable related to the acquisition of MMSI and $4.5 million of proceeds from stock option exercises offset by treasury stock purchases of $4.0 million.

Contractual and commercial commitments

The Company's contractual obligations are as follows.

(In millions)	Long term debt	Operating leases

Less than one year	$ 15.0	$ 13.2
One to three years	157.3	26.3
Four to five years	--	11.3
After five years	--	16.2
Total	$172.3	$ 67.0

The Company's long-term debt obligations are discussed below in the "Financing Arrangements" section. The Company leases property in its normal business operations under noncancellable operating leases. Certain of these leases contain renewal options and certain leases also provide for cost escalation payments.

The Company has various agreements with International Business Machines Corporation ("IBM") Global Services to provide systems development, technical support, a customer support center and server farm management services to the Company. The noncancellable portions of these contracts have lapsed allowing the Company to cancel these contracts subject to termination charges ranging from $9.6 million in fiscal 2002 to $1.7 million in fiscal 2006 depending on the year in which the cancellation becomes effective.

The Company has outstanding letters of credit of approximately $7.5 million under separate agreements expiring in April 2003 primarily relating to its worker's compensation program.

The Company anticipates it will be able to meet its commitments detailed above through funds generated from operations or from unused credit under its revolving line of credit.

FINANCING ARRANGEMENTS

The Company maintains a credit agreement which provides for total credit facilities of $300 million, consisting of a $135 million term loan and a $165 million revolving line of credit. At March 30, 2002, there was $172.3 million of debt outstanding, with $15.0 million classified as current due to scheduled principal payments. The Company anticipates it will be able to meet its debt obligations through funds generated from operations. During April 2002, the Company borrowed an additional $15.0 million under the revolving line of credit.

Under the terms of the credit agreement, the Company is required to maintain certain financial ratios. In addition, the credit agreement also places restrictions on disposals of assets, mergers and acquisitions, dividend payments, investments and additional debt.

NEW ACCOUNTING PRONOUNCEMENTS

Effective October 1, 2001, the Company adopted Statement of Financial Accounting Standards ("Statement") No. 142, "Goodwill and Other Intangible Assets". Under Statement No. 142, goodwill and intangible assets that have indefinite useful lives are no longer subject to amortization. Accordingly, the Company ceased amortization of all goodwill upon adoption. Additionally, intangible assets that have a finite life continue to be amortized over their useful lives. Operating income was $17.2 million and $19.3 million for the second quarter of fiscal 2002 and 2001, respectively, and $40.2 million and $47.8 million for the first six months of fiscal 2002 and 2001, respectively. Had the Company applied the non-amortization provisions of Statement No. 142 in fiscal 2001, operating income would have been $19.7 million and $48.5 million for the three and six months ended March 31, 2001. See the discussion in Note 3 of the "Notes to Consolidated Financial Statements" of this report for a further discussion of the impact of Statement No. 142 to the Company.

Statement No. 142 also requires that goodwill be tested for impairment at least annually. Impairment exists when the carrying amount of goodwill exceeds its fair market value. The Company performed the impairment tests upon the adoption of Statement No. 142 on October 1, 2001. Fair value was determined using the discounted cash flow methodology. The Company has determined that no impairment of goodwill exists. Additional evaluations of goodwill may be performed in future periods should any circumstances arise that would indicate that the carrying value of goodwill might be impaired. Impairment adjustments recognized after adoption, if any, are required to be recognized as operating expenses.

CRITICAL ACCOUNTING POLICIES

The SEC issued financial reporting release FR-60, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies". Critical accounting polices are defined as those that are most important to the portrayal of a company's financial condition and results and which require complex or subjective judgements or estimates. The preparation of financial statements in conformity with general accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates under different assumptions and conditions. The Company had determined its critical accounting polices to include the allowance for doubtful accounts and the valuation of goodwill and intangible assets.

Allowance for doubtful accounts

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The Company reviews the collectibility of its receivables on an ongoing basis taking into account a combination of factors. On a monthly basis, the Company conducts meetings to identify and review potential problems, such as a bankruptcy filing or deterioration in the customer's financial condition to ensure the Company is adequately accrued for potential loss. The Company also calculates a trended write-off of bad debts over a rolling twelve-month period and takes into account aging category and historical trends. If a customer's situation changes, such as bankruptcy or creditworthiness, or there is a change in the current economic climate, the Company may modify its estimate of the allowance for doubtful accounts.

Valuation of goodwill and intangible assets

Goodwill represents the excess purchase price over fair value of net assets acquired in connection with purchase business combinations. With the adoption of Statement No. 142, the Company ceased amortization of goodwill, but is now subject to an annual impairment test as discussed under "New Accounting Pronouncements". The Company's goodwill impairment test was performed by comparing the net present value of projected cash flows to the carrying value of goodwill. The Company utilized discount rates determined by management to be similar with the level of risk in the current business model. The Company has determined that no impairment of goodwill exists. If the assumptions the Company made regarding estimated cash flows, such as future operating performance and other factors to determine the fair value, is less favorable than expected, the Company may be required to record an impairment charge.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's interest expense is sensitive to changes in interest rates. In this regard, changes in interest rates affect the interest paid on its debt. To mitigate the impact of interest rate fluctuations, the Company has historically maintained interest rate swap agreements on notional amounts totaling $100 million which is currently over 50% of its outstanding debt balance.

The Company believes that the interest rate swap agreements limit substantial risk if interest rates should fluctuate. If interest rates should change by 2 percentage points for the remainder of the 2002 fiscal year from those rates in effect at March 30, 2002, assuming no change in the outstanding debt balance and considering the effects of the Company's interest rate swap agreements, interest expense would increase/decrease by approximately $1.2 million.

FORWARD LOOKING STATEMENTS

Except for the historical information stated herein, the matters discussed in this Management's Discussion and Analysis of Financial Condition and Results of Operations contain forward looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Such forward looking statements are based on current information and expectations and are subject to risks and uncertainties which could cause the Company's actual results to differ materially from those in the forward looking statements. Such risks and uncertainties include but are not limited to: changes in customer demand and pricing; the possibility of consolidation throughout the retail sector; the impact of economic and political conditions on retail advertising spending and our distribution system; postal and paper prices; possible governmental regulation or legislation affecting aspects of the Company's business; the efficiencies achieved with technology upgrades and other general economic factors.

PART II - OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibit Index

Exhibit No. Exhibits

(b) Reports on Form 8-K

No report on Form 8-K was filed by the Company with respect to the quarter ended March 30, 2002.

Omitted from this Part II are items which are inapplicable or to which the answer is negative for the period covered.

SIGNATURES

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

ADVO, Inc.

Date: May 14, 2002

By: /s/ JOHN SPERIDAKOS

John Speridakos
Vice President and Controller
(Principal Accounting Officer)