SOUTHWALL TECHNOLOGIES INC /DE/
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Registration No. 333-85576

Prospectus

3,500,000 Shares

Common Stock

We are offering 3,500,000 shares of our common stock. Our common stock is listed on the Nasdaq National Market under the symbol "SWTX." On July 1, 2002, the last reported sale price of our common stock on the Nasdaq National Market was $4.76 per share.

Investing in our common stock involves certain risks. See "Risk Factors" beginning on page 7.

	Per Share	Total
Public Offering Price	$ 4.50	$ 15,750,000
Underwriting Discount	$ 0.27	$ 945,000
Proceeds, before expenses, to Southwall	$ 4.23	$ 14,805,000

We have granted the underwriters the right to purchase up to an additional 507,300 shares and the selling stockholders have granted the underwriters the right to purchase up to an additional 17,700 shares of our common stock to cover over-allotments.

The Securities and Exchange Commission and state securities regulators have not approved or disapproved of these securities or determined if this prospectus is truthful or complete. It is illegal for any person to tell you otherwise.

Needham & Company, Inc.

Adams, Harkness & Hill, Inc.

Wells Fargo Securities, LLC

The date of this prospectus is July 1, 2002.

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We have not authorized anyone to provide you with information different than that contained in this document. This document may only be used where it is legal to sell these securities. The information in this document is given as of the date of this document regardless of the time of delivery of this prospectus or of any sale of our common stock.

PROSPECTUS SUMMARY

This summary highlights information contained elsewhere in this prospectus. This summary does not contain all of the information that you should consider before investing in our common stock. References in this prospectus to "Southwall Technologies," "Southwall," "we," "us," or "our" are to Southwall Technologies Inc. and its subsidiaries. You should read this entire prospectus carefully. Unless otherwise indicated, all information in this prospectus assumes that the underwriters have not exercised their option to purchase additional shares.

Southwall Technologies Inc.

We are a global developer, manufacturer and marketer of thin film coatings for the automotive glass, electronic display and architectural markets. We have developed a variety of products that selectively absorb, reflect or transmit light and control the flow of energy. Our products consist of transparent insulation and solar-control films for automotive and architectural glass, and anti-reflective films for computer and television screens, including flat panel and plasma displays. They also include transparent conductive films for use in touch screen and liquid crystal displays. Based upon our production capacity, we believe we are one of the world's largest producers of rolls of clear plastic, or substrates, coated with thin films.

Recent advances in manufacturing processes and techniques are reducing our production costs. These reductions allow our thin film coated substrates to more cost-effectively address the following markets:

Automotive glass. The thin film coated substrates we sell in this market reflect infrared heat and reduce the transmission of ultra-violet light. These coatings allow carmakers to use more glass and to increase the energy efficiency and comfort of their vehicles. We sell thin film coated substrates in this market primarily to original equipment manufacturers that produce glass for sale to European manufacturers of new cars. Our products are used in cars manufactured by Mercedes Benz, Renault, Audi, BMW, Volvo, Volkswagen and the PSA Group, among other companies. According to the Freedonia Group, the worldwide demand for new and replacement glass sold for the motor vehicle market is expected to increase from approximately 7.2 billion square feet in 1999 to approximately 8.7 billion square feet in 2009.

Electronic displays. The thin film coated substrates we sell in this market primarily reduce glare caused by reflection from glass surfaces, improve contrast and image quality, and reduce energy emission from and the build up of static charge on computer display screens. Our thin film coated substrates are used in computer display tubes, or CDTs, liquid crystal and plasma displays, and in applications such as touch screens, wireless telephones and automated teller machines. The combined worldwide market for 17 inch and 19 inch flat screen computer display tubes and active matrix liquid crystal displays used for computer and handheld applications is anticipated to grow from approximately 75 million units in 2000 to approximately 155 million units in 2005, according to a 2001 Stanford Resources, Inc. research study.

Architectural. The thin film coated substrates we sell in this market are primarily used to control the transmission of heat through window glass and to limit ultra-violet light damage. Glass windows are significantly responsible for heat build-up and loss in buildings. According to the Freedonia Group, the worldwide market for new and replacement glass sold for use in residential buildings is expected to increase from approximately 5.2 billion square feet in 1999 to approximately 8.0 billion square feet in 2009. Also according to Freedonia, the market for new and replacement glass for use in commercial buildings is expected to increase from approximately 16.2 billion square feet in 1999 to approximately 25.4 billion square feet in 2009.

To address market demands, we have expanded our operations. We began manufacturing in a new facility in Dresden, Germany in January 2001. The facility presently contains two production machines. We expect that our third production machine in Dresden will begin commercial production by the first quarter of 2003. In 2000, we also increased our commercial production capacity in Tempe, Arizona by adding a second production machine.

Our Competitive Advantages

We believe we are well positioned for continued growth in sales of thin film coatings for the automotive glass, electronic display and architectural markets, and that our competitive advantages include:

- Proprietary thin film manufacturing process knowledge and control systems;
- Extensive thin film materials expertise and optical design capabilities;
- Over twenty years' experience providing large quantities of sophisticated coatings on flexible film for demanding applications and customers;
- The world's largest installed base of coating machinery for application of sputter coatings to flexible film; and
- Substantial expertise and technical support in the areas of product testing, reliability and applications.

Our Strategy

Our objective is to enhance our position as a global developer, manufacturer and marketer of thin film coatings on flexible substrates for the automotive glass, electronic display and architectural markets. The following are key elements of our strategy:

- Increase penetration and expand customer base in the automotive glass market;
- Increase production capacity in the automotive glass and architectural market;
- Use expanded production capacity and new products to increase sales in the architectural markets;

Capitalize on expanding flat panel display markets; and

Continue to advance thin film production technology.

We were incorporated in 1979 as a Delaware corporation. Our principal executive offices are located at 1029 Corporation Way, Palo Alto, California 94303, and our telephone number is (650) 962-9111. Our corporate web site is located at *www.southwall.com.* The information contained in our web site is not a part of this prospectus.

Recent Development

On June 24, 2002, we disclosed preliminary estimates of our financial results for the quarter ended June 30, 2002, indicating that we expected revenues for the quarter to be between $19.5 million and $20.5 million and net income for the quarter to be between $1.2 million and $1.4 million. We also disclosed preliminary estimates of our financial results for the fiscal year ended December 31, 2002, indicating that we expected revenues for 2002 to be between $78.0 million and $82.0 million and net income for 2002 to be between $4.8 million and $5.2 million before including any adjustments from the sale of common stock that we are offering by means of this propectus. These estimates are, however, subject to certain assumptions, risks and uncertainties that could cause actual revenues or net income for our second quarter or 2002 to be different than the estimates presented.

We expect the remainder of 2002 to continue to be affected by a slowdown in sales by European automobile manufacturers. We do not anticipate a significant improvement, if any, over our first quarter sales to the automotive market for any of the remaining quarters of 2002. However, we recently announced a new ten-year distribution agreement with Globamatrix Holdings Pte. Ltd., or Globamatrix, which includes commitments by Globamatrix to purchase an annually increasing amount, subject to volume and quality standards, of our solar control products for retrofit applications to the automotive and residential and commercial architectural glass markets. As a result, we believe that we will have somewhat greater revenues from Globamatrix in 2002 than in 2001, and that this growth will continue through 2003.

Our revenues from the CDT portion of our electronic display business have declined during 2002 as compared to 2001 primarily due to lower prices. During the same period, however, sales to the liquid crystal and plasma display portions of this market have increased. We recently started shipping production quantities and sizes of new films specifically designed for the liquid crystal display and plasma display panel markets that maintain optical clarity while reducing the reflection of ambient light to improve image quality. We expect the decline of the CDT portion of our electronic display business and the growth in sales of our new electronic display films to continue through 2003.

Due to production capacity constraints, in the past we have not allocated resources to expanding revenues from our architectural products. Additional production capacity for architectural products has recently been created, in part, by the addition of our new Dresden facility. Our revenues from our architectural business have increased during 2002 as compared to 2001, and we expect that the availability of production capacity in 2003 will allow for continued growth in this business. However, we can give no assurances that availability of production capacity will increase our revenues from architectural products.

The Offering

Common stock offered by us	3,500,000 shares
Common stock to be outstanding after this offering	12,086,278 shares
Over-allotment option:	
Common stock offered by us	507,300 shares
Common stock offered by selling stockholders	17,700 shares
Use of proceeds	To pay down existing indebtedness, capital expenditures including purchasing a new production machine, replacing our enterprise resource planning system and updating our Palo Alto and Tempe facilities, and for working capital and general corporate purposes, including possible acquisitions.

Nasdaq National Market symbol	SWTX

The number of shares of our common stock to be outstanding after this offering is based on our shares outstanding as of May 23, 2002 and excludes 2,096,204 shares which consist of:

1,401,859 shares subject to outstanding options under our 1997 stock incentive plan with a weighted average exercise price of $5.24 per share; and

694,345 shares subject to outstanding options under our 1998 stock option plan for employees and consultants with a weighted average exercise price of $6.61 per share.

Summary Consolidated Financial Data

The following tables summarize consolidated statements of operations and consolidated balance sheet data for our business. You should read this information together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes included elsewhere in this prospectus. The pro forma as adjusted consolidated balance sheet data reflects the sale of 3,500,000 shares of common stock offered by us at the public offering price of $4.50, after deducting estimated underwriting discounts and commissions and estimated offering expenses.

The consolidated statements of operations data for the five years ended December 31, 2001 are derived from our audited consolidated financial statements. The consolidated statements of operations data for the three months ended April 1, 2001 and March 31, 2002 and the consolidated balance sheet data as of March 31, 2002 have not been audited. In the opinion of management, such unaudited financial statements have been prepared on the same basis as the audited financial statements referred to above and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of results of operations for the indicated periods when read in conjunction with our audited financial statements and notes. Results of operations for the three months ended March 31, 2002 are not necessarily indicative of the results that may be expected for the full year.

	Year Ended December 31,					Three Months Ended	
	1997	1998	1999	2000	2001	April 1, 2001	March 31, 2002
	(In thousands, except per share data)						
Consolidated Statements of Operations Data:							
Net revenues by product:							
Automotive glass	$ 6,629	$ 12,845	$ 19,477	$ 20,198	$ 37,385	$ 8,007	$ 7,003
Electronic display	21,957	16,954	16,014	47,734	29,691	6,724	7,925
Architectural	21,503	20,234	19,107	17,416	15,900	2,982	4,341
Net revenues	50,089	50,033	54,598	85,348	82,976	17,713	19,269
Gross profit	14,779	5,780	13,892	16,288	22,828	2,864	6,844
Income (loss) from operations	2,446	(7,130)	(527)	(3,594)	6,336	(1,217)	1,322
Net income (loss)	$ 2,281	$ (7,869)	$ (1,865)	$ (6,180)	$ 4,635	$ (1,131)	$ 1,181
Net income (loss) per share:							
Basic	$ 0.32	$ (1.03)	$ (0.25)	$ (0.81)	$ 0.58	$ (0.15)	$ 0.14
Diluted	$ 0.29	$ (1.03)	$ (0.25)	$ (0.81)	$ 0.57	$ (0.15)	$ 0.13
Weighted average number of common stock and dilutive common stock equivalents:							
Basic	7,107	7,608	7,421	7,642	8,032	7,743	8,417
Diluted	7,799	7,608	7,421	7,642	8,186	7,743	9,277

	March 31, 2002	
	Actual	Pro Forma As Adjusted
	(In thousands)	
Consolidated Balance Sheet Data:		
Cash and cash equivalents	$ 2,713	$ 3,001
Working capital (deficit)	(4,987)	(93)
Property, plant and equipment, net	47,326	53,326
Total assets	73,067	78,605
Term debt	13,800	9,800
Total liabilities	44,781	36,175
Total stockholders' equity	28,286	42,430

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RISK FACTORS

An investment in our common stock involves a high degree of risk. You should consider carefully the following risks, together with all other information included in this prospectus, before you decide to buy our common stock. If any of the following risks actually occur, our business, prospects, financial condition or results of operations would likely suffer materially. As a result, the trading price of our common stock may decline, and you could lose all or part of the money you paid to buy our common stock.

Financial Risks

Our negative working capital position, leverage and historical performance may prevent us from obtaining additional loans.

We have a working capital deficit, significant debt and substantial ongoing debt service obligations. These and other factors related to our business during recent years, including the restatement in 2000 of our financial statements for prior periods, operating losses in 1998, 1999 and 2000, our failure to comply with covenants in our financing agreements and suspension of trading of our common stock on Nasdaq in 2000, may make it difficult for us to secure additional borrowings on favorable terms or at all. We intend to seek additional borrowings, and difficulties in borrowing money could have a material adverse effect on our operations, planned capital expenditures, ability to comply with the terms of government grants and future growth.

Covenants or defaults under our credit agreements may prevent us from borrowing or force us to curtail our operations.

As of March 31, 2002, we had total outstanding obligations under our credit agreements of $21.6 million. Following the application of the proceeds from this offering, approximately $23.1 million of our assets will remain as collateral to secure loans under our credit facilities. Our inability to make timely payments of interest or principal under these facilities could materially adversely affect our ability to borrow money under existing credit facilities, to secure additional borrowings or to function as a going concern. Our current credit facilities contain financial covenants that will require us to meet certain financial performance targets and operating covenants that limit our discretion with respect to business matters. Among other things, these covenants restrict our ability to borrow additional money, create liens or other encumbrances, and make certain payments including dividends and capital expenditures. Many of these loans contain provisions that permit the lender to declare the loans immediately due if there is a material adverse change in our business. These credit facilities also contain events of default that could require us to pay off indebtedness before its maturity. The restrictions imposed by these credit facilities or the failure of lenders to advance funds under these facilities could force us to curtail our operations or have a material adverse effect on our liquidity.

Our ability to borrow is limited by the nature of our equipment and some of our accounts receivable.

Our equipment is custom designed for a special purpose. In addition, a large portion of our accounts receivable are from foreign sales, which are often more difficult to collect than domestic accounts receivable. As a result of the nature of our equipment and accounts receivable, lenders will generally allow us to borrow less against these items as collateral than they would for other types of equipment or domestic accounts receivable.

If we default under our secured credit facilities and financing arrangements, the lenders could foreclose on the assets we have pledged to them requiring us to significantly curtail or even cease our operations.

In connection with our current borrowing facilities and financing arrangements, we have granted security interests in and liens on substantially all of our assets, including our production machines and our Dresden facility, to secure the loans. We are currently being sued under a master sale-leaseback agreement with respect to two of our production machines because we have withheld lease payments in

connection with a dispute with the leasing company. The leasing company holds a security interest in the production machines and may be able to repossess those machines. If the leasing company were to repossess one or more of those machines, our ability to produce product would be materially impaired. Our revenues, gross margins and operating efficiency would also be materially adversely affected. Our obligations under our secured credit facilities contain cross-default and cross-acceleration provisions and provisions that allow the lenders to declare the loans immediately due if there is a material adverse change in our business. If we default under the credit facilities or financing arrangements the lenders could declare all of the funds borrowed thereunder, together with all accrued interest, immediately due and payable. If we are unable to repay such indebtedness, the lenders could foreclose on the pledged assets. If the lenders foreclose on our assets, we would be forced to significantly curtail or even cease our operations.

Our first quarter revenues are generally lower than revenues in the following quarters due to seasonal demand for our products.

Our revenue from the electronic display and architectural markets are affected by seasonality patterns with the highest sales occurring during the second, third and fourth fiscal quarters. During the past three fiscal years, 21% of our sales have occurred during the first quarter with 25%, 29% and 25% occurring during the second, third and fourth quarters, respectively. Demand in the electronic display market is generally at its highest before the holiday season, in our second and third quarters, when production of electronic goods is at its highest. Demand for architectural glass generally increases when the weather is warmer in northern climates and construction activity increases. To a lesser extent, demand for our after-market automotive glass products generally increases when weather is warmer in northern climates and the replacement of glass windows in motor vehicles increases. Lower demand for our products during the first quarter generally results in lower sales, margins and operating results during that quarter. We believe this seasonality in the demand for our products will continue to affect our results in the future.

Our quarterly revenue and operating results are volatile and difficult to predict. If we fail to meet the expectations of public market analysts or investors, the market price of our common stock may decrease significantly.

Our quarterly revenue and operating results have varied significantly in the past and will likely vary significantly in the future. Our revenue and operating results may fall below the expectations of securities analysts or investors in future periods. Our failure to meet these expectations would likely adversely affect the market price of our common stock.

Our quarterly revenue and operating results may vary depending on a number of factors, including:

- fluctuating customer demand, which is influenced by a number of factors, including market acceptance of our products and the products of our customers and end-users, changes in product mix, and the timing, cancellation or delay of customer orders and shipments;
- the timing of shipments of our products by us and by independent subcontractors to our customers;
- manufacturing and operational difficulties that may arise due to, among other things, quality control, capacity utilization of our production machines, unscheduled equipment maintenance, and the hiring and training of additional staff;
- our ability to introduce new products on a timely basis; and
- competition, including the introduction or announcement of new products by competitors, the adoption of competitive technologies by our customers, the addition of new production capacity by competitors and competitive pressures on prices of our products and those of our customers.

We expect to be subject to increased foreign currency risk in our international operations.

In 2002, we expect that 10% to 15% of our revenues will be denominated in euros, primarily related to sales from our Dresden operation, including sales to one of our largest customers, a European automotive glass manufacturer. As a result, our operating results and cash flows may vary due to fluctuations of the euro against the dollar. In addition, other customers may also make payments in foreign currencies. Also, certain transactions with foreign suppliers are denominated in foreign currencies, primarily yen.

The majority of our international sales are currently invoiced and collected in U.S. dollars. A strengthening in the dollar relative to the currencies of those countries in which we do business would increase the prices of our products as stated in those currencies and could hurt our sales in those countries. Significant fluctuations in the exchange rates between the U.S. dollar and foreign currencies could cause us to lower our prices and thus reduce our profitability. These fluctuations could also cause prospective customers to cancel or delay orders because of the increased relative cost of our products.

Operational Risks

We depend on a small number of customers for nearly all of our sales, and the loss of a large customer could materially adversely affect our revenues or operating results.

Our ten largest customers accounted for approximately 69%, 85%, 85% and 85% of net sales in 1999, 2000, 2001 and the first quarter of 2002, respectively. We have contracts extending past 2002 with only two of these customers. We expect to continue to derive a significant portion of our net sales from this relatively small number of customers. Accordingly, the loss of a large customer could materially hurt our business, and the deferral or loss of anticipated orders from a large customer or a small number of customers could materially reduce our revenue and operating results in any period.

We must continue to develop new products or enhance existing products on a timely basis to compete successfully in a rapidly changing marketplace.

Our future success depends upon our ability to introduce new products, improve existing products and processes to keep pace with technological and market developments, and to address the increasingly sophisticated and demanding needs of our customers, especially in the electronic display and automotive markets. Technological changes, process improvements, or operating improvements that could adversely affect us include:

- the development of competing technologies to our anti-reflective and silver reflector films for liquid crystal displays in the flat panel display industry;
- changes in the way coatings are applied to alternative substrates such as tetra acetate cellulose, or TAC;
- the development of new technologies that improve the manufacturing efficiency of our competitors;
- the development of new materials that improve the performance of products that could compete with our products; and
- improvements in the alternatives to the sputtering technology we use to produce our products, such as plasma enhanced chemical vapor deposition, or PECVD.

Our research and development efforts may not be successful in developing products in the time, or with the characteristics, necessary to meet customer needs. If we do not adapt to technological changes, or process or operating improvements, our competitive position, operations and prospects would be materially adversely affected.

Our ability to successfully identify suitable target companies and integrate acquired companies or technologies may affect our future growth.

A potential part of our continuing business strategy is to consider acquiring companies, products, and technologies that complement our current products, enhance our market coverage, technical capabilities or production capacity, or offer other growth opportunities. Our ability to successfully complete acquisitions requires that we identify suitable target companies, agree on acceptable terms, and obtain acquisition financing on acceptable terms. In connection with these acquisitions, we could incur debt, amortization expenses relating to identified intangibles, impairment charges relating to goodwill, or merger related charges, or could issue stock that would dilute our current shareholders' percentage of ownership. The success of any acquisitions will depend upon our ability to integrate acquired operations, retain and motivate acquired personnel, and increase the customer base of the combined businesses. We cannot assure you that we will be able to accomplish all of these goals. Any future acquisitions would involve certain additional risks, including:

difficulty integrating the purchased operations, technologies, or products;

unanticipated costs, which would reduce our profitability;

diversion of management's attention from our core business;

potential entrance into markets in which we have limited or no prior experience; and

potential loss of key employees, particularly those of the acquired business.

Failure to meet the volume requirements of our customers may result in a loss of business or contractual penalties.

Our long-term competitive position will depend to a significant extent on our manufacturing capacity. The failure to have sufficient capacity, to fully utilize capacity when needed or to successfully integrate and manage additional capacity in the future could adversely affect our relationships with customers and cause customers to buy similar products from our competitors if we are unable to meet their needs. For example, we believe that we lost substantial potential architectural products sales in 2001 because we did not have the capacity to manufacture the required amounts of products. Also, our failure to produce required amounts of products under some of our contracts will result in price reductions on future sales under such contracts or penalties under which we would be required to reimburse the customer for the full cost of any product not delivered in a timely manner, either of which would reduce our gross margins.

We depend on our OEM customers for the sale of our products.

We sell a substantial portion of our products to a relatively small number of original equipment manufacturers, or OEMs. The timing and amount of sales to these customers ultimately depend on sales levels and shipping schedules for the OEM products into which our products are incorporated. We have no control over the volume of products shipped by our OEM customers or shipping dates, and we cannot be certain that our OEM customers will continue to ship products that incorporate our products at current levels or at all. We currently have a long-term contract with only one of our OEM customers. Failure of our OEM customers to achieve significant sales of products incorporating our products and fluctuations in the timing and volume of such sales could be harmful to our business. Failure of these customers to inform us of changes in their production needs in a timely manner could also hinder our ability to effectively manage our business.

We rely upon our OEM customers for information relating to the development of new products so that we are able to meet end-user demands.

We rely on our OEM customers to inform us of opportunities to develop new products that serve end-user demands. If our OEM customers do not present us with market opportunities early enough

for us to develop products to meet end-user needs in a timely fashion, or if the OEMs fail to anticipate end-user needs at all, we may fail to develop new products or modify our existing products for the end-user markets for our products. In addition, if our OEM customers fail to accurately anticipate end-user demands, we may spend resources on products that are not commercially successful.

We depend on a distributor for the sale of our after-market products.

We primarily use one independent distributor to sell our after-market products. We have a distribution agreement with Globamatrix Holdings Pte. Ltd., or Globamatrix, under which we granted an exclusive worldwide license to distribute our after-market applied film in the automotive and architectural glass markets. Failure of Globamatrix to achieve significant sales of products incorporating our products and fluctuations in the timing and volume of such sales could be harmful to our business. We believe that the success of our after-market products will continue to depend upon this distributor.

We face intense competition, which could affect our ability to increase our revenue, maintain our margins and increase our market share.

The market for each of our products is intensely competitive and we expect competition to increase in the future. Competitors vary in size and in the scope and breadth of the products they offer. We compete both with companies using technology similar to ours and companies using other technologies or developing improved technologies. Many of our current and potential competitors have significantly greater financial, technical, marketing and other resources than we have. In addition, many of our competitors have well-established relationships with our current and potential customers and have extensive knowledge of our industry. In fact, some of our current and potential customers currently produce, or are capable of creating, products that compete with our products.

We may not be able to expand our manufacturing capacity efficiently which could lead to lower gross margins.

We have ordered for our Dresden manufacturing facility a new machine (PM 10), which we anticipate will begin commercial production in the first quarter of 2003. In addition, we anticipate that PM 7 in our Tempe facility will begin commercial production during the third quarter of 2002. During the processes of bringing PM 7 and PM 10 up to commercial production levels, we expect to have decreased manufacturing yields and higher costs, which will lower our gross margins.

We are dependent on key suppliers of materials which may prevent us from delivering product in a timely manner.

We manufacture all of our products using materials procured from third-party suppliers. We do not have long-term contracts with our third-party suppliers, except for an agreement with a third-party supplier to purchase Indium metal through the second quarter of 2003. Certain of the materials we require are obtained from a limited number of sources. Delays or reductions in product shipments could damage our relationships with customers. Further, a significant increase in the price of one or more of the materials used in our products could have a material adverse effect on our cost of goods sold and operating results.

We are dependent on a few qualified subcontractors to add properties to some of our products.

We rely on third-party subcontractors to add properties, such as adhesives, to some of our products. There are only a limited number of qualified subcontractors that can provide some of the services we require and we do not have long-term contracts with any of those subcontractors. Qualifying alternative subcontractors could take a great deal of time or cause us to change product designs. The loss of a subcontractor could adversely affect our ability to meet our scheduled product deliveries to customers, which could damage our relationships with customers. If our subcontractors do not produce a quality product, our yield will decrease and our margins will be lower. Further, a

significant increase in the price charged by one or more of our subcontractors could force us to raise prices on our products or lower our margins, which could have a material adverse effect on our operating results.

We are dependent on key suppliers of production machines which may prevent us from delivering an acceptable product on a timely basis and limit our capacity for revenue growth.

Our production machines are large, complex and difficult to manufacture. It can take up to a year from the time we order a machine until it is delivered. Following delivery, it can take us, with the assistance of the manufacturer, up to six additional months to test and prepare the machine for commercial production. There are a very limited number of companies that are capable of manufacturing these machines. Our inability in the future to have new production machines manufactured and prepared for commercial production in a timely manner would prevent us from delivering product on a timely basis and limit our capacity for revenue growth.

Fluctuations or slowdowns in the overall electronic display industry have and may continue to adversely affect our revenues.

Our business depends in part on sales by manufacturers of products that include electronic displays. The markets for electronic display products are highly cyclical and have experienced periods of oversupply resulting in significantly reduced demand for our products. For example, due to the deteriorating economic environment, sales by flat panel cathode ray tube manufacturers decreased in 2001, contributing to our electronic display product revenues declining by 38% from 2000. If the flat panel display and other electronic display markets in which we sell our products do not recover or experience further slowdowns in the future, it could cause revenues from our electronic display products to decrease.

Performance, reliability or quality problems with our products may cause our customers to reduce or cancel their orders.

We manufacture our products based on specific, technical requirements of each of our customers. We believe that future orders of our products will depend in part on our ability to maintain the performance, reliability and quality standards required by our customers. If our products have performance, reliability or quality problems, then we may experience:

- delays in collecting accounts receivable;

higher manufacturing costs;

additional warranty and service expenses; and

reduced or cancelled orders.

For example, in 1998, our operating results were materially adversely affected by quality problems associated with the electronic display film produced by us for one of our largest customers.

If we fail to recruit and retain a significant number of qualified technical personnel, we may not be able to develop, enhance and introduce our products on a timely basis, and our business will be harmed.

We require the services of a substantial number of qualified technical personnel. The market for skilled technical personnel is characterized by intense competition and aggressive recruiting, as well as a high-level of employee mobility. These characteristics make it particularly difficult for us to attract and retain the qualified technical personnel we require. We have experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees with appropriate technical qualifications. It is especially difficult for us to recruit qualified personnel to move to the location of our Palo Alto, California offices because of the high-cost of living. If we are unable to recruit and retain a sufficient number of qualified technical employees, we may not be able to complete the

development of, or enhance, our products in a timely manner. As a result, our business may be harmed and our operating results may suffer.

We may be unable to attract or retain the other highly skilled employees that are necessary for the success of our business.

In addition to our dependence on our technical personnel, our success also depends on our continuing ability to attract and retain other highly skilled employees. We depend on the continued services of our senior management, particularly Thomas G. Hood, our President and Chief Executive Officer, Robert R. Freeman our Chief Financial Officer, Dr. Sicco W. T. Westra, our Senior Vice President, Sales and Marketing, and Wolfgang Heinze, our plant manager in Dresden, and other personnel. We do not have employment contracts with any of our officers or key person life insurance covering any officer or employee. Our officers have technical and industry knowledge that cannot easily be replaced. Competition for similar personnel in our industry where we operate is intense. We have experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. If we do not succeed in attracting or retaining the necessary personnel, our business could be adversely affected.

If we are unable to adequately protect our intellectual property, third parties may be able to duplicate our products or develop functionally equivalent or superior technology.

Our success depends in large part upon our proprietary technology. We rely on our know-how, as well as a combination of patent, trademark and trade secret protection, to establish and protect our intellectual property rights. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or to obtain and use information that we regard as proprietary. Policing unauthorized use of our products is difficult. Our means of protecting our proprietary rights may not be adequate. In addition, the laws of some foreign countries do not protect our proprietary rights to as great an extent as do the laws of the United States. During 2001, one of our U.S. patents relating to our architectural products expired. In the next three years, two more U.S. patents will expire. Expiration of these patents or our failure to adequately protect our proprietary rights may allow third parties to duplicate our products or develop functionally equivalent or superior technology. In addition, our competitors may independently develop similar technology or design around our proprietary intellectual property.

Our business is susceptible to numerous risks associated with international operations.

We have expanded our operations and hired additional personnel to address international markets for the thin film coatings industry. International revenues amounted to approximately 78%, 85%, 87% and 86% of our net revenues during 1999, 2000, 2001 and the first quarter of 2002, respectively. The distance between Palo Alto and Dresden creates logistical and communications challenges. In addition, to achieve acceptance in international markets, our products must be modified to handle a variety of factors specific to each international market as well as local regulations. We may also be subject to a number of other risks associated with international business activities. These risks include:

unexpected changes in and the burdens and costs of compliance with a variety of foreign laws and regulatory requirements;

potentially adverse tax consequences; and

global economic turbulence and political instability.

Labor strikes in Germany could disrupt the production schedule of automotive products that incorporate our films, which could have a material adverse effect on our revenues.

On May 6, 2002, German metal workers represented by IG Metal began rolling strikes against a number of companies in Germany, including DaimlerChrysler, in connection with negotiations over a

new labor contract. Our customers in the automotive glass market sell glass incorporating our products to German automobile manufacturers including DaimlerChrysler. A prolonged strike by IG Metal or other workers or a significant delay in DaimlerChrysler's production schedule or the production schedules of others as a result of labor activity could disrupt the demand for our products, which would adversely affect our revenues.

If we fail to comply with environmental regulations, our operations could be suspended.

We use hazardous chemicals in producing our products and have air and water emissions that require controls. As a result, we are subject to a variety of local, state and federal governmental regulations relating to the storage, discharge, handling, emission, generation, manufacture and disposal of toxic or other hazardous substances used to manufacture our products, compliance with which is expensive. Our failure to comply with current or future regulations could result in the imposition of substantial fines on us, suspension of production, alteration of our manufacturing processes, increased costs or cessation of operations.

We rely on our domestic sales representatives, without whom our architectural product sales may suffer.

We use independent sales representatives to promote our Heat Mirror products to architects in the United States. If some or all of our sales representatives experience financial difficulties, or otherwise become unable or unwilling to promote our products, our business could be harmed. These sales representatives could reduce or discontinue promotion of our products. They may not devote the resources necessary to provide effective marketing support to us. In addition, we depend upon the continued viability and financial resources of these representatives, many of which are small organizations with limited working capital. These representatives, in turn, depend substantially on general economic conditions and other factors affecting the markets for the products they promote. We believe that our success in this market will continue to depend upon these sales representatives.

We may experience unanticipated warranty or other claims with respect to our products which may lead to extensive litigation costs and expenses.

In the ordinary course of business, we have periodically become engaged in litigation principally as a result of disputes with customers of our architectural products. We have settled some of these suits and others are pending. We may become engaged in similar or other lawsuits in the future. For example, we have recently received a letter that threatens litigation based upon the allegation that a sealant provided by a third party and used with our film was defective, and as a result the plaintiff has suffered elevated warranty replacement claims and costs. Some of our products that have been the basis for lawsuits against us could be the basis for future lawsuits. An adverse outcome in the defense of a warranty or other claim could subject us to significant liabilities to third parties. Any litigation, regardless of the outcome, could be costly and require significant time and attention of key members of our management and technical personnel.

We may face extensive damages or litigation costs if our insurance carriers seek to have us indemnify them for settlements of past and outstanding litigation.

Several of our insurance carriers have reserved their rights to seek indemnification from us for substantial amounts paid to plaintiffs by the insurance carriers as part of settlements of litigation relating to our architectural products. Our insurance carriers in a case in which the plaintiff alleged we were responsible for defects in window products manufactured by others have advised us that they intend to seek reimbursement for settlement and defense costs. Any claims, with or without merit, could require significant time and attention of key members of our management and result in costly litigation. Some of the proceeds of this offering could be used to defend or satisfy obligations arising from this potential litigation.

Offering Risks

Our stock price could fluctuate widely in response to various factors, many of which are beyond our control.

The market price of our common stock has been, and we expect will continue to be, subject to significant fluctuations. For example, over the past year the closing market price of our common stock has fluctuated between $2.60 on May 22, 2001 and $4.76 on July 1, 2002 while reaching a high of $15.45 on April 17, 2002. Factors affecting our market price include:

- the limited number of shares of common stock available for purchase or sale in the public markets;
- sales or purchases of large blocks of our shares;
- quarterly variations in our results of operations;
- failure to meet earnings estimates;
- changes in earnings estimates or buy/sell recommendations by analysts;
- the operating and stock price performance of comparable companies;
- developments in the financial markets;
- the announcement of new products or product enhancements or business results by us or our competitors; and
- general market conditions or market conditions specific to the industries in which we operate.

Recent events have caused stock prices for many companies, including our company, to fluctuate in ways unrelated or disproportionate to their operating performance. General economic and political events may affect market conditions generally, and, in particular, the market price of our common stock. These events and market trends are beyond our control. The market price of our common stock at any particular time may not remain the market price in the future.

Certain provisions of our charter, by-laws and Delaware law make a takeover difficult.

Certain provisions of our corporate charter and by-laws and Delaware law, might discourage, delay or prevent a change of control or a change in our management, even if such changes would be beneficial to our stockholders. These provisions include the ability of our board of directors, without stockholder approval, to issue any class or series of preferred stock with dividend rights, dividend rates, conversion rights, redemption rights, preferences on liquidation or dissolution, voting rights and any other preferences, which could adversely affect the voting and other rights of the holders of common stock. These provisions could discourage proxy contests and make it more difficult for you and other stockholders to elect directors and take other corporate actions. We also have a severance policy that covers all of our officers and some of our key employees under which they may become entitled to special benefits in connection with certain changes in control of Southwall. The existence of all of these provisions and policies could limit the price that investors might be willing to pay for shares of our common stock and could deprive you of an opportunity to receive a premium for your common stock as part of a sale of Southwall. See "Description of Capital Stock."

The market price of our common stock may drop significantly when the restrictions on resale by our existing securityholders lapse.

Following this offering, we will have approximately 12.1 million shares of common stock outstanding. Holders of approximately 1,612,129 shares have agreed not to sell these shares for at least 180 days following the date of this prospectus. As these restrictions on resale end, the market price of our common stock could drop significantly if holders of these shares sell them or if the market perceives they intend to sell them. We also currently have 1,401,859 shares subject to outstanding options under our 1997 stock incentive plan with a weighted average exercise price of $5.24 per share and 694,345 shares subject to outstanding options under our 1998 stock option plan with a weighted average purchase price of $6.61 per share, all of which may be exercised and sold by option holders in the future. These potential future exercises and sales also may make it difficult for us to sell equity securities in the future at a time and price that we deem appropriate.

FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements, as that term is defined in the Private Securities Litigation Reform Act of 1995, that are subject to a number of risks and uncertainties. All statements other than statements of historical facts are forward-looking statements. These statements are identified by terminology such as "may," "will," "could," "should," "expects," "plans," "intends," "seeks," "anticipates," "believes," "estimates," "potential," or "continue," or the negative of such terms or other comparable terminology, although not all forward-looking statements contain these identifying words. Forward-looking statements are only predictions and include statements relating to:

- our strategy, future operations and financial plans, including, without limitation, our plans to install and commercially produce products on new machines;
- future applications of thin film coating technologies and our development of new products;
- our projected need for additional borrowings and our future liquidity;
- our competition;
- our expectations with respect to future grants, investment allowances and bank guarantees from the Saxony government;
- statements about the future size of markets;
- pending and threatened litigation and its outcome;
- our use of the proceeds of this offering; and
- our projected capital expenditures.

You should not place undue reliance on our forward-looking statements. Actual events or results may differ materially. In evaluating these statements, you should specifically consider various factors, including the risks outlined under "Risk Factors." These factors may cause our actual results to differ materially from any forward-looking statement. Although we believe the expectations reflected in our forward-looking statements are reasonable as of the date they are being made, we cannot guarantee our future results, levels of activity, performance, or achievements. Moreover, neither we nor any other person assumes responsibility for the future accuracy and completeness of these forward-looking statements.

USE OF PROCEEDS

We estimate our net proceeds from the sale of 3,500,000 shares of common stock that we are offering by means of this prospectus will be approximately $14.1 million, at the public offering price of $4.50 per share, after deducting estimated underwriting discounts and commissions, and offering expenses. If the underwriters' over-allotment option is exercised in full, we estimate our net proceeds will be approximately $16.3 million. We will not receive any proceeds from the sale of shares in the over- allotment option by the selling stockholders.

We intend to use a portion of our net proceeds from this offering as follows:

- to pay off the outstanding balance of our accounts receivable financing line of credit, which as of June 30, 2002 was approximately $3.4 million; this indebtedness bears interest at 0.88% per month of the average daily balance of accounts receivable against which we have borrowed and expires in June 2003;

- approximately $2.5 million to pay down a note payable to a Japanese bank and guaranteed by Teijin Limited; this indebtedness bears interest per annum at a percentage rate of LIBOR plus 1.0% and we are required to make equal semi-annual principal repayments of $1.25 million each May and November until the note is fully repaid in November 2004; the $2.5 million we intend to repay in 2002 would be applied towards the last two required payments;

- approximately $2.0 million to replace our enterprise resource planning system;

- approximately $2.5 million towards the purchase of a new production machine (PM 10);

- approximately $1.5 million to maintain and update our production facilities in Palo Alto and Tempe; and

- approximately $0.75 million to partially repay a loan from a German bank; this loan bears interest at 5.8% per annum on the total committed amount under the loan of $1.5 million and is due in June 2009.

The remaining net proceeds from this offering may be used as follows:

- to make future acquisitions of product lines or technologies or other companies, although we currently have no acquisition agreements or understandings in place;

- the potential resolution of disputes with insurers or settlement of litigation, including litigation with Matrix Funding Corporation arising out of sale-leaseback agreements for two of our production machines; and

- the balance for funding of working capital and general corporate purposes.

With respect to the balance of the net proceeds after the repayment of debt, replacement of our enterprise resource planning system, the purchase of PM 10 and the maintenance and updating of our production facilities in Palo Alto and Tempe, we have not determined the amount of net proceeds to be used for the other purposes indicated. Accordingly, our management will have flexibility in applying net proceeds of the offering. Pending any use, we intend to invest our net proceeds from this offering in short-term, interest-bearing, investment-grade securities, certificates of deposit or direct or guaranteed obligations of the United States.

DIVIDEND POLICY

We have never declared or paid any cash dividends on our common stock, and we do not anticipate paying cash dividends in the foreseeable future. We currently intend to retain future earnings, if any, to fund the expansion and growth of our business. Payment of future cash dividends, if any, will be at the discretion of our board of directors after taking into account various factors, including our financial condition, operating results, current and anticipated cash needs and plans for expansion.

CAPITALIZATION

The following table sets forth our capitalization as of March 31, 2002 on an actual basis and on a pro forma as adjusted basis to reflect the sale by us of 3,500,000 shares of common stock offered hereby at the public offering price of $4.50 per share, after deducting the estimated underwriting discount and estimated offering expenses payable by us, and to reflect the net proceeds of the offering as applied.

This information should be read in conjunction with our consolidated financial statements and notes thereto, appearing elsewhere in this prospectus.

	March 31, 2002	
	Actual	Pro Forma as Adjusted
	(in thousands)	
Line of credit	$ 4,606	$
Current portion of long-term debt	$ 7,579	$ 7,579
Term debt, less current portion	13,800	9,800
Total long-term debt	$ 21,379	$ 17,379
Stockholders' equity:		
Common Stock, $0.001 par value: 20,000 shares authorized; 8,562 shares issued and outstanding (actual); 12,062 shares issued and outstanding (pro forma as adjusted)	9	12
Capital in excess of par value	53,467	67,608
Notes receivable	(103)	(103)
Translation loss on subsidiary	(356)	(356)
Accumulated deficit	(24,731)	(24,731)
Total stockholders' equity	28,286	42,430
Total capitalization	$ 49,665	$ 59,809

This information excludes 1,979,494 shares, which consist of:

1,450,653 shares subject to outstanding options as of March 31, 2002 under our 1997 stock incentive plan, with a weighted average exercise price of $5.24 per share; and

528,841 shares subject to outstanding options as of March 31, 2002 under our 1998 stock option plan for employees and consultants, with a weighted average exercise price of $5.20 per share.

PRICE RANGE OF COMMON STOCK

Our common stock has been traded on the Nasdaq National Market System under the symbol "SWTX" since the completion of our initial public offering in June 1987. From August 2, 2000 through November 28, 2000, the trading of our common stock was suspended by Nasdaq in connection with the restatement of our financial statements. Prices in the following table represent the high and low closing sales prices per share for our common stock as reported by Nasdaq during the periods indicated.

	High	Low
2000		

	High	Low
First quarter	$ 11.87	$ 4.68
Second quarter	11.25	7.37
Third quarter	14.00	6.12
Fourth quarter	4.17	2.62
2001		
First quarter	3.63	2.00
Second quarter	3.47	2.03
Third quarter	5.41	2.97
Fourth quarter	7.26	4.55
2002		
First quarter	12.99	7.19
Second quarter	15.45	4.68

On July 1, 2002 the last reported sale price for our common stock as reported on Nasdaq was $4.76 per share. On such date, there were approximately 350 holders of record of our common stock, and we believe there were approximately 3,000 beneficial owners of our common stock.

SELECTED CONSOLIDATED FINANCIAL DATA

(in thousands, except per share data)

The following selected consolidated financial data as of and for the five years ended December 31, 2001 are derived from our audited consolidated financial statements. The following selected consolidated financial data as of and for the three months ended April 1, 2001 and March 31, 2002 have been derived from our unaudited consolidated financial statements for the three months ended March 31, 2002. In the opinion of management, such unaudited financial statements have been prepared on the same basis as the audited financial statements referred to above and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of results of operations for the indicated period when read in conjunction with our audited financial statements and related notes. Results of operations for the three months ended March 31, 2002 are not necessarily indicative of the results that may be expected for the full year. This information should be read together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes included elsewhere in this prospectus.