

NET 1 UEPS TECHNOLOGIES INC
Form 10-Q
May 08, 2014

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

(Mark One)

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

For the quarterly period ended **March 31, 2014**

OR

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

For the transition period from _____ To _____

Commission file number: **000-31203**

NET 1 UEPS TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

Florida
(State or other jurisdiction
of incorporation or organization)

98-0171860
(IRS Employer
Identification No.)

President Place, 4th Floor, Cnr. Jan Smuts Avenue and Bolton Road

Rosebank, Johannesburg 2196, South Africa

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: **27-11-343-2000**

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

YES ☒ NO ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES ☒ NO ☐

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (check one):

☐ Large accelerated filer

☒ Accelerated filer

☐ Non-accelerated filer

☐ Smaller reporting company

(do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES ☐ NO ☒

As of May 8, 2014 (the latest practicable date), 50,183,342 shares of the registrant's common stock, par value \$0.001 per share, net of treasury shares, were outstanding.

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Part I. Financial Information**Item 1. Financial Statements**

NET 1 UEPS TECHNOLOGIES, INC.
Unaudited Condensed Consolidated Balance Sheets

| | Unaudited March 31, 2014 | (A) June 30, 2013 |
|---|-----------------------------------|-------------------------|
| | (In thousands, except share data) | |
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 30,875 | \$ 53,665 |
| Pre-funded social welfare grants receivable (Note 2) | 4,728 | 2,934 |
| Accounts receivable, net of allowances of March: \$1,592; June: \$4,701 | 132,356 | 102,614 |
| Finance loans receivable, net of allowances of March: \$1,815; June: \$- | 42,379 | 8,350 |
| Inventory (Note 3) | 10,491 | 12,222 |
| Deferred income taxes | 5,350 | 4,938 |
| Total current assets before settlement assets | 226,179 | 184,723 |
| Settlement assets (Note 4) | 744,782 | 752,476 |
| Total current assets | 970,961 | 937,199 |
| PROPERTY, PLANT AND EQUIPMENT, net of accumulated depreciation of March: \$92,314; June: \$84,808 | | |
| | 46,150 | 48,301 |
| EQUITY-ACCOUNTED INVESTMENTS | 1,347 | 1,183 |
| GOODWILL (Note 6) | 179,832 | 175,806 |
| INTANGIBLE ASSETS, net (Note 6) | 69,265 | 77,257 |
| OTHER LONG-TERM ASSETS, including reinsurance assets (Note 7) | 34,338 | 36,576 |
| TOTAL ASSETS | 1,301,893 | 1,276,322 |
| LIABILITIES | | |
| CURRENT LIABILITIES | | |
| Bank overdraft (Note 8) | - | - |
| Accounts payable | 14,592 | 26,567 |
| Other payables | 35,682 | 33,808 |
| Current portion of long-term borrowings (Note 9) | 14,005 | 14,209 |
| Income taxes payable | 11,749 | 2,275 |
| Total current liabilities before settlement obligations | 76,028 | 76,859 |
| Settlement obligations (Note 4) | 744,782 | 752,476 |
| Total current liabilities | 820,810 | 829,335 |
| DEFERRED INCOME TAXES | 17,343 | 18,727 |
| LONG-TERM BORROWINGS (Note 9) | 58,061 | 66,632 |
| OTHER LONG-TERM LIABILITIES, including insurance policy liabilities (Note 7) | 20,117 | 21,659 |
| TOTAL LIABILITIES | 916,331 | 936,353 |
| COMMITMENTS AND CONTINGENCIES (Note 17) | | |
| EQUITY | | |
| COMMON STOCK (Note 10) | | |
| Authorized: 200,000,000 with \$0.001 par value; | 59 | 59 |
| Issued and outstanding shares, net of treasury - March: 45,783,342; | | |

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June: 45,592,550

PREFERRED STOCK

Authorized shares: 50,000,000 with \$0.001 par value;

Issued and outstanding shares, net of treasury: March: -; June: -

-

-

ADDITIONAL PAID-IN-CAPITAL

165,076

160,670

TREASURY SHARES, AT COST: March: 13,455,090; June: 13,455,090

(175,823)

(175,823)

ACCUMULATED OTHER COMPREHENSIVE LOSS

(97,910)

(100,858)

RETAINED EARNINGS

494,145

452,618

TOTAL NET1 EQUITY

385,547

336,666

NON-CONTROLLING INTEREST

15

3,303

TOTAL EQUITY

385,562

339,969

TOTAL LIABILITIES AND SHAREHOLDERS EQUITY\$

1,301,893

\$

1,276,322

(A) Derived from audited financial statements

See Notes to Unaudited Condensed Consolidated Financial Statements

NET 1 UEPS TECHNOLOGIES, INC.
Unaudited Condensed Consolidated Statements of Operations

| | Three months ended March 31, | | Nine months ended March 31, | |
|--|---|-------------|--|-------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (In thousands, except per share data) | | (In thousands, except per share data) | |
| REVENUE | \$ 138,126 | \$ 111,141 | \$ 398,903 | \$ 334,265 |
| EXPENSE | | | | |
| Cost of goods sold, IT processing, servicing and support | 63,149 | 51,461 | 187,591 | 143,789 |
| Selling, general and administration | 40,586 | 53,846 | 121,916 | 149,854 |
| Depreciation and amortization | 10,442 | 10,560 | 30,245 | 31,051 |
| OPERATING INCOME (LOSS) | 23,949 | (4,726) | 59,151 | 9,571 |
| INTEREST INCOME | 3,438 | 2,515 | 9,993 | 8,195 |
| INTEREST EXPENSE | 1,734 | 2,023 | 5,712 | 6,117 |
| INCOME (LOSS) BEFORE INCOME TAX EXPENSE | 25,653 | (4,234) | 63,432 | 11,649 |
| INCOME TAX EXPENSE (note 16) | 8,535 | 472 | 22,119 | 7,172 |
| NET INCOME (LOSS) BEFORE EARNINGS FROM EQUITY-ACCOUNTED INVESTMENTS | 17,118 | (4,706) | 41,313 | 4,477 |
| EARNINGS FROM EQUITY-ACCOUNTED INVESTMENTS | 52 | 22 | 202 | 204 |
| NET INCOME (LOSS) | 17,170 | (4,684) | 41,515 | 4,681 |
| ADD NET LOSS ATTRIBUTABLE TO NON- CONTROLLING INTEREST | (12) | (3) | (12) | (11) |
| NET INCOME (LOSS) ATTRIBUTABLE TO NET1 | \$ 17,182 | \$ (4,681) | \$ 41,527 | \$ 4,692 |
| Net income (loss) per share, in United States dollars (note 13) | | | | |
| Basic earnings (loss) attributable to Net1 shareholders | \$ 0.38 | \$ (0.10) | \$ 0.91 | \$ 0.10 |

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| | | | | | | | |
|---|----|------|----|--------|----|------|---------|
| Diluted earnings (loss) attributable to | | | | | | | |
| Net1 shareholders | \$ | 0.37 | \$ | (0.10) | \$ | 0.90 | \$ 0.10 |

See Notes to Unaudited Condensed Consolidated Financial Statements

NET 1 UEPS TECHNOLOGIES, INC.
Unaudited Condensed Consolidated Statements of Comprehensive Income

| | Three months ended | | Nine months ended | |
|---|---------------------------|-------------|--------------------------|-------------|
| | March 31, | | March 31, | |
| | 2014 | 2013 | 2014 | 2013 |
| | (In thousands) | | (In thousands) | |
| Net income (loss) | \$ 17,170 | \$ (4,684) | \$ 41,515 | \$ 4,681 |
| Other comprehensive (loss) income | | | | |
| Net unrealized income on asset available for sale, net of tax | 327 | - | 288 | 258 |
| Movement in foreign currency translation reserve | (2,134) | (22,993) | 2,838 | (12,811) |
| Total other comprehensive (loss) income, net of taxes | (1,807) | (22,993) | 3,126 | (12,553) |
| Comprehensive income (loss) | 15,363 | (27,677) | 44,641 | (7,872) |
| Add comprehensive loss attributable to non-controlling interest | 12 | 3 | 12 | 11 |
| Comprehensive income (loss) attributable to Net1 | \$ 15,375 | \$ (27,674) | \$ 44,653 | \$ (7,861) |

See Notes to Unaudited Condensed Consolidated Financial Statements

NET 1 UEPS TECHNOLOGIES, INC.
Consolidated Statement of Changes in Equity (dollar amounts in thousands)

Net 1 UEPS Technologies, Inc. Shareholder

| | | | | | | | | | | Accumulated |
|--|----------------|------------|--------|--------------|--------------|-------------|------------|------------|---------------|-------------|
| | | Number of | Amount | Number of | Treasury | Number of | Additional | Retained | comprehensive | other |
| | | Shares | | Treasury | Shares | shares, net | Paid-In | Earnings | (loss) | income |
| | | | | Shares | | of treasury | Capital | | | |
| Balance | July 1, 2013 | 59,047,640 | \$ 59 | (13,455,090) | \$ (175,823) | 45,592,550 | \$ 160,670 | \$ 452,618 | \$ | (100,858) |
| Restricted stock granted | | 187,963 | | | | 187,963 | | | | |
| Exercise of stock option | | 10,000 | | | | 10,000 | 88 | | | |
| Stock-based compensation charge | | | | | | | 2,826 | | | |
| Reversal of stock-based compensation charge | | (7,171) | | | | (7,171) | (6) | | | |
| Income tax benefit from vested stock awards | | | | | | | 6 | | | |
| Acquisition of KSNET non-controlling interest (Note 10) | | | | | | | 1,492 | | | (178) |
| Net income | | | | | | | | 41,527 | | |
| Other comprehensive income | | | | | | | | | | 3,126 |
| Balance | March 31, 2014 | 59,238,432 | \$ 59 | (13,455,090) | \$ (175,823) | 45,783,342 | \$ 165,076 | \$ 494,145 | \$ | (97,910) |
| See Notes to Unaudited Condensed Consolidated Financial Statements | | | | | | | | | | |

See Notes to Unaudited Condensed Consolidated Financial Statements

NET 1 UEPS TECHNOLOGIES, INC.
Unaudited Condensed Consolidated Statements of Cash Flows

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|---------------------------------|------------------|--------------------------------|------------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (In thousands) | | (In thousands) | |
| Cash flows from operating activities | | | | |
| Net income (loss) | \$ 17,170 | \$ (4,684) | \$ 41,515 | \$ 4,681 |
| Depreciation and amortization | 10,442 | 10,560 | 30,245 | 31,051 |
| Earnings from equity-accounted investments | (52) | (22) | (202) | (204) |
| Fair value adjustments | 110 | (299) | 49 | 408 |
| Interest payable | 30 | 1,054 | 1,696 | 3,363 |
| (Profit) loss on disposal of property, plant and equipment | (26) | 3 | (42) | (83) |
| Stock-based compensation charge | 922 | 1,092 | 2,820 | 3,325 |
| Facility fee amortized | 79 | 71 | 657 | 235 |
| Increase in accounts receivable, pre-funded social welfare grants receivable and finance loans receivable | (6,443) | (4,818) | (67,521) | (3,987) |
| Decrease (Increase) in inventory | 2,821 | 4,949 | 979 | (2,260) |
| Increase (Decrease) in accounts payable and other payables | 2,656 | 4,533 | (10,895) | (1,755) |
| Increase in taxes payable | 8,069 | 948 | 9,431 | 354 |
| Decrease in deferred taxes | (1,141) | (1,201) | (3,019) | (4,133) |
| Net cash provided by operating activities | 34,637 | 12,186 | 5,713 | 30,995 |
| Cash flows from investing activities | | | | |
| Capital expenditures | (4,848) | (5,053) | (17,309) | (17,103) |
| Proceeds from disposal of property, plant and equipment | 123 | 31 | 2,124 | 387 |
| Acquisitions, net of cash acquired | - | - | - | (2,143) |
| (Investment in equity in) Repayment of loan by equity-accounted investment | (25) | - | (25) | 3 |
| Proceeds from maturity of investments related to insurance business | - | - | - | 545 |
| Other investing activities, net | 571 | - | 570 | - |
| Net change in settlement assets | (277,912) | (156,363) | (21,409) | (168,419) |
| Net cash used in investing activities | (282,091) | (161,385) | (36,049) | (186,730) |
| Cash flows from financing activities | | | | |
| Long-term borrowings obtained (Note 9) | 1,028 | - | 72,633 | - |
| Repayment of long-term borrowings (Note 9) | - | - | (87,008) | (7,307) |
| Payment of facility fee (Note 9) | - | - | (872) | - |
| Proceeds from bank overdraft | - | - | 24,580 | - |
| Repayment of bank overdraft | (23,335) | - | (23,335) | - |
| Acquisition of interests in KSNET (Note 10) | - | - | (1,968) | - |
| Proceeds from issue of common stock | 88 | - | 88 | 240 |
| Net change in settlement obligations | 277,912 | 156,363 | 21,409 | 168,419 |
| Net cash provided by financing activities | 255,693 | 156,363 | 5,527 | 161,352 |
| activities | | | | |
| Effect of exchange rate changes on cash | 274 | (2,664) | 2,019 | (2,124) |

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| | | | | | |
|--|----------------------------|-----------|-----------|-----------|-----------|
| Net increase (decrease) in cash and cashequivalents | | 8,513 | 4,500 | (22,790) | 3,493 |
| Cash and cash equivalents | beginning of period | 22,362 | 38,116 | 53,665 | 39,123 |
| Cash and cash equivalents | end of period | \$ 30,875 | \$ 42,616 | \$ 30,875 | \$ 42,616 |

See Notes to Unaudited Condensed Consolidated Financial Statements

NET 1 UEPS TECHNOLOGIES, INC.

**Notes to the Unaudited Condensed Consolidated Financial Statements
for the three and nine months ended March 31, 2014 and 2013**

(All amounts in tables stated in thousands or thousands of United States Dollars, unless otherwise stated)

1. Basis of Presentation and Summary of Significant Accounting Policies

Unaudited Interim Financial Information

The accompanying unaudited condensed consolidated financial statements include all majority-owned subsidiaries over which the Company exercises control and have been prepared in accordance with US generally accepted accounting principles (GAAP) and the rules and regulations of the Securities and Exchange Commission for quarterly reports on Form 10-Q and include all of the information and disclosures required for interim financial reporting. The results of operations for the three and nine months ended March 31, 2014 and 2013, are not necessarily indicative of the results for the full year. The Company believes that the disclosures are adequate to make the information presented not misleading.

These financial statements should be read in conjunction with the financial statements, accounting policies and financial notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2013. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments), which are necessary for a fair representation of financial results for the interim periods presented.

References to the Company refer to Net1 and its consolidated subsidiaries, unless the context otherwise requires. References to Net1 are references solely to Net 1 UEPS Technologies, Inc.

The Company has updated its accounting policy for the allowance for doubtful finance loans receivable as a result of the increase in its UEPS-based lending book which is included in finance loans receivable in its unaudited condensed consolidated balance sheet. The Company does not believe that an allowance for doubtful finance loans receivable is required for finance loans receivable as of June 30, 2013, because this was an established book and has been recovered. However, the profile of the loan book has changed due to the expansion of the UEPS-based lending book during the nine months ended March 31, 2014, and accordingly an allowance for doubtful finance loans receivable is deemed required by the Company.

Loan provisions and allowance for doubtful accounts receivable

UEPS-based lending

The Company's policy is to regularly review the ageing of outstanding amounts due from borrowers and adjust the provision based on management's estimate of the recoverability of finance loans receivable. The Company writes off UEPS-based loans and related service fees if a borrower is in arrears with repayments for more than three months or dies.

Recent accounting pronouncements adopted

In February 2013, the FASB issued guidance regarding *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. This guidance requires entities to present (either on the face of the statement of operations or in the notes) the effects on the line items of the statement of operations for amounts reclassified out of accumulated other comprehensive income. The guidance is effective for the Company beginning July 1, 2013 and is applied prospectively. The adoption of this guidance did not have a material impact on the Company's financial statements.

Recent accounting pronouncements not yet adopted as of March 31, 2014

In March 2013, the FASB issued guidance regarding *Parent's Accounting for the Cumulative Translation Adjustment Upon Derecognition of Certain Subsidiaries or Groups of Assets Within a Foreign Entity or of an Investment in a Foreign Entity*. This guidance requires that the parent release any related cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. The guidance is effective for the Company beginning July 1, 2014. Early adoption is permitted. The Company is currently evaluating the impact of this guidance on its financial statements on adoption.

2. Pre-funded social welfare grants receivable

Pre-funded social welfare grants receivable represents amounts pre-funded by the Company to certain merchants participating in the merchant acquiring system. The April 2014 payment service commenced on April 1, 2014, but the Company pre-funded certain merchants participating in the merchant acquiring system on the last day of March 2014.

3. Inventory

The Company's inventory comprised the following categories as of March 31, 2014 and June 30, 2013.

| | March 31, | | June 30, | |
|----------------|------------------|--------|-----------------|--------|
| | 2014 | | 2013 | |
| Finished goods | \$ | 10,491 | \$ | 12,222 |
| | \$ | 10,491 | \$ | 12,222 |

4. Settlement assets and settlement obligations

Settlement assets comprise (1) cash received from the South African government that the Company holds pending disbursement to beneficiaries of social welfare grants, (2) cash received from health care plans which the Company disburses to health care service providers once it adjudicates claims and (3) cash received from customers on whose behalf the Company processes payroll payments that the Company will disburse to customer employees, payroll-related payees and other payees designated by the customer.

Settlement obligations comprise (1) amounts that the Company is obligated to disburse to beneficiaries of social welfare grants, (2) amounts which are due to health care service providers after claims have been adjudicated and reconciled, provided that the Company shall have previously received such funds from health care plan customers and (3) amounts that the Company is obligated to pay to customer employees, payroll-related payees and other payees designated by the customer.

The balances at each reporting date may vary widely depending on the timing of the receipts and payments of these assets and obligations

5. Fair value of financial instruments and equity-accounted investments

Fair value of financial instruments

Risk management

The Company seeks to reduce its exposure to currencies other than the South African rand through a policy of matching, to the extent possible, assets and liabilities denominated in those currencies. In addition, the Company uses financial instruments in order to economically hedge its exposure to exchange rate and interest rate fluctuations arising from its operations. The Company is also exposed to equity price and liquidity risks as well as credit risks.

Currency exchange risk

The Company is subject to currency exchange risk because it purchases inventories that it is required to settle in other currencies, primarily the euro and US dollar. The Company uses forward contracts in order to limit its exposure in these transactions to fluctuations in exchange rates between the ZAR, on the one hand, and the US dollar and the euro, on the other hand.

The Company's outstanding foreign exchange contracts are as follows:

As of March 31, 2014

| Notional amount | | Strike price | | Fair market value price | | Maturity |
|------------------------|---------|---------------------|---------|--------------------------------|---------|-----------------|
| EUR | 192,375 | ZAR | 14.9984 | ZAR | 14.5664 | April 22, 2014 |

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| | | | | | | |
|-----|---------|-----|---------|-----|---------|--------------------|
| EUR | 192,375 | ZAR | 15.1351 | ZAR | 14.5664 | April 22, 2014 |
| EUR | 192,195 | ZAR | 15.2014 | ZAR | 14.6290 | May 20, 2014 |
| EUR | 192,195 | ZAR | 15.0637 | ZAR | 14.6290 | May 20, 2014 |
| EUR | 180,023 | ZAR | 15.2750 | ZAR | 14.7011 | June 20, 2014 |
| EUR | 180,023 | ZAR | 15.1349 | ZAR | 14.7011 | June 20, 2014 |
| EUR | 182,273 | ZAR | 15.2077 | ZAR | 14.7778 | July 21, 2014 |
| EUR | 182,273 | ZAR | 15.3488 | ZAR | 14.7778 | July 21, 2014 |
| EUR | 180,023 | ZAR | 15.4228 | ZAR | 14.8537 | August 20, 2014 |
| EUR | 180,023 | ZAR | 15.2819 | ZAR | 14.8537 | August 20, 2014 |
| EUR | 180,023 | ZAR | 15.3623 | ZAR | 14.9372 | September 22, 2014 |
| EUR | 180,023 | ZAR | 15.5041 | ZAR | 14.9372 | September 22, 2014 |

5. Fair value of financial instruments and equity-accounted investments (continued)**Fair value of financial instruments (continued)***Risk management (continued)**Currency exchange risk (continued)*

As of March 31, 2014 (continued)

| Notional amount | Strike price | Fair market value price | Maturity |
|-----------------|--------------|-------------------------|-------------------|
| EUR 181,571 | ZAR 15.5739 | ZAR 15.0122 | October 20, 2014 |
| EUR 181,571 | ZAR 15.4316 | ZAR 15.0122 | October 20, 2014 |
| EUR 180,023 | ZAR 15.6552 | ZAR 15.0976 | November 20, 2014 |
| EUR 180,023 | ZAR 15.5136 | ZAR 15.0976 | November 20, 2014 |
| EUR 180,023 | ZAR 15.5970 | ZAR 15.1859 | December 22, 2014 |
| EUR 180,023 | ZAR 15.7391 | ZAR 15.1859 | December 22, 2014 |
| EUR 174,425 | ZAR 15.8119 | ZAR 15.2688 | January 20, 2015 |
| EUR 174,425 | ZAR 15.6729 | ZAR 15.2688 | January 20, 2015 |

As of June 30, 2013

| Notional amount | Strike price | Fair market value price | Maturity |
|-----------------|--------------|-------------------------|--------------------|
| USD 4,000,000 | ZAR 9.0600 | ZAR 10.1397 | September 30, 2013 |

Translation risk

Translation risk relates to the risk that the Company's results of operations will vary significantly as the US dollar is its reporting currency, but it earns most of its revenues and incurs most of its expenses in ZAR. The US dollar to ZAR exchange rate has fluctuated significantly over the past two years. As exchange rates are outside the Company's control, there can be no assurance that future fluctuations will not adversely affect the Company's results of operations and financial condition.

Interest rate risk

As a result of its normal borrowing and leasing activities, the Company's operating results are exposed to fluctuations in interest rates, which it manages primarily through regular financing activities. The Company generally maintains limited investment in cash equivalents and has occasionally invested in marketable securities.

Credit risk

Credit risk relates to the risk of loss that the Company would incur as a result of non-performance by counterparties. The Company maintains credit risk policies with regard to its counterparties to minimize overall credit risk. These policies include an evaluation of a potential counterparty's financial condition, credit rating, and other credit criteria and risk mitigation tools as the Company's management deems appropriate.

With respect to credit risk on financial instruments, the Company maintains a policy of entering into such transactions only with South African and European financial institutions that have a credit rating of BBB or better, as determined by credit rating agencies such as Standard & Poor's, Moody's and Fitch Ratings.

UEPS-based microlending credit risk

The Company is exposed to credit risk in its UEPS-based microlending activities, which provides unsecured short-term loans to qualifying customers. The Company manages this risk by performing an affordability test for each prospective customer and assigns a creditworthiness score, which takes into account a variety of factors such as other debts and total expenditures on normal household and lifestyle expenses.

5. Fair value of financial instruments and equity-accounted investments (continued)

Fair value of financial instruments (continued)

Risk management (continued)

Equity price and liquidity risk

Equity price risk relates to the risk of loss that the Company would incur as a result of the volatility in the exchange-traded price of equity securities that it holds and the risk that it may not be able to liquidate these securities. The market price of these securities may fluctuate for a variety of reasons, consequently, the amount the Company may obtain in a subsequent sale of these securities may significantly differ from the reported market value.

Liquidity risk relates to the risk of loss that the Company would incur as a result of the lack of liquidity on the exchange on which these securities are listed. The Company may not be able to sell some or all of these securities at one time, or over an extended period of time without influencing the exchange traded price, or at all.

The following section describes the valuation methodologies the Company uses to measure its significant financial assets and liabilities at fair value.

In general, and where applicable, the Company uses quoted prices in active markets for identical assets or liabilities to determine fair value. This pricing methodology applies to Level 1 investments. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then the Company uses quoted prices for similar assets and liabilities or inputs other than the quoted prices that are observable either directly or indirectly. These investments are included in Level 2 investments. In circumstances in which inputs are generally unobservable, values typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models, and similar techniques. Investments valued using such techniques are included in Level 3 investments.

Asset measured at fair value using significant unobservable inputs investment in Finbond Group Limited (Finbond)

The Company's Level 3 asset represents an investment of 156,788,712 shares of common stock of Finbond, which are exchange-traded equity securities. Finbond's shares are traded on the JSE Limited (JSE) and the Company has designated such shares as available for sale investments. The Company has concluded that the market for Finbond shares is not active and consequently has employed alternative valuation techniques in order to determine the fair value of such stock. Currently, the operations of Finbond relate primarily to the provision of microlending products. In addition, it has a mutual banking licence and issues financial products under this licence. In determining the fair value of Finbond, the Company has considered amongst other things Finbond's historical financial information (including its most recent public accounts), press releases issued by Finbond and its published net asset value. The Company believes that the best indicator of fair value of Finbond is its published net asset value and has used this value to determine the fair value.

The fair value of these securities as of March 31, 2014, represented approximately 1% of the Company's total assets, including these securities.

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of March 31, 2014, according to the fair value hierarchy:

Quoted

| | Price in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|--|---|---|--|----------|
| Assets | | | | |
| Related to insurance business (included in other long-term assets): | | | | |
| Cash and cash equivalents | \$ 1,778 | \$ - | \$ - | \$ 1,778 |
| Investment in Finbond (available for sale assets included in other long-term assets) | - | - | 7,662 | 7,662 |
| Other | - | 138 | - | 138 |
| Total assets at fair value | \$ 1,778 | \$ 138 | \$ 7,662 | \$ 9,578 |

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5. Fair value of financial instruments and equity-accounted investments (continued)

| | Quoted Price in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|---------------------------------|---|---|--|--------|
| Liabilities | | | | |
| Foreign exchange contracts | \$ - | \$ 170 | \$ - | \$ 170 |
| Total liabilities at fair value | \$ - | \$ 170 | \$ - | \$ 170 |

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of June 30, 2013, according to the fair value hierarchy:

| | Quoted Price in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|--|---|---|--|-----------|
| Assets | | | | |
| Related to insurance business (included in other long-term assets): | | | | |
| Cash and cash equivalents | \$ 1,833 | \$ - | \$ - | \$ 1,833 |
| Investment in Finbond (available for sale assets included in other long-term assets) | - | - | 8,303 | 8,303 |
| Other | - | 147 | - | 147 |
| Total assets at fair value | \$ 1,833 | \$ 147 | \$ 8,303 | \$ 10,283 |
| Liabilities | | | | |
| Foreign exchange contracts | \$ - | \$ 436 | \$ - | \$ 436 |
| Total liabilities at fair value | \$ - | \$ 436 | \$ - | \$ 436 |

Changes in the Company's investment in Finbond (Level 3 that are measured at fair value on a recurring basis) were insignificant during the three and nine months ended March 31, 2014 and 2013, respectively. There have been no transfers in or out of Level 3 during the three and nine months ended March 31, 2014 and 2013, respectively.

Assets and liabilities measured at fair value on a nonrecurring basis

The Company measures its assets at fair value on a nonrecurring basis when they are deemed to be other-than-temporarily impaired. The Company has no liabilities that are measured at fair value on a nonrecurring basis. The Company reviews the carrying values of its assets when events and circumstances warrant and considers all available evidence in evaluating when declines in fair value are other-than-temporary.

The fair values of the Company's assets are determined using the best information available, and may include quoted market prices, market comparables, and discounted cash flow projections. An impairment charge is recorded when the cost of the assets exceeds its fair value and the excess is determined to be other-than-temporary. The Company has not recorded any impairment charges during the reporting periods presented herein.

6. Goodwill and intangible assets**Goodwill**

Summarized below is the movement in the carrying value of goodwill for the nine months ended March 31, 2014:

| | Gross value | Accumulated impairment | Carrying value |
|--|--------------------|-------------------------------|-----------------------|
| Balance as of June 30, 2013 | \$ 218,558 | \$ (42,752) | \$ 175,806 |
| Foreign currency adjustment ⁽¹⁾ | 6,032 | (2,006) | 4,026 |
| Balance as of March 31, 2014 | \$ 224,590 | \$ (\$44,758) | \$ 179,832 |

(1) the foreign currency adjustment represents the effects of the fluctuations between the South African rand and the Korean won, and the US dollar on the carrying value.

Goodwill has been allocated to the Company's reportable segments as follows:

| | As of March 31, 2014 | As of June 30, 2013 |
|---|-----------------------------|----------------------------|
| SA transaction-based activities | \$ 28,532 | \$ 30,525 |
| International transaction-based activities | 121,656 | 113,972 |
| Smart card accounts | - | - |
| Financial services | - | - |
| Hardware, software and related technology sales | 29,644 | 31,309 |
| Total | \$ 179,832 | \$ 175,806 |

Intangible assets***Carrying value and amortization of intangible assets***

Summarized below is the carrying value and accumulated amortization of the intangible assets as of March 31, 2014 and June 30, 2013:

| | As of March 31, 2014 | | | As of June 30, 2013 | | |
|--------------------------------------|-----------------------------|---------------------------------|---------------------------|-----------------------------|---------------------------------|---------------------------|
| | Gross carrying value | Accumulated amortization | Net carrying value | Gross carrying value | Accumulated amortization | Net carrying value |
| Finite-lived intangible assets: | | | | | | |
| Customer relationships | \$ 94,309 | \$ (37,373) | \$ 56,936 | \$ 90,469 | \$ (29,818) | \$ 60,651 |
| Software and unpatented technology | 35,851 | (27,512) | 8,339 | 34,951 | (22,151) | 12,800 |
| FTS patent | 3,620 | (3,620) | - | 3,873 | (3,873) | - |
| Exclusive licenses | 4,506 | (4,506) | - | 4,506 | (4,506) | - |
| Trademarks | 6,671 | (2,681) | 3,990 | 6,611 | (2,805) | 3,806 |
| Customer database | 574 | (574) | - | 614 | (614) | - |
| Total finite-lived intangible assets | \$ 145,531 | \$ (76,266) | \$ 69,265 | \$ 141,024 | \$ (63,767) | \$ 77,257 |

Aggregate amortization expense on the finite-lived intangible assets for the three and nine months ended March 31, 2014, was approximately \$4.6 million and \$12.5 million, respectively (three and nine months ended March

31, 2013, was approximately \$4.4 million and \$14.0 million, respectively).

Future estimated annual amortization expense for the next five fiscal years and thereafter, assuming exchange rates prevailing on March 31, 2014, is presented in the table below. Actual amortization expense in future periods could differ from this estimate as a result of acquisitions, changes in useful lives, exchange rate fluctuations and other relevant factors.

| | | |
|------------|----|--------|
| 2014 | \$ | 16,229 |
| 2015 | | 15,080 |
| 2016 | | 11,280 |
| 2017 | | 8,958 |
| 2018 | | 8,958 |
| Thereafter | \$ | 20,671 |
| | | 12 |

7. Reinsurance assets and policy holder liabilities under insurance and investment contracts**Reinsurance assets and policy holder liabilities under insurance contracts**

Summarized below is the movement in reinsurance assets and policy holder liabilities under insurance contracts during the nine months ended March 31, 2014:

| | Reinsurance assets (1) | Insurance contracts (2) |
|--|-----------------------------------|------------------------------------|
| Balance as of June 30, 2013 | \$ 19,557 | \$ (19,711) |
| Foreign currency adjustment ⁽³⁾ | (1,276) | 1,287 |
| Balance as of March 31, 2014 | \$ 18,281 | \$ (18,424) |

- (1) Included in other long-term assets.
- (2) Included in other long-term liabilities.
- (3) The foreign currency adjustment represents the effects of the fluctuations between the ZAR against the US dollar.

The Company has agreements with reinsurance companies in order to limit its losses from large insurance contracts, however, if the reinsurer is unable to meet its obligations, the Company retains the liability.

The value of insurance contract liabilities is based on best estimates assumptions of future experience plus prescribed margins, as required in the markets in which these products are offered, namely South Africa. The process of deriving the best estimates assumptions plus prescribed margins includes assumptions related to future mortality and morbidity (an appropriate base table of standard mortality is chosen depending on the type of contract and class of business), withdrawals (based on recent withdrawal investigations and expected future trends), investment returns (based on government treasury rates adjusted by an applicable margin), expense inflation (based on a 10 year real return on CPI-linked government bonds from the risk-free rate and adding an allowance for salary inflation and book shrinkage of 1% per annum) and claim reporting delays (based on average industry experience).

Assets and policy holder liabilities under investment contracts

Summarized below is the movement in assets and policy holder liabilities under investment contracts during the nine months ended March 31, 2014:

| | Assets (1) | Investment contracts (2) |
|--|-------------------|-------------------------------------|
| Balance as of June 30, 2013 | \$ 953 | \$ (953) |
| Foreign currency adjustment ⁽³⁾ | (62) | 62 |
| Balance as of March 31, 2014 | \$ 891 | \$ (891) |

- (1) Included in other long-term assets.
- (2) Included in other long-term liabilities.
- (3) The foreign currency adjustment represents the effects of the fluctuations between the ZAR against the US dollar.

The Company does not offer any investment products with guarantees related to capital or returns.

8. Short-term credit facility South Africa

The Company's short-term South African credit facility with Nedbank Limited comprises an overdraft facility of up to ZAR 250 million and indirect and derivative facilities of up to ZAR 150 million, which include letters of guarantee, letters of credit and forward exchange contracts. The Company temporarily increased its overdraft facility

to ZAR 500 million for the four months to March 31, 2014, after which it reverted back to ZAR 250 million. As of March 31, 2014, the interest rate on the overdraft facility was 7.85% . The Company has ceded its investment in Cash Paymaster Services Proprietary Limited (CPS), a wholly owned South African subsidiary, as security for its repayment obligations under the facility. A commitment fee of 0.35% per annum is payable on the monthly unutilized amount of the overdraft portion of the short-term facility. The Company is required to comply with customary non-financial covenants, including, without limitation, covenants that restrict the Company's ability to dispose of or encumber its assets, incur additional indebtedness or engage in certain business combinations. As of March 31, 2014, the Company had not utilized any of its ZAR 250.0 million (\$23.6 million, translated at exchange rates applicable as of March 31, 2014) overdraft facility. The Company had utilized approximately ZAR 143.1 million (\$13.5 million, translated at exchange rates applicable as of March 31, 2014) of its facility to enable the bank to issue guarantees, including stand-by letters of credit, in order for the Company to honor its obligations to third parties requiring such guarantees (Refer to Note 17). As of June 30, 2013, the Company had utilized none of this facility.

8. Short-term credit facility Korea

The Company obtained a KRW 10 billion short-term overdraft facility from Hana Bank, a Korean bank, in January 2014. As of March 31, 2014, the interest rate on the overdraft facility was 4.98% . The Company has ceded the warehouse it owns in Korea as security for its repayment obligations under the facility. As of March 31, 2014, the Company had not utilized any of its KRW 10.0 billion (\$9.3 million, translated at exchange rates applicable as of March 31, 2014) overdraft facility. The facility expires in January 2015.

9. Long-term borrowings

In October 2013, the Company refinanced its existing long-term Korean credit facility and signed a new five-year senior secured facilities agreement (the Facilities Agreement) with a consortium of Korean banks. The Facilities Agreement provides for three separate facilities to the Company's wholly owned subsidiary, Net1 Applied Technologies Korea (Net1 Korea): a Facility A loan of up to KRW 60.0 billion (\$56.0 million), a Facility B loan of up to KRW 15 billion (\$14.0 million) and a Facility C revolving credit facility of up to KRW 10.0 billion (\$9.3 million) (all facilities denominated in KRW and translated at exchange rates applicable as of March 31, 2014).

The Facility A and B loans were fully drawn on October 29, 2013, and used to repay KRW 75.0 billion (\$70.6 million) of the KRW 92.4 billion (\$87.0 million) loan outstanding under the existing facility. The remaining outstanding KRW 17.4 billion (\$16.4 million) balance of that facility was paid from cash on hand on October 29, 2013. In addition, the Company drew KRW 1.1 billion (\$1.0 million) of the revolving credit facility on October 29, 2013, to pay fees and expenses related to the Facilities Agreement and drew a further KRW 1.1 billion (\$1.0 million) in January 2014 to pay interest due under the Facilities Agreement.

Interest on the loans and revolving credit facility is payable quarterly and is based on the Korean CD rate in effect from time to time plus a margin of 3.10% for the Facility A loan and Facility C revolving credit facility; and a margin of 2.90% for the Facility B loan. The CD rate was 2.65% on March 31, 2014 and therefore the interest rate in effect as of March 31, 2014, for the Facility A loan and Facility C revolving credit facility was 5.75% and for the Facility B loan was 5.55%, respectively. The Company paid facilities fees of approximately KRW 0.9 billion on October 29, 2013 and amortized approximately \$0.1 million and \$0.6 million, respectively, during the three and nine months ended March 31, 2014. A commitment fee of 0.3% is payable on any un-drawn and un-cancelled amount of the revolving credit facility. Total interest expense related to the new and refinanced facilities during the three and nine months ended March 31, 2014 and 2013, was \$1.1 million and \$3.7 million; and \$1.7 million and \$5.3 million, respectively.

The Facility A loan is repayable in three scheduled annual installments of KRW 10 billion each beginning 30 months after initial drawdown and one final installment of KRW 30 billion on the maturity date, namely October 29, 2018. The Facility B loan is repayable in full on October 29, 2014. The Facility C revolving credit facility is repayable in full on the maturity date. Prepayment of the revolving credit facility may be withdrawn at any time up to three months before the maturity date.

The loans under the Facilities Agreement are secured by a pledge by Net1 Korea of its entire equity interest in KSNET and a pledge by the immediate parent of Net1 Korea (also one of the Company's subsidiaries) of its entire equity interest in Net1 Korea. The Facilities Agreement contains customary covenants that require Net1 Korea to maintain agreed leverage and debt service coverage ratios and restricts Net1 Korea's ability to make certain distributions with respect to its capital stock, prepay other debt, encumber its assets, incur additional indebtedness, or engage in certain business combinations. The loans under the Facilities Agreement are without recourse to, and the covenants and other agreements contained therein do not apply to, the Company or any of the Company's subsidiaries (other than Net1 Korea).

The Company's refinanced KRW 92.4 billion Korean senior secured loan facility is described in Note 13 to the Company's audited consolidated financial statements included in its Annual Report on Form 10-K for the year ended June 30, 2013. The Company has expensed the remaining prepaid facility fees related to the refinanced facility of approximately \$0.4 million during the nine months ended March 31, 2014. The third scheduled repayment related to this refinanced facility of \$7.3 million was paid on October 29, 2012.

10. Capital structure

The following table presents reconciliation between the number of shares, net of treasury, presented in the consolidated statement of changes in equity during the nine months ended March 31, 2014 and 2013, respectively, and the number of shares, net of treasury, excluding non-vested equity shares that have not vested during the nine months ended March 31, 2014 and 2013, respectively:

| | Nine months ended March 31, | |
|---|--------------------------------|------------|
| | 2014 | 2013 |
| Number of shares, net of treasury: | | |
| Statement of changes in equity | 45,783,342 | 45,600,471 |
| Less: Non-vested equity shares that have not vested | (385,778) | (461,417) |
| Number of shares, net of treasury excluding non-vested equity shares that have not vested | 45,397,564 | 45,139,054 |

December 2013 Black Economic Empowerment transactions

On December 10, 2013, the Company entered into definitive agreements relating to two Black Economic Empowerment (BEE) transactions. As of March 31, 2014, the transactions had not been implemented because the agreed conditions had not been satisfied. Subsequently, the conditions were satisfied and the transactions were implemented on April 16, 2014.

Pursuant to these Relationship Agreements between the Company and its BEE partners, the Company sold an aggregate of 4,400,000 shares of its common stock (BEE shares) for a purchase price of ZAR 60.00 per share. The ZAR 60.00 per share purchase price for the BEE shares, which are contractually restricted as to resale as described below, was paid in ZAR and represents 75% of the closing price of the Company's common stock on the JSE on December 6, 2013, the date the Company completed final negotiation of the terms of these BEE transactions.

The Relationship Agreements provided that the entire purchase price for the BEE shares be financed through a five-year loan to be extended to each of the BEE partners by a South African subsidiary of the Company. The obligations of the BEE partners under the loans are several, and not joint. Each of the BEE partners granted the lender a security interest in all the BEE shares purchased by such BEE partner to secure the repayment of its loan. The principal amount of the loans being made by the subsidiary was contributed by Net1 to the equity capital of the subsidiary. As a result of the making of the loans, the net cash position of the Company after the sale of the BEE shares remained unchanged.

The loans bear interest at a rate equal to the Johannesburg Interbank Rate (638 basis points as of March 31, 2014) plus 300 basis points. Interest on the loans is payable semi-annually in arrears on January 1 and July 1 of each year. 10% of the outstanding principal amount of the loans will be payable on each of the first and second anniversaries of the date of issuance of the BEE shares, 15% of the outstanding principal amount of the loans will be payable on each of the third and fourth anniversaries of the date of issuance of the BEE shares and the remaining outstanding principal amount of the loans will be payable on the fifth anniversary of the date of issuance of the BEE shares. Further, the entire outstanding principal amount of the loans will be payable if the price of the Company's common stock on the JSE equals or exceeds ZAR 120.00 per share at any time during term of the loans. Upon the occurrence of certain trigger events with respect to a BEE partner, the BEE shares held by that BEE partner may be repurchased by the Company or one of its designees. These trigger events include the following:

- failure by the BEE partner to pay any amount due on its loan (including interest) to the lender (in this case, the Company may repurchase only that number of shares which would raise sufficient funds to settle any amount

due and unpaid);

- any other breach by the BEE partner (or in certain circumstances its shareholders) of any provision of the Relationship Agreement, including without limitation, its failure to maintain its BEE status;
- the Company's common stock trades at or below ZAR 60.00 on the JSE or at or below the equivalent trading price on Nasdaq;
- the occurrence of certain insolvency events or liquidation proceedings affecting the BEE partner; or
- the BEE partner fails to satisfy any judgment or arbitration award granted or made against it within 7 days.

10. Capital structure (continued)**December 2013 Black Economic Empowerment transactions (continued)**

If the trigger event involves a failure by a BEE partner to pay any amount due on its loan, then the repurchase price is the volume-weighted average price of the Company's common stock on the Nasdaq for the period of 30 trading days prior to the trigger event, or 30-day VWAP. In the case of other trigger events, the repurchase price is the lower of the 30-day VWAP or ZAR 60.00 per share.

The BEE shares are contractually restricted as to resale for a period of five years from the date of issuance, with the exception of periodic sales which may be made to fund the repayment of principal and interest on the loans. In addition, the Company may call the BEE shares then owned by the BEE partners, either in exchange for a minority interest in CPS or for a cash payment equal to the 30-day VWAP. Further, after the fifth anniversary of the date of issuance of the BEE shares, the Company will have a right of first refusal on the shares owned by the BEE partners.

The loans to the BEE partners do not provide that they are recourse only to the BEE shares. Nevertheless, the Company expects that the sole source of repayment of the loans will be proceeds from the sale of its shares by the BEE partners from time to time, in open market or in privately negotiated transactions.

Acquisition of KSNET non-controlling interests

The Company acquired all of the issued share capital of KSNET, Inc. that it did not previously own for approximately \$2.0 million in cash. The Company intends to realize certain Korean tax efficiencies in the future and is currently discussing the feasibility with its Korean tax advisors. The transaction was accounted for as an equity transaction with a non-controlling interest and accordingly, no gain or loss was recognized in the Company's consolidated statement of operations. The carrying amount of the non-controlling interest was adjusted to reflect the change in ownership interest in KSNET. The difference between the fair value of the consideration paid and the amount by which the non-controlling interest was adjusted, of \$1.5 million, was recognized in equity attributable to Net1.

11. Accumulated other comprehensive (loss) income

The table below presents the change in accumulated other comprehensive (loss) income per component during the nine months ended March 31, 2014:

| | | | | | Nine months ended March 31, 2014 Net unrealized income (loss) on asset available for sale, net of tax | Total |
|--|----|---|------------|-----|--|--------------|
| | | Foreign currency translation reserve | 000 | | 000 | 000 |
| Balance as of June 30, 2013 | \$ | (101,188) | \$ | 330 | \$ | (100,858) |
| Movement in foreign currency translation reserve | | 2,660 | | - | | 2,660 |

| | | | | |
|--|----|----------|-----|-------------|
| Unrealized loss on asset available for sale, | | | | |
| net of | | | | |
| tax of \$112 | | | | |
| | | - | 288 | 288 |
| Balance as of March 31, 2014 | \$ | (98,528) | \$ | 618 |
| | | | | \$ (97,910) |

There were no reclassifications from accumulated other comprehensive loss to comprehensive (loss) income during the nine months ended March 31, 2014 or 2013, respectively.

12. Stock-based compensation**Stock option and restricted stock activity***Options*

The following table summarizes stock option activity for the nine months ended March 31, 2014 and 2013:

| | | Number of shares | Weighted average exercise price (\$) | Weighted Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (\$ 000) | Weighted Average Grant Date Fair Value (\$) |
|---------------------|----------------|-----------------------------|---|---|---|--|
| Outstanding | June 30, 2013 | 2,648,583 | 15.15 | 5.98 | 313 | |
| Granted under Plan: | August 2013 | 224,896 | 7.35 | 10.00 | 568 | 2.53 |
| Exercised | | (10,000) | 8.75 | | 12 | |
| Forfeited | | (136,420) | 23.51 | | | |
| Outstanding | March 31, 2014 | 2,727,059 | 14.12 | 5.63 | 2,290 | |
| Outstanding | June 30, 2012 | 2,247,583 | 16.28 | 6.43 | 602 | |
| Granted under Plan: | August 2012 | 431,000 | 8.75 | 10.00 | 1,249 | 2.90 |
| Exercised | | (30,000) | 7.98 | | 24 | |
| Outstanding | March 31, 2013 | 2,648,583 | 15.15 | 6.74 | 978 | |

The fair value of each option is estimated on the date of grant using the Cox Ross Rubinstein binomial model that uses the assumptions noted in the following table. The estimated expected volatility is calculated based on the Company's 250 day volatility. The estimated expected life of the option was determined based historical behavior of employees who were granted options with similar terms. The Company has estimated no forfeitures for options awarded in August 2013 and 2014, respectively. The table below presents the range of assumptions used to value options granted during the three and nine months ended March 31, 2014 and 2013:

| | Three and nine months ended March 31, | |
|--------------------------|--|-------------|
| | 2014 | 2013 |
| Expected volatility | 50% | 49% |
| Expected dividends | 0% | 0% |
| Expected life (in years) | 3 | 3 |
| Risk-free rate | 0.9% | 0.3% |

During the three and nine months ended March 31, 2014, terminated employees forfeited 136,420 stock options. There were no forfeitures during the three and nine months ended March 31, 2013.

The following table presents stock options vesting and expecting to vest as of March 31, 2014:

| | Number of shares | Weighted average exercise price (\$) | Weighted Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (\$ 000) |
|--|-----------------------------|---|---|---|
| | 2,727,059 | 14.12 | 5.63 | 2,290 |

Vested and expecting to vest March 31,
2014

These options have an exercise price range of \$6.59 to \$24.46.

12. Stock-based compensation (continued)**Stock option and restricted stock activity (continued)***Options (continued)*

| | Number of shares | Weighted average exercise price (\$) | Weighted Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (\$ 000) |
|-------------|-----------------------------|---|---|---|
| Exercisable | 1,998,497 | 16.08 | 4.80 | 1,057 |

During each of the three months ended March 31, 2014 and 2013, respectively, no stock options became exercisable. During the nine months ended March 31, 2014 and 2013, respectively, 358,333 and 244,666 stock options became exercisable. Included in the 244,666 stock options are 30,000 stock options with respect to which the Remuneration Committee of the Board agreed to accelerate vesting, in August 2012, prior to the resignation of a non-employee director. During the three and nine months ended March 31, 2014, the Company received approximately \$0.1 million from 10,000 stock options exercised. During the nine months ended March 31, 2013, the Company received approximately \$0.2 million from 30,000 stock options exercised by the non-employee director that resigned. No stock options were exercised during the three months ended March 31, 2013. The Company issues new shares to satisfy stock option exercises.

Restricted stock

The following table summarizes restricted stock activity for the nine months ended March 31, 2014 and 2013:

| | Number of Shares of Restricted Stock | Weighted Average Grant Date Fair Value (\$ 000) |
|---------------------------|---|--|
| Non-vested June 30, 2013 | 405,226 | 4,393 |
| Granted August 2013 | 187,963 | 1,382 |
| Vested August 2013 | (16,907) | 161 |
| Vested February 2014 | (183,333) | 1,742 |
| Forfeitures October 2013 | (7,171) | 84 |
| Non-vested March 31, 2014 | 385,778 | 3,534 |
| Non-vested June 30, 2012 | 646,617 | 7,061 |
| Granted August 2012 | 21,569 | 189 |
| Granted February 2013 | (183,333) | 1,016 |
| Vested August 2012 | (23,436) | 216 |
| Non-vested March 31, 2013 | 461,417 | 4,988 |

The fair value of restricted stock vesting during the three months ended March 31, 2014 and 2013, respectively, was \$1.7 million and \$1.0 million. The fair value of restricted stock vesting during the nine months ended March 31, 2014 and 2013, respectively, was \$1.9 million and \$1.2 million. A non-employee director resigned during the nine months ended March 31, 2014, and forfeited 7,171 shares of restricted stock. Included in the 23,436 shares of restricted stock that vested in August 2012 are 8,547 shares with respect to which the Remuneration Committee of the Board agreed to accelerate vesting prior to the resignation of a non-employee director.

The fair value of restricted stock is based on the closing price of the Company's stock quoted on The Nasdaq Global Select Market on the date of grant.

12. Stock-based compensation (continued)**Stock-based compensation charge and unrecognized compensation cost**

The Company has recorded a stock compensation charge of \$0.9 million and \$1.1 million for the three months ended March 31, 2014 and 2013, respectively, which comprised:

| | | Total charge | Allocated to cost of goods sold, IT processing, servicing and support | Allocated to selling, general and administration |
|--|-----------|-------------------------|--|---|
| Three months ended March 31, 2014 | | | | |
| Stock-based compensation charge | \$ | 922 | \$ - | \$ 922 |
| Total three months ended March 31, 2014 | \$ | 922 | \$ - | \$ 922 |
| Three months ended March 31, 2013 | | | | |
| Stock-based compensation charge | \$ | 1,092 | \$ - | \$ 1,092 |
| Total three months ended March 31, 2013 | \$ | 1,092 | \$ - | \$ 1,092 |

The Company has recorded a stock compensation charge of \$2.8 million and \$3.3 million for the nine months ended March 31, 2014 and 2013, respectively, which comprised:

| | | Total charge | Allocated to cost of goods sold, IT processing, servicing and support | Allocated to selling, general and administration |
|---|-----------|-------------------------|--|---|
| Nine months ended March 31, 2014 | | | | |
| Stock-based compensation charge | \$ | 2,826 | \$ - | \$ 2,826 |
| Reversal of stock compensation charge related to restricted stock forfeited | | (6) | - | (6) |
| Total nine months ended March 31, 2014 | \$ | 2,820 | \$ - | \$ 2,820 |
| Nine months ended March 31, 2013 | | | | |
| Stock-based compensation charge | \$ | 3,325 | \$ - | \$ 3,325 |
| Total nine months ended March 31, 2013 | \$ | 3,325 | \$ - | \$ 3,325 |

The stock-based compensation charges have been allocated to selling, general and administration based on the allocation of the cash compensation paid to the employees.

As of March 31, 2014, the total unrecognized compensation cost related to stock options was approximately \$1.1 million, which the Company expects to recognize over approximately three years. As of March 31, 2014, the total unrecognized compensation cost related to restricted stock awards was approximately \$3.0 million, which the Company expects to recognize over approximately two years.

As of each of March 31, 2014 and June 30, 2013, respectively, the Company has recorded a deferred tax asset of approximately \$1.5 million related to the stock-based compensation charge recognized related to employees and directors of Net1 as it is able to deduct the grant date fair value for taxation purposes in the United States.

13. Earnings per share

Basic earnings per share include shares of restricted stock that meet the definition of a participating security because these shares are eligible to receive non-forfeitable dividend equivalents at the same rate as common stock. Basic earnings per share have been calculated using the two-class method and basic earnings per share for the three and nine months ended March 31, 2014 and 2013, reflects only undistributed earnings. The computation below of basic earnings per share excludes the net income attributable to shares of unvested restricted stock (participating non-vested restricted stock) from the numerator and excludes the dilutive impact of these unvested shares of restricted stock from the denominator.

13. Earnings per share (continued)

Diluted earnings per share has been calculated to give effect to the number of shares of additional common stock that would have been outstanding if the potential dilutive instruments had been issued in each period. Stock options are included in the calculation of diluted earnings per share utilizing the treasury stock method and are not considered to be participating securities as the stock options do not contain non-forfeitable dividend rights. The calculation of diluted earnings per share includes the dilutive effect of a portion of the restricted stock granted to employees in February 2012 and August 2013 as these shares of restricted stock are considered contingently returnable shares for the purposes of the diluted earnings per share calculation and the vesting conditions in respect of a portion of the restricted stock had been satisfied. The vesting conditions are discussed in Note 17 to the Company's audited consolidated financial statements included in its Annual Report on Form 10-K for the year ended June 30, 2013.

The following table presents net income attributable to Net1 (income from continuing operations) and the share data used in the basic and diluted earnings per share computations using the two-class method:

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|--|------------|--|----------|
| | 2014 | 2013 | 2014 | 2013 |
| | (in thousands except percent and per share data) | | (in thousands except percent and per share data) | |
| Numerator: | | | | |
| Net income (loss) attributable to Net1 | \$ 17,182 | \$ (4,681) | \$ 41,527 | \$ 4,692 |
| Undistributed earnings (loss) | 17,182 | (4,681) | 41,527 | 4,692 |
| Percent allocated to common shareholders (Calculation 1) | 99% | 99% | 99% | 99% |
| Numerator for earnings (loss) per share: basic and diluted | \$ 16,944 | \$ (4,634) | \$ 40,917 | \$ 4,637 |
| Denominator: | | | | |
| Denominator for basic earnings per share: weighted-average | | | | |
| common shares outstanding | 45,142 | 45,098 | 45,070 | 45,018 |
| Effect of dilutive securities: | | | | |
| Performance shares related to acquisition | - | 16 | - | 5 |
| Stock options | 91 | 26 | 106 | 37 |
| Denominator for diluted earnings per share: adjusted weighted average common shares outstanding and assumed conversion | 45,233 | 45,140 | 45,176 | 45,060 |
| Earnings (loss) per share: | | | | |
| Basic | \$ 0.38 | \$ (0.10) | \$ 0.91 | \$ 0.10 |
| Diluted | \$ 0.37 | \$ (0.10) | \$ 0.90 | \$ 0.10 |
| (Calculation 1) | | | | |
| | 45,142 | 45,098 | 45,070 | 45,018 |

| | | | | |
|--|--------|--------|--------|--------|
| Basic weighted-average common shares outstanding (A) | | | | |
| Basic weighted-average common shares outstanding and unvested restricted shares expected to vest (B) | 45,776 | 45,557 | 45,742 | 45,552 |
| Percent allocated to common shareholders (A) / (B) | 99% | 99% | 99% | 99% |

Options to purchase 2,040,339 shares of the Company's common stock at prices ranging from \$7.35 to \$24.46 per share were outstanding during the three and nine months ended March 31, 2014, but were not included in the computation of diluted earnings per share because the options' exercise price were greater than the average market price of the Company's common shares. The options, which expire at various dates through August 21, 2023, were still outstanding as of March 31, 2014.

14. Supplemental cash flow information

The following table presents the supplemental cash flow disclosures for the three and nine months ended March 31, 2014 and 2013:

| | Three months ended March 31, | | Nine months ended March 31, | |
|-----------------------------|---|-------------|--|-------------|
| | 2014 | 2013 | 2014 | 2013 |
| Cash received from interest | \$ 3,422 | \$ 2,395 | \$ 9,886 | \$ 8,104 |
| Cash paid for interest | \$ 1,651 | \$ 2,020 | \$ 5,317 | \$ 6,073 |
| Cash paid for income taxes | \$ 1,570 | \$ 1,701 | \$ 16,097 | \$ 12,180 |

15. Operating segments

The Company discloses segment information as reflected in the management information systems reports that its chief operating decision maker uses in making decisions and to report certain entity-wide disclosures about products and services, major customers, and the countries in which the entity holds material assets or reports material revenues. A description of the Company's operating segments is contained in Note 22 to the Company's audited consolidated financial statements included in its Annual Report on Form 10-K for the year ended June 30, 2013.

The following tables summarize segment information which is prepared in accordance with GAAP:

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|---|-------------|--|-------------|
| | 2014 | 2013 | 2014 | 2013 |
| Revenues from external customers | | | | |
| SA transaction-based activities | \$ 64,864 | \$ 59,009 | \$ 200,133 | \$ 181,137 |
| International transaction-based activities | 34,994 | 33,119 | 109,099 | 97,881 |
| Smart card accounts | 10,612 | 8,657 | 33,178 | 25,240 |
| Financial services | 11,099 | 1,651 | 19,725 | 4,483 |
| Hardware, software and related technology sales | 16,557 | 8,705 | 36,768 | 25,524 |
| Total | 138,126 | 111,141 | 398,903 | 334,265 |
| Inter-company revenues | | | | |
| SA transaction-based activities | 3,433 | 1,492 | 8,665 | 9,360 |
| International transaction-based activities | - | - | - | - |
| Smart card accounts | - | - | - | - |
| Financial services | 259 | 308 | 784 | 1,095 |
| Hardware, software and related technology sales | 76 | 135 | 595 | 722 |
| Total | 3,768 | 1,935 | 10,044 | 11,177 |
| Operating income (loss) | | | | |
| SA transaction-based activities | 11,145 | (4,197) | 37,825 | 4,136 |
| International transaction-based activities | 1,322 | (1,362) | 4,738 | (1,331) |
| Smart card accounts | 3,025 | 2,467 | 9,456 | 7,194 |
| Financial services | 5,119 | 1,147 | 6,902 | 3,292 |
| Hardware, software and related technology sales | 4,000 | 1,699 | 8,540 | 4,478 |
| Subtotal: Operating segments | 24,611 | (246) | 67,461 | 17,769 |
| Corporate/Eliminations | (662) | (4,480) | (8,310) | (8,198) |
| Total | 23,949 | (4,726) | 59,151 | 9,571 |

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| | | | | |
|---|----------|----------|----------|----------|
| Interest income | | | | |
| SA transaction-based activities | - | - | - | - |
| International transaction-based activities | - | - | - | - |
| Smart card accounts | - | - | - | - |
| Financial services | - | - | - | - |
| Hardware, software and related technology sales | - | - | - | - |
| Subtotal: Operating segments | - | - | - | - |
| Corporate/Eliminations | 3,438 | 2,515 | 9,993 | 8,195 |
| Total | \$ 3,438 | \$ 2,515 | \$ 9,993 | \$ 8,195 |
| 21 | | | | |

15. Operating segments (continued)

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|---|-------------|--|-------------|
| | 2014 | 2013 | 2014 | 2013 |
| Interest expense | | | | |
| SA transaction-based activities | \$ 28 | \$ 244 | \$ 71 | \$ 589 |
| International transaction-based activities | 2 | - | 46 | - |
| Smart card accounts | - | - | - | - |
| Financial services | 418 | - | 807 | - |
| Hardware, software and related technology sales | 181 | 81 | 540 | 207 |
| Subtotal: Operating segments | 629 | 325 | 1,464 | 796 |
| Corporate/Eliminations | 1,105 | 1,698 | 4,248 | 5,321 |
| Total | 1,734 | 2,023 | 5,712 | 6,117 |
| Depreciation and amortization | | | | |
| SA transaction-based activities | 2,895 | 3,198 | 7,827 | 9,628 |
| International transaction-based activities | 7,364 | 7,049 | 21,834 | 20,753 |
| Smart card accounts | - | - | - | - |
| Financial services | 115 | 163 | 348 | 347 |
| Hardware, software and related technology sales | 68 | 150 | 236 | 323 |
| Subtotal: Operating segments | 10,442 | 10,560 | 30,245 | 31,051 |
| Corporate/Eliminations | - | - | - | - |
| Total | 10,442 | 10,560 | 30,245 | 31,051 |
| Income taxation expense (benefit) | | | | |
| SA transaction-based activities | 3,113 | (1,245) | 10,571 | 991 |
| International transaction-based activities | 17 | (587) | 661 | (1,167) |
| Smart card accounts | 848 | 691 | 2,647 | 2,014 |
| Financial services | 1,320 | 327 | 1,723 | 937 |
| Hardware, software and related technology sales | 1,095 | 409 | 2,097 | 1,039 |
| Subtotal: Operating segments | 6,393 | (405) | 17,699 | 3,814 |
| Corporate/Eliminations | 2,142 | 877 | 4,420 | 3,358 |
| Total | 8,535 | 472 | 22,119 | 7,172 |
| Net income (loss) attributable to Net1 | | | | |
| SA transaction-based activities | 8,003 | (3,199) | 27,182 | 2,552 |
| International transaction-based activities | 1,591 | (642) | 4,577 | 193 |
| Smart card accounts | 2,177 | 1,776 | 6,808 | 5,178 |
| Financial services | 3,394 | 839 | 4,432 | 2,409 |
| Hardware, software and related technology sales | 2,729 | 1,210 | 5,912 | 3,239 |
| Subtotal: Operating segments | 17,894 | (16) | 48,911 | 13,571 |
| Corporate/Eliminations | (712) | (4,665) | (7,384) | (8,879) |
| Total | 17,182 | (4,681) | 41,527 | 4,692 |
| Expenditures for long-lived assets | | | | |

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| | | | | |
|---|----------|----------|-----------|-----------|
| SA transaction-based activities | 302 | 2,583 | 2,601 | 7,552 |
| International transaction-based activities | 4,231 | 2,074 | 13,744 | 8,844 |
| Smart card accounts | - | - | - | - |
| Financial services | 222 | 357 | 408 | 629 |
| Hardware, software and related technology sales | 93 | 39 | 556 | 78 |
| Subtotal: Operating segments | 4,848 | 5,053 | 17,309 | 17,103 |
| Corporate/Eliminations | - | - | - | - |
| Total | \$ 4,848 | \$ 5,053 | \$ 17,309 | \$ 17,103 |

The segment information as reviewed by the chief operating decision maker does not include a measure of segment assets per segment as all of the significant assets are used in the operations of all, rather than any one, of the segments. The Company does not have dedicated assets assigned to a particular operating segment. Accordingly, it is not meaningful to attempt an arbitrary allocation and segment asset allocation is therefore not presented.

It is impractical to disclose revenues from external customers for each product and service or each group of similar products and services.

16. Income tax

Income tax in interim periods

For the purposes of interim financial reporting, the Company determines the appropriate income tax provision by first applying the effective tax rate expected to be applicable for the full fiscal year to ordinary income. This amount is then adjusted for the tax effect of significant unusual or extraordinary items, for instance, changes in tax law, valuation allowances and non-deductible transaction-related expenses that are reported separately, and have an impact on the tax charge. The cumulative effect of any change in the enacted tax rate, if and when applicable, on the opening balance of deferred tax assets and liabilities is also included in the tax charge as a discrete event in the interim period in which the enactment date occurs.

For the three and nine months ended March 31, 2014, the tax charge was calculated using the expected effective tax rate for the year. The Company's effective tax rate for the three and nine months ended March 31, 2014, was 33.3% and 34.9%, respectively, and was higher than the South African statutory rate primarily as a result of non-deductible expenses (including interest expense related to the Company's long-term Korean borrowings and stock-based compensation charges).

The Company's effective tax rate for the three months ended March 31, 2013, was (11.1%) and is negative as a result of the loss before income taxes and differed from the South African statutory rate primarily as a result of a valuation allowance for foreign tax credits, non-deductible expenses (including interest expense related to the Company's long-term Korean borrowings and stock-based compensation charges) and South African dividend withholding taxes. The Company's effective tax rate for the nine months ended March 31, 2013, was 61.6% and was higher than the South African statutory rate primarily as a result of a valuation allowance for foreign tax credits, non-deductible expenses (including interest expense related to the Company's long-term Korean borrowings and stock-based compensation charges) and South African dividend withholding taxes.

Uncertain tax positions

There were no changes during the three and nine months ended March 31, 2014. As of March 31, 2014, the Company had accrued interest related to uncertain tax positions of approximately \$0.2 million on its balance sheet.

The Company does not expect changes related to its unrecognized tax benefits will have a significant impact on its results of operations or financial position in the next 12 months.

The Company files income tax returns mainly in South Africa, Korea, Austria, Botswana, the Russian Federation and in the US federal jurisdiction. As of March 31, 2014, the Company is no longer subject to any new income tax examination by the South African Revenue Service for years before June 30, 2009. In 2011, the Korea National Tax Service had completed the examination of the Company's returns in Korea related to years 2006 through 2010. The Company is subject to income tax in other jurisdictions outside South Africa and Korea, none of which are individually material to its financial position, cash flows, or results of operations.

17. Commitments and contingencies

Guarantees

The South African Revenue Service and certain of the Company's customers, suppliers and other business partners have asked the Company to provide them with guarantees, including standby letters of credit, issued by a South African bank. The Company is required to procure these guarantees for these third parties to operate its business.

Nedbank has issued guarantees to these third parties amounting to ZAR 143.1 million (\$13.5 million, translated at exchange rates applicable as of March 31, 2014) and thereby utilizing part of the Company's short-term facility. The Company in turn has provided nonrecourse, unsecured counter-guarantees to Nedbank for the same amount. The Company pays commission of between 0.2% per annum to 2.0% per annum of the face value of these guarantees and does not recover any of the commission from third parties.

The Company has not recognized any obligation related to these counter-guarantees in its unaudited condensed consolidated balance sheet as of March 31, 2014. The maximum potential amount that the Company could pay under these guarantees is ZAR 143.1 million (\$13.5 million, translated at exchange rates applicable as of March 31, 2014). The guarantees have reduced the amount available for borrowings under the Company's short-term credit facility described in Note 8.

17. Commitments and contingencies (continued)

Contingencies

Securities Litigation

On December 24, 2013, Net1, its chief executive officer and its chief financial officer were named as defendants in a purported class action lawsuit filed in the United States District Court for the Southern District of New York alleging violations of the federal securities laws.

The lawsuit alleges that Net1 made materially false and misleading statements regarding its business and compliance policies in its SEC filings and other public disclosures. The lawsuit was brought on behalf of a purported shareholder of Net1 and all other similarly situated shareholders who purchased its securities between August 27, 2009 and November 27, 2013. The lawsuit seeks unspecified damages. The Company believes this lawsuit has no merit and intends to defend it vigorously.

The Company is subject to a variety of insignificant claims and suits that arise from time to time in the ordinary course of business.

Management currently believes that the resolution of these matters, individually or in the aggregate, will not have a material adverse impact on the Company's financial position, results of operations and cash flows.

18. Subsequent events

On April 17, 2014, the South African Constitutional Court (Court) ruled on the appropriate remedy following its declaration on November 29, 2013, that the tender process followed by the South African Social Security Agency (SASSA) in awarding a contract to the Company's wholly-owned subsidiary, CPS, was constitutionally invalid. The declaration of invalidity of the contract between SASSA and CPS was upheld, but suspended until a new tender is awarded, or for the remainder of the existing contract period if no tender is awarded. SASSA is required to initiate a new tender process within 30 days of the Court's ruling and any award must be for a period of five years. In addition, the Court required new and independent Bid Evaluation and Bid Adjudication Committees to be appointed to evaluate and adjudicate the new tender process. If a new tender is not awarded, the declaration of invalidity of the current contract between SASSA and CPS will further be suspended until the completion of the five-year period for which the contract was originally awarded.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with our Annual Report on Form 10-K for the year ended June 30, 2013, and the unaudited condensed consolidated financial statements and the accompanying notes included in this Form 10-Q.

Forward-looking statements

Some of the statements in this Form 10-Q constitute forward-looking statements. These statements relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed, implied or inferred by these forward-looking statements. Such factors include, among other things, those listed under Item 1A. Risk Factors and elsewhere in our Annual Report on Form 10-K for the year ended June 30, 2013, and Item 1A Risk Factors and elsewhere in this Form 10-Q. In some cases, you can identify forward-looking statements by terminology such as may, will, should, could, would, expects, plans, intends, anticipates, believes, potential or continue or the negative of such terms and other comparable terminology.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we do not know whether we can achieve positive future results, levels of activity, performance, or goals. Actual events or results may differ materially. We undertake no obligation to update any of the forward-looking statements after the date of this Form 10-Q to conform those statements to reflect the occurrence of unanticipated events, except as required by applicable law.

You should read this Form 10-Q and the documents that we reference herein and the documents we have filed as exhibits hereto and which we have filed with the Securities and Exchange Commission completely and with the understanding that our actual future results, levels of activity, performance and achievements may be materially different from what we expect. We qualify all of our forward-looking statements by these cautionary statements.

Recent Developments

Constitutional Court pronounces remedy for SASSA tender award

On April 17, 2014, the South African Constitutional Court, or Constitutional Court, ruled on the appropriate remedy following its declaration on November 29, 2013, that the tender process followed by the South African Social Security Agency, or SASSA, in awarding a contract to Net1's wholly-owned subsidiary, Cash Paymaster Services, or CPS, was constitutionally invalid. The declaration of invalidity of the contract between SASSA and CPS was upheld, but suspended until a new tender is awarded, or for the remainder of the existing contract period if no tender is awarded. SASSA is required to initiate a new tender process within 30 days of the Constitutional Court's ruling and any award must be for a period of five years. In addition, the Constitutional Court required new and independent Bid Evaluation and Bid Adjudication Committees to be appointed to evaluate and adjudicate the new tender process. If a new tender is not awarded, the declaration of invalidity of the current contract between SASSA and CPS will further be suspended until the completion of the five-year period for which the contract was originally awarded.

See Part II, Item 1 Legal Proceedings, for additional details.

Implementation of December 2013 Black Economic Empowerment, or BEE, transactions

On April 16, 2014, we implemented our two previously-announced BEE transactions and issued an aggregate of 4,400,000 shares of our common stock to our BEE partners for ZAR 60.00 per share. Refer to note 10 to our unaudited condensed consolidated financial statements for a full description of the BEE transactions.

Growth in mobile value-added services

Our Net1 Mobile Solutions business unit introduced a new suite of mobile value-added services, commencing with a prepaid airtime product during the first quarter of fiscal 2014. We continued to see adoption of this product during the third quarter of fiscal 2014. This product allows our customers in South Africa to electronically purchase prepaid airtime without having to visit a physical prepaid airtime vendor. Net1 Mobile Solutions also introduced a similar service under the brand "Pasavute" in partnership with Telecom Networks Malawi during the third quarter of fiscal 2014.

Traditional prepaid airtime procurement is usually time consuming for the customer and results in them having to pay additional costs. Our product allows our customers, many of whom do not have their own means of transport or ready access to transport, to purchase prepaid airtime without having to travel. We also believe that our product is substantially cheaper than traditional prepaid airtime channels, which often require customers to pay a substantial premium to obtain airtime.

At March 31, 2014, we had over 2.4 million registered users, effecting more than one million transactions per day during peak periods. In December 2013, Net1 Mobile Solutions launched additional mobile value-added services, including prepaid electricity, and adoption rates of these products could be similar to its prepaid airtime offering. We believe that these new products are also cheaper than existing offerings and will make a meaningful difference in the lives of users of these new products.

Pay in Private

During the third quarter of fiscal 2014, our Net1 Mobile Solutions business unit launched our Mobile Virtual Card, or MVC, technology through Pay in Private in the United States in partnership with a US-based marketer with experience in online financial services. The Pay in Private solution offers unmatched security and accessibility to transact online using a mobile handset using our proprietary one-time use MVC Debit MasterCard generated by a smart phone app.

Financial services

In the beginning of fiscal 2014, our Financial Services business unit commenced the national rollout of our financial services offering in the six provinces in which we did not offer our product during fiscal 2013. We have experienced significant growth in our lending book during fiscal 2014 compared with 2013, however, during the third quarter of fiscal 2014, the growth rate slowed down as it appears there is less demand for our financial services offering during the beginning of the calendar year, following the summer holiday period in South Africa. This seasonal trend seems to be confirmed by the re-acceleration of the growth rate during March and April 2014.

Critical Accounting Policies

Our unaudited condensed consolidated financial statements have been prepared in accordance with US GAAP, which requires management to make estimates and assumptions about future events that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities. As future events and their effects cannot be determined with absolute certainty, the determination of estimates requires management's judgment based on a variety of assumptions and other determinants such as historical experience, current and expected market conditions and certain scientific evaluation techniques.

Critical accounting policies are those that reflect significant judgments or uncertainties, and potentially may result in materially different results under different assumptions and conditions. Management has identified the following critical accounting policies that are described in more detail in our Annual Report on Form 10-K for the year ended June 30, 2013:

- Business combinations and the recoverability of goodwill;
- Intangible assets acquired through acquisitions;
- Deferred taxation;
- Stock-based compensation and equity instrument issued pursuant to BEE transaction;
- Accounts receivable and allowance for doubtful accounts receivable; and
- Research and development.

During fiscal 2014, we created an allowance for doubtful finance loans receivable related to our financial services segment as a result of UEPS-based loans provided to our customers. Our policy is to regularly review the ageing of outstanding amounts due from borrowers and adjust the provision based on management's estimate of the recoverability of finance loans receivable. We write off UEPS-based loans and related service fees if a borrower is in arrears with repayments for more than three months or dies.

This is a new allowance and management considered factors including the period of the UEPS-loan outstanding, creditworthiness of the customers and the past payment history and trends of its established UEPS-based lending book. We consider this policy to be appropriate taking into account factors such as historical bad debts, current economic trends and changes in our customer payment patterns. Additional allowances may be required should the ability of our customers to make payments when due deteriorate in the future. A significant amount of judgment is required to assess the ultimate recoverability of these finance loan receivables, including on-going evaluation of the creditworthiness of each customer.

Recent accounting pronouncements adopted

Refer to Note 1 to our unaudited condensed consolidated financial statements for a full description of recent accounting pronouncements adopted, including the dates of adoption and the effects on our condensed consolidated financial statements.

Recent accounting pronouncements not yet adopted as of March 31, 2014

Refer to Note 1 to our unaudited condensed consolidated financial statements for a full description of recent accounting pronouncements not yet adopted as of March 31, 2014, including the expected dates of adoption and effects on our financial condition, results of operations and cash flows.

Currency Exchange Rate Information**Actual exchange rates**

The actual exchange rates for and at the end of the periods presented were as follows:

| Table 1 | Three months ended | | Nine months ended | | Year ended |
|-------------------------------------|---------------------------|-------------|--------------------------|-------------|-------------------|
| | March 31, | | March 31, | | June 30, |
| | 2014 | 2013 | 2014 | 2013 | 2013 |
| ZAR : \$ average exchange rate | 10.8622 | 8.9461 | 10.3375 | 8.6355 | 8.8462 |
| Highest ZAR : \$ rate during period | 11.2667 | 9.3645 | 11.2667 | 9.3645 | 10.3587 |
| Lowest ZAR : \$ rate during period | 10.4848 | 8.4067 | 9.6324 | 8.0444 | 8.0444 |
| Rate at end of period | 10.5833 | 9.2451 | 10.5833 | 9.2451 | 9.8925 |
| KRW : \$ average exchange rate | 1,071 | 1,090 | 1,083 | 1,107 | 1,112 |
| Highest KRW : \$ rate during period | 1,089 | 1,126 | 1,168 | 1,156 | 1,162 |
| Lowest KRW : \$ rate during period | 1,053 | 1,019 | 1,052 | 1,019 | 1,019 |
| Rate at end of period | 1,071 | 1,121 | 1,071 | 1,121 | 1,144 |

Translation exchange rates for financial reporting purposes

For financial reporting purposes we are required to translate our results of operations from ZAR and KRW to US dollars on a monthly basis. Thus, the average rates used to translate this data for the three and nine months ended March 31, 2014 and 2013, vary from the averages shown in the table above. The translation rates we use in presenting our results of operations are the rates shown in the following table:

| Table 2 | Three months ended March 31, | | Nine months ended March 31, | | Year ended June 30, |
|---------------------------------------|---|-------------|--|-------------|--------------------------------|
| | 2014 | 2013 | 2014 | 2013 | 2013 |
| Income and expense items: \$1 = ZAR . | 10.8743 | 8.4662 | 10.3801 | 8.4578 | 8.7105 |
| Income and expense items: \$1 = KRW | 1,070 | 1,113 | 1,076 | 1,112 | 1,072 |
| Balance sheet items: \$1 = ZAR | 10.5833 | 9.2451 | 10.5833 | 9.2451 | 9.8925 |
| Balance sheet items: \$1 = KRW | 1,071 | 1,121 | 1,071 | 1,121 | 1,144 |

Results of operations

The discussion of our consolidated overall results of operations is based on amounts as reflected in our unaudited condensed consolidated financial statements which are prepared in accordance with US GAAP. We analyze our results of operations both in US dollars, as presented in the consolidated financial statements, and supplementally

in ZAR, because ZAR is the functional currency of the entities which contribute the majority of our profits and is the currency in which the majority of our transactions are initially incurred and measured. Due to the significant impact of currency fluctuations between the US dollar and ZAR on our reported results and because we use the US dollar as our reporting currency, we believe that the supplemental presentation of our results of operations in ZAR is useful to investors to understand the changes in the underlying trends of our business.

Nine months ended March 31, 2013, includes SmartSwitch Botswana from December 1, 2012 and Pbel (renamed Net1 Mobile Solutions during the third quarter of fiscal 2014) from September 1, 2012.

We analyze our business and operations in terms of five inter-related but independent operating segments: (1) South African transaction-based activities, (2) international transaction-based activities, (3) smart card accounts, (4) financial services, and (5) hardware, software and related technology sales. In addition, corporate and corporate office activities that are impracticable to ascribe directly to any of the other operating segments, as well as any inter-segment eliminations, are included in corporate/eliminations.

Third quarter of fiscal 2014 compared to third quarter of fiscal 2013

The following factors had an influence on our results of operations during the third quarter of fiscal 2014 as compared with the same period in the prior year:

- **Unfavorable impact from the strengthening of the US dollar against the ZAR:** The US dollar appreciated by 28% against the ZAR during the third quarter of fiscal 2014, which negatively impacted our reported results;
- **SASSA implementation complete:** Our SASSA contract implementation is complete. We incurred implementation-related expenditure, including smart card costs, of approximately \$20.6 million during the third quarter of fiscal 2013;
- **Growth in financial services:** The year-over-year expansion of our financial services offering during the third quarter of fiscal 2014, resulted in higher revenue and operating income from UEPS-based lending;
- **Higher revenue resulting from an increase in low-margin prepaid airtime sales:** Our revenue has increased as a result of the growth of our prepaid airtime offering during the third quarter of fiscal 2014, which has lower margins compared with our other South African businesses;
- **Increased contribution by KSNET:** Our results were positively impacted by growth in our Korean operations;
- **Ad hoc hardware sales in fiscal 2014:** We sold more terminals and cards during the third quarter of fiscal 2014 as a result of ad hoc orders received from our customers;
- **Lower US government investigation-related and US lawsuit expenses:** We incurred fewer US government investigation-related expenses during the third quarter of fiscal 2014 compared to during 2013, which was partially offset by an increase in US lawsuit-related expenses; and
- **Fiscal 2013 bad debt provision:** In fiscal 2013 we provided \$2.3 million related to the expired NUETS Iraqi customer contracts.

Consolidated overall results of operations

This discussion is based on the amounts which were prepared in accordance with US GAAP.

The following tables show the changes in the items comprising our statements of operations, both in US dollars and in ZAR:

| | In United States Dollars (US GAAP) | | |
|--|---------------------------------------|----------------|---------------|
| | Three months ended March 31, | | |
| | 2014 \$ 000 | 2013 \$ 000 | \$% change |
| Revenue | 138,126 | 111,141 | 24% |
| Cost of goods sold, IT processing, servicing and support | 63,149 | 51,461 | 23% |
| Selling, general and administration | 40,586 | 53,846 | (25%) |
| Depreciation and amortization | 10,442 | 10,560 | (1%) |
| Operating income (loss) | 23,949 | (4,726) | nm |
| Interest income | 3,438 | 2,515 | 37% |
| Interest expense | 1,734 | 2,023 | (14%) |
| Income (loss) before income tax expense | 25,653 | (4,234) | nm |

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| | | | |
|---|--------|---------|--------|
| Income tax expense | 8,535 | 472 | 1,708% |
| Net income (loss) before earnings from equity-accounted investments | 17,118 | (4,706) | nm |
| Earnings from equity-accounted investments | 52 | 22 | 136% |
| Net income (loss) | 17,170 | (4,684) | nm |
| Add net loss attributable to non-controlling interest | (12) | (3) | 300% |
| Net income (loss) attributable to us | 17,182 | (4,681) | nm |

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Table 4

| In South African Rand (US GAAP) | | | |
|---|--------------------|--------------------|-----------------|
| Three months ended March 31, | | | |
| | 2014 ZAR 000 | 2013 ZAR 000 | ZAR % change |
| Revenue | 1,502,024 | 940,942 | 60% |
| Cost of goods sold, IT processing, servicing and support | 686,701 | 435,680 | 58% |
| Selling, general and administration | 441,345 | 455,871 | (3%) |
| Depreciation and amortization | 113,549 | 89,403 | 27% |
| Operating income (loss) | 260,429 | (40,012) | nm |
| Interest income | 37,386 | 21,292 | 76% |
| Interest expense | 18,856 | 17,127 | 10% |
| Income (loss) before income tax expense | 278,959 | (35,847) | nm |
| Income tax expense | 92,812 | 3,996 | 2,223% |
| Net income (loss) before earnings from equity-accounted investments | 186,147 | (39,843) | nm |
| Earnings from equity-accounted investments | 565 | 186 | 204% |
| Net income (loss) | 186,712 | (39,657) | nm |
| Add net loss attributable to non-controlling interest | (130) | (25) | 420% |
| Net income (loss) attributable to us | 186,842 | (39,632) | nm |

The increase in revenue was primarily due to a higher contribution from KSNET, more ad hoc terminal and card sales, more low-margin transaction fees generated from beneficiaries using the South African National Payment System, higher prepaid airtime sales driven by the rollout of our prepaid airtime product, and an increase in the number of UEPS-based loans.

The increase in cost of goods sold, IT processing, servicing and support was primarily due to higher expenses incurred from increased usage of the South African National Payment System by beneficiaries and higher prepaid airtime, terminal and card sales. These increases were offset by the substantial elimination of expenses related to our SASSA contract implementation, which we completed in the fourth quarter of fiscal 2013.

Our selling, general and administration expense decreased due to the substantial elimination of SASSA contract implementation costs and fewer legal and other fees incurred related to the US government investigations and the US lawsuit, which was partially offset by increases in goods and services purchased from third parties.

Our operating income (loss) margin for the third quarter of fiscal 2014 and 2013 was 17% and (4)%, respectively. We discuss the components of operating income (loss) margin under Results of operations by operating segment. The increase is primarily attributable to the elimination of implementation costs in fiscal 2014.

In ZAR, depreciation and amortization were higher primarily as a result of an increase in depreciation related to assets used to service our obligations under our SASSA contract, which was partially offset by no MediKredit or FIHRST intangible asset amortization as these intangible assets were fully amortized at the end of June 2013. The tables below present the acquisition-related intangible asset amortization that has been allocated to our operating segments:

Table 5

| Three months ended March 31, | |
|---------------------------------|----------------|
| 2014 \$ 000 | 2013 \$ 000 |

| | |
|---|-------|
| Amortization included in depreciation and amortization expense: | 4,587 |
|---|-------|