SOUTH AFRICA'S $1.5-BN CHAMPION

MONEYWEB, August 8, 2005
BY Barry Sergeant

Remember Aplitec? When the “smart card” technology stock was delisted from the Johannesburg bourse in mid-2004, its price-equivalent was $3 a share. Fast-forward to this week, when the stock listed on the Nasdaq National Exchange in the US, and traded at $28 a share. At current prices of $27.50 a share, the stock boasts a market value of $1.5-bn

The stock’s gain rates it as a “fifteen-bagger,” having advanced from a value of just over $100-m upon delisting in Johannesburg to fifteen times that level on the Nasdaq this week.

The company, now fully named Net 1 UEPS Technologies, Inc., (“Net1”), has not fundamentally changed since it delisted in Johannesburg, although the business itself has since made a number of landmark breakthroughs, and profits are now growing at a scorching pace.

The Nasdaq listing marks the first US IPO (initial public offer) of a company whose management and current core of business is based in South Africa. Despite the $30-m cash the company raised upon its listing this week, South African resident shareholders still hold a healthy chunk of the stock.

Tim Allsop of Polaris Capital, which runs the top-rated Nedbank Rainmaker Equity Fund, says Net1 continues to offer genuine “blue sky” value. Despite the massive rebasing of Net1’s value, Allsop will be holding onto the Net1 stock inherited from the Aplitec holding.

South African linked shareholdings in Net1 are complicated and indirect, due to hurdles kept in place by South Africa’s foreign exchange laws. Domestic shareholders – now the so-called Aplitec reinvesting shareholders – hold their interests in Net1 via a special South African trust, which is linked, in turn, to a trust in the Cayman Islands.

Apart from the Nedbank Rainmaker Equity Fund, other South African linked shareholders in Net1 include Brenthurst Private Equity II Limited, Brenthurst Private Equity South Africa I Limited, South African Private Equity Fund III, L.P., South African Private Equity Trust III, Brait International Limited, and Nedbank Limited. Of these, it would appear from filings that South African Private Equity Fund III, L.P. rates as the largest Net1 holder, at around 24%.

Brait, the specialist financial services outfit listed in Johannesburg, Luxembourg and London, along with a number of its managed private equity funds, comprises one of the single largest underlying shareholders in Net1. Brait advised, structured and financed the Johannesburg delisting transaction, and during the process invested substantially in what is now Net1, on its own behalf and on behalf of its private clients.

Brait executive chairman Anthony Ball says Net1’s smart card technology was seen as “devastating” in its ability to get to the unbanked. Brait advised that the company needed to make the migration to the Nasdaq, where it would be better understood and valued. Ball says

Brait is very pleased with the value the market has now placed on Net1, and is delighted with this week's events.

Beth Mandel, of Morgan Stanley, one of the two investment banks (along with JP Morgan) that painstakingly prepared Net1 for its roaring Nasdaq debut, attributes the vast upgrade in the stock's value to a host of reasons, including deep understanding of technology issues by US investors, Net1's many new "wins" in the past year, the reality of "right technology, right time," and exceptional growth prospects.

The timing of Net1's Nasdaq listing has also been helpful; in the past few days, the technology-rich Nasdaq Composite index has traded up at four year highs (along with another key US exchange, the Standard & Poor's 500).

Net1's valuation can be approached from a number of perspectives, but given the Nasdaq's history of hosting technology companies notoriously unable to deliver on profit promises, profits may be the place to start. The Net1 prospectus, as filed with the US's Securities & Exchange Commission, shows that Net1's net profit (attributable to shareholders) increased from $7.6-m in the year to June 30, 2000 to $13.3-m in the 2004 financial year.

However, accounts prepared for the nine months to March 31, 2005, show net profit almost doubling to $34.4-m from $18.6-m for the previous comparable nine months. Net1's offer price this week was at $22 a share, but the stock has already traded at $28 and is currently priced at $27.50.

Based on 55-m shares in issue, and crudely annualizing the stock's net profit to (say) $46-m for 12 months, the figures put Net1 on a crude price:earnings (PE) ratio of 33 times. While this is below (and thus "cheaper" than) the average Nasdaq PE, Net1 is seen as priced at reasonable levels relative to its peer group, and very well priced relative to its forward potential.

As to Net1's underlying value, and its business model, the company provides its universal electronic payment system (UEPS) as "an alternative payment system for the unbanked and under-banked populations of developing economies." Net1 believes that it is the first company worldwide to implement a system that can enable an estimated four billion people "who generally have limited or no access to a bank account to enter affordably into electronic transactions with each other, government agencies, employers, merchants and other financial service providers."

The potential is literally mind-boggling. Net1's technologies, which include input from several parallel areas such as biometric fingerprint development, is widely used in South Africa by 3.3-m clients in five provinces, who receive social welfare grants using its smart cards.

Recently, Cell C, a mobile telephone service provider in South Africa, chose Net1's solution as the transaction payment system for its planned roll-out of some 52 000 public cellular pay phones that will provide lower income consumers with telephone access at reduced rates.

Outside of South Africa, the Reserve Bank of Malawi has implemented Net1's solution as a national payment system. To date, seven South African financial institutions and BP, a bulk fuel supplier, are using the Net1 system for transaction switching and settlement.

Net1 has deployed smaller, more limited versions of its system in Burundi, Ghana, Latvia, Mozambique, Rwanda, and Zimbabwe. The rate-of-growth in the system can be astonishing; in South Africa, during the nine months to March 31, 2005, the rate of client purchases using Net1 smart cards (rather than merely downloading the value for cash) grew at a compounded monthly growth rate of 71%, while the value of such transactions grew at a compounded monthly growth rate of 60%.

Those familiar with Net1 inevitably share positive anecdotes about the company. The group “head office” is a single floor in a Rosebank, Johannesburg office block, and founder-CEO, Serge Belamant, is a friendly and outgoing person with endless enthusiasm. Each day, one of Net1’s employees puts banners outside the building housing the head office, promising that UEPS will “Enhance Your Lifestyle.”

Net1’s smart cards and associated technologies are seen as a genuine meeting point of high technology with people the world is lobbying to uplift. For Belamant and his team, it has taken ten long years to get the message across. The most recent journey, when Net1 migrated to the Nasdaq, was never easy, and the Johannesburg delisting was both somewhat controversial, and somewhat sad. However, with a market value of $1.5-bn, the Net1 story will resound, and will offer a precedent for future champions.