

EZCORP INC  
Form 10-Q  
May 06, 2008

**Table of Contents**

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, DC 20549**  
**FORM 10-Q**  
**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the Quarterly Period Ended March 31, 2008**  
**Commission File No. 000-19424**  
**EZCORP, INC.**  
 (Exact name of registrant as specified in its charter)

**Delaware** **74-2540145**  
 (State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)  
 organization)

**1901 Capital Parkway**  
**Austin, Texas 78746**  
 (Address of principal executive offices)  
 Registrant's telephone number: **(512) 314-3400**

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

**APPLICABLE ONLY TO CORPORATE ISSUERS:**

The only class of voting securities of the registrant issued and outstanding is the Class B Voting Common Stock, par value \$.01 per share, all of which is owned by one record holder who is an affiliate of the registrant. There is no trading market for the Class B Voting Common Stock.

As of March 31, 2008, 38,427,776 shares of the registrant's Class A Non-voting Common Stock, par value \$.01 per share and 2,970,171 shares of the registrant's Class B Voting Common Stock, par value \$.01 per share were outstanding.

**EZCORP, INC.**  
**INDEX TO FORM 10-Q**

|  | Page |
|--|------|
| <b><u>PART I. FINANCIAL INFORMATION</u></b>  |      |
| <i><u>Item 1. Financial Statements (Unaudited)</u></i>   |      |
| <u>Condensed Consolidated Balance Sheets as of March 31, 2008, March 31, 2007 and September 30, 2007</u>                 | 1    |
| <u>Condensed Consolidated Statements of Operations for the Three Months and Six Months Ended March 31, 2008 and 2007</u> | 2    |
| <u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended March 31, 2008 and 2007</u>                  | 3    |
| <u>Notes to Interim Condensed Consolidated Financial Statements</u>  | 4    |
| <i><u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u></i>              | 14   |
| <i><u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u></i>   | 31   |
| <i><u>Item 4. Controls and Procedures</u></i>  | 32   |
| <b><u>PART II. OTHER INFORMATION</u></b>   |      |
| <i><u>Item 1. Legal Proceedings</u></i>  | 33   |
| <i><u>Item 1A. Risk Factors</u></i>  | 33   |
| <i><u>Item 6. Exhibits</u></i>   | 33   |
| <b><u>SIGNATURE</u></b>  | 34   |
| <b><u>EXHIBIT INDEX</u></b>  | 35   |
| <b>CERTIFICATIONS</b>  |      |
| <u>Stock Purchase Agreement</u>  |      |
| <u>Amendment No. 1 to Stock Purchase Agreement</u>   |      |
| <u>Certification of CEO Pursuant to Section 302</u>  |      |
| <u>Certification of CFO Pursuant to Section 302</u>  |      |
| <u>Certification of CEO Pursuant to Section 906</u>  |      |
| <u>Certification of CFO Pursuant to Section 906</u>  |      |

---

**Table of Contents****PART I****Item 1. Financial Statements**

## Condensed Consolidated Balance Sheets

|   | March 31,<br>2008<br><i>(Unaudited)</i> | March 31,<br>2007<br><i>(Unaudited)</i><br><i>(In thousands)</i> | September<br>30,<br>2007 |
|---|---|--|--------------------------|
| Assets:   |   |  |                          |
| Current assets:   |   |  |                          |
| Cash and cash equivalents   | \$ 35,551                               | \$ 61,605  | \$ 22,533                |
| Pawn loans  | 56,701                                  | 43,109   | 60,742                   |
| Payday loans, net   | 5,290                                   | 3,314  | 4,814                    |
| Pawn service charges receivable, net  | 8,983                                   | 6,986  | 10,113                   |
| Signature loan fees receivable, net   | 4,781                                   | 4,334  | 5,992                    |
| Inventory, net  | 35,999                                  | 28,649   | 37,942                   |
| Deferred tax asset, net   | 9,006                                   | 7,150  | 8,964                    |
| Prepaid expenses and other assets   | 7,281                                   | 5,373  | 6,146                    |
| Total current assets  | 163,592                                 | 160,520  | 157,246                  |
| Investment in unconsolidated affiliate  | 36,904                                  | 20,955   | 35,746                   |
| Property and equipment, net   | 38,413                                  | 30,967   | 33,806                   |
| Deferred tax asset, non-current   | 5,346                                   | 4,249  | 4,765                    |
| Goodwill  | 24,422                                  | 768  | 16,211                   |
| Other assets, net   | 5,350                                   | 2,952  | 3,412                    |
| Total assets  | \$ 274,027                              | \$ 220,411   | \$ 251,186               |
| Liabilities and stockholders' equity:   |   |  |                          |
| Current liabilities:  |   |  |                          |
| Accounts payable and other accrued expenses   | \$ 22,202                               | \$ 18,594  | \$ 25,592                |
| Customer layaway deposits   | 2,456                                   | 2,168  | 1,988                    |
| Federal income taxes payable  | 2,363                                   | 1,104  | 4,795                    |
| Total current liabilities   | 27,021                                  | 21,866   | 32,375                   |
| Deferred gains and other long-term liabilities  | 3,003                                   | 3,067  | 2,886                    |
| Commitments and contingencies   |   |  |                          |
| Stockholders' equity:   |   |  |                          |
| Preferred Stock, par value \$.01 per share; 5 million shares authorized; none issued and outstanding  |   |  |                          |
| Class A Non-voting Common Stock, par value \$.01 per share; 50 million shares authorized; 38,454,875 issued and 38,427,776 outstanding at March 31, 2008; 38,304,741 issued and 38,277,642 outstanding at March 31, 2007; 38,363,176 issued and 38,336,077 outstanding at | 384                                     | 383  | 383                      |

Edgar Filing: EZCORP INC - Form 10-Q

September 30, 2007

Class B Voting Common Stock, convertible, par value \$.01  
per share; 3 million shares authorized; 2,970,171 issued  
and outstanding

|  |            |            |            |
|--|------------|------------|------------|
|  | 30         | 30         | 30         |
| Additional paid-in capital                               | 133,430    | 128,916    | 131,098    |
| Cumulative effect of adopting a new accounting principle | (106)      |            |            |
| Retained earnings  | 107,418    | 63,930     | 81,847     |
|  | 241,156    | 193,259    | 213,358    |
| Treasury stock, at cost (27,099 shares)                  | (35)       | (35)       | (35)       |
| Accumulated other comprehensive income                   | 2,882      | 2,254      | 2,602      |
| Total stockholders' equity                               | 244,003    | 195,478    | 215,925    |
| Total liabilities and stockholders' equity               | \$ 274,027 | \$ 220,411 | \$ 251,186 |

See Notes to Condensed Consolidated Financial Statements (unaudited).

1

---

**Table of Contents**

## Condensed Consolidated Statements of Operations (Unaudited)

|  | Three Months Ended<br>March 31,                 |           | Six Months Ended<br>March 31, |           |
|--|---|-----------|-------------------------------|-----------|
|  | 2008  | 2007      | 2008                          | 2007      |
|  | <i>(In thousands, except per share amounts)</i> |           |                               |           |
| Revenues:  |   |           |                               |           |
| Sales  | \$ 61,330                                       | \$ 50,032 | \$ 116,837                    | \$ 99,012 |
| Pawn service charges                             | 21,785  | 16,556    | 44,693                        | 34,518    |
| Signature loan fees                              | 30,166  | 22,713    | 63,694                        | 47,108    |
| Other  | 344   | 342       | 707                           | 692       |
| Total revenues                                   | 113,625   | 89,643    | 225,931                       | 181,330   |
| Cost of goods sold                               | 36,731  | 30,374    | 70,272                        | 60,197    |
| Net revenues                                     | 76,894  | 59,269    | 155,659                       | 121,133   |
| Operating expenses:                              |   |           |                               |           |
| Operations                                       | 37,521  | 31,104    | 74,592                        | 62,492    |
| Signature loan bad debt                          | 6,632   | 2,916     | 16,302                        | 8,944     |
| Administrative                                   | 9,829   | 7,968     | 19,734                        | 15,495    |
| Depreciation and amortization                    | 3,119   | 2,401     | 5,946                         | 4,699     |
| Total operating expenses                         | 57,101  | 44,389    | 116,574                       | 91,630    |
| Operating income                                 | 19,793  | 14,880    | 39,085                        | 29,503    |
| Interest income                                  | (137)   | (567)     | (194)                         | (881)     |
| Interest expense                                 | 75  | 83        | 156                           | 147       |
| Equity in net income of unconsolidated affiliate | (1,118)   | (820)     | (2,165)                       | (1,465)   |
| Loss on sale / disposal of assets                | 81  |           | 243                           | 24        |
| Income before income taxes                       | 20,892  | 16,184    | 41,045                        | 31,678    |
| Income tax expense                               | 7,876   | 5,988     | 15,474                        | 11,721    |
| Net income                                       | \$ 13,016                                       | \$ 10,196 | \$ 25,571                     | \$ 19,957 |
| Net income per common share:                     |   |           |                               |           |
| Basic  | \$ 0.31   | \$ 0.25   | \$ 0.62                       | \$ 0.49   |
| Diluted  | \$ 0.30   | \$ 0.23   | \$ 0.59                       | \$ 0.46   |
| Weighted average shares outstanding:             |   |           |                               |           |
| Basic  | 41,382  | 41,002    | 41,360                        | 40,773    |

Edgar Filing: EZCORP INC - Form 10-Q

|   |        |        |        |        |
|---|--------|--------|--------|--------|
| Diluted   | 43,228 | 43,445 | 43,241 | 43,347 |
| See Notes to Interim Condensed Consolidated Financial Statements (unaudited). |        |        |        |        |

---

**Table of Contents**

## Condensed Consolidated Statements of Cash Flows (Unaudited)

|   | Six Months Ended      |               |
|---|-----------------------|---------------|
|   | March 31,             |               |
|   | 2008                  | 2007          |
|   | <i>(In thousands)</i> |               |
| <b>Operating Activities:</b>  |                       |               |
| Net income  | \$ 25,571             | \$ 19,957     |
| Adjustments to reconcile net income to net cash provided by operating activities: |                       |               |
| Depreciation and amortization   | 5,946                 | 4,699         |
| Payday loan loss provision  | 3,612                 | 1,338         |
| Deferred taxes  | (583)                 | (500)         |
| Net loss on sale or disposal of assets  | 243                   | 24            |
| Share-based compensation  | 1,924                 | 1,664         |
| Income from investment in unconsolidated affiliate                                | (2,165)               | (1,465)       |
| Changes in operating assets and liabilities, net of business acquisitions:        |                       |               |
| Service charges and fees receivable, net  | 2,568                 | 1,294         |
| Inventory, net  | 618                   | 1,053         |
| Prepaid expenses, other current assets, and other assets, net                     | (1,214)               | (1,519)       |
| Accounts payable and accrued expenses   | (3,392)               | (3,999)       |
| Customer layaway deposits   | 403                   | 278           |
| Deferred gains and other long-term liabilities                                    | 84                    | (182)         |
| Excess tax benefit from stock-based compensation                                  | (261)                 | (824)         |
| Federal income taxes  | (2,277)               | 2,534         |
| <b>Net cash provided by operating activities</b>                                  | <b>31,077</b>         | <b>24,352</b> |
| <b>Investing Activities:</b>  |                       |               |
| Pawn loans made   | (117,641)             | (92,358)      |
| Pawn loans repaid   | 70,063                | 55,464        |
| Recovery of pawn loan principal through sale of forfeited collateral              | 57,160                | 50,003        |
| Payday loans made   | (36,304)              | (19,110)      |
| Payday loans repaid   | 32,216                | 16,903        |
| Additions to property and equipment   | (9,625)               | (6,248)       |
| Acquisitions, net of cash acquired  | (15,439)              |               |
| Dividends from unconsolidated affiliate   | 1,103                 | 826           |
| <b>Net cash provided by (used in) investing activities</b>                        | <b>(18,467)</b>       | <b>5,480</b>  |
| <b>Financing Activities:</b>  |                       |               |
| Proceeds from exercise of stock options and warrants                              | 147                   | 1,293         |
| Excess tax benefit from stock-based compensation                                  | 261                   | 824           |
| Debt issuance costs   |                       | (283)         |
| <b>Net cash provided by financing activities</b>                                  | <b>408</b>            | <b>1,834</b>  |
| <b>Change in cash and equivalents</b>   | <b>13,018</b>         | <b>31,666</b> |
| <b>Cash and equivalents at beginning of period</b>                                | <b>22,533</b>         | <b>29,939</b> |



|   |           |            |
|---|-----------|------------|
| Cash and equivalents at end of period   | \$ 35,551 | \$ 61,605  |
| Non-cash Investing and Financing Activities:                                  |           |            |
| Pawn loans forfeited and transferred to inventory                             | \$ 54,880 | \$ 44,089  |
| Foreign currency translation adjustment                                       | \$ (280)  | \$ (1,029) |
| Cumulative effect of adopting a new accounting principle                      | \$ 106    | \$         |
| See Notes to Interim Condensed Consolidated Financial Statements (unaudited). |           |            |

3

---

**Table of Contents**

**EZCORP, Inc. and Subsidiaries**  
**Notes to Interim Condensed Consolidated Financial Statements (Unaudited)**  
**March 31, 2008**

**Note A: Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Management has included all adjustments it considers necessary for a fair presentation. These adjustments are of a normal, recurring nature except for those related to an acquired business (described in Note C) and the adoption of a new accounting principle for uncertain tax positions (described in Note K). The accompanying financial statements should be read with the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended September 30, 2007. The balance sheet at September 30, 2007 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Certain prior period balances have been reclassified to conform to the current presentation.

Our business is subject to seasonal variations, and operating results for the three and six-month periods ended March 31, 2008 (the current quarter and current year-to-date period ) are not necessarily indicative of the results of operations for the full fiscal year.

**Note B: Significant Accounting Policies**

**CONSOLIDATION:** The consolidated financial statements include the accounts of EZCORP, Inc. and its wholly owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation. We account for our interest in Albemarle & Bond Holdings, plc using the equity method.

**PAWN LOAN AND SALES REVENUE RECOGNITION:** We record pawn service charges using the interest method for all pawn loans we believe to be collectible. We base our estimate of collectible loans on several factors, including recent redemption rates, historical trends in redemption rates and the amount of loans due in the following two to three months. Unexpected variations in any of these factors could change our estimate of collectible loans, affecting our earnings and financial condition. If a pawn loan is not repaid, we value the forfeited collateral (inventory) at the lower of cost (pawn loan principal) or market (net realizable value) of the property. We record sales revenue and the related cost when this inventory is sold.

**CREDIT SERVICE REVENUE RECOGNITION:** We earn credit service fees when we assist customers in obtaining a loan from unaffiliated lenders. We initially defer recognition of the fees we expect to collect, net of direct expenses, and recognize that deferred net amount over the life of the related loans. We reserve the percentage of credit service fees we expect not to collect. Accrued fees related to defaulted loans reduce credit service fee revenue upon loan default, and increase credit service fee revenue upon collection. Credit service revenue is included in Signature loan fees on our statements of operations.

**CREDIT SERVICE BAD DEBT:** We issue letters of credit to enhance the creditworthiness of our credit service customers seeking loans from unaffiliated lenders. The letters of credit assure the lenders that if borrowers default on the loans, we will pay the lenders, upon demand, the principal and accrued interest owed it by the borrowers plus any insufficient funds fee. Although amounts paid under letters of credit may be collected later, we charge those amounts to signature loan bad debt upon default. We record recoveries under the letters of credit as a reduction of bad debt at the time of collection. After attempting collection of bad debts internally, we occasionally sell them to an unaffiliated company as another method of recovery. We account for the sale of defaulted accounts in the same manner as internal collections of defaulted accounts.

The majority of our credit service customers obtain short-term loans with a single maturity date. These short-term loans, with maturity dates averaging about 18 days, are considered defaulted if they have not been repaid or renewed by the maturity date. Other credit service customers obtain installment loans with a series of payments due over as

**Table of Contents**

much as a five-month period. If one payment of an installment loan is delinquent, that one payment is considered defaulted. If more than one installment payment is delinquent at any time, the entire loan is considered defaulted. CREDIT SERVICE ALLOWANCE FOR LOSSES: We also provide an allowance for losses we expect to incur under letters of credit for loans that have not yet matured. The allowance is based on recent loan default experience adjusted for seasonal variations. It includes all amounts we expect to pay to the unaffiliated lenders upon loan default, including loan principal, accrued interest, and insufficient funds fees, net of the amounts we expect to collect from borrowers ( Expected LOC Losses ). Changes in the allowance are charged to signature loan bad debt expense. We include the balance of Expected LOC Losses in Accounts payable and other accrued expenses on our balance sheet. At March 31, 2008, the allowance for Expected LOC Losses was \$1.2 million. At that date, our maximum exposure for losses on letters of credit, if all brokered loans defaulted and none was collected, was \$21.4 million. This amount includes principal, interest, and insufficient funds fees. Based on the expected loss and collection percentages, we also provide an allowance for the credit service fees we expect not to collect, and charge changes in this allowance to signature loan fee revenue.

PAYDAY LOAN REVENUE RECOGNITION: We accrue fees on the percentage of payday loans we believe to be collectible. Accrued fees related to defaulted loans reduce fee revenue upon loan default, and increase fee revenue upon collection. Payday loan fee revenue is included in Signature loan fees on our statements of operations. Loan terms are generally less than 30 days, averaging about 18 days.

PAYDAY LOAN BAD DEBT: We consider a loan defaulted if it has not been repaid or renewed by the maturity date. Although defaulted loans may be collected later, we charge the loan principal to signature loan bad debt upon default, leaving only active loans in the reported balance. We record collections of principal as a reduction of signature loan bad debt when collected. After attempting collection of bad debts internally, we occasionally sell them to an unaffiliated company as another method of recovery. We account for the sale of defaulted accounts in the same manner as internal collections of defaulted accounts.

PAYDAY LOAN ALLOWANCE FOR LOSSES: We also provide an allowance for losses on payday loans that have not yet matured and related fees receivable, based on recent loan default experience adjusted for seasonal variations. We charge any changes in the principal valuation allowance to signature loan bad debt. We record changes in the fee receivable valuation allowance to signature loan fee revenue.

INVENTORY: If a pawn loan is not redeemed, we record the forfeited collateral at cost. We do not record loan loss allowances or charge-offs on the principal portion of pawn loans, as they are fully collateralized. In order to state inventory at the lower of cost (specific identification) or market (net realizable value), we record an allowance for shrinkage and excess, obsolete, or slow-moving inventory. The allowance is based on the type and age of merchandise and recent sales trends and margins. At March 31, 2008, the inventory valuation allowance was \$4.7 million, or 11.6% of gross inventory. We record changes in the inventory valuation allowance as cost of goods sold.

INTANGIBLE ASSETS: Goodwill and other intangible assets having indefinite lives are not subject to amortization. They are tested for impairment each July 1<sup>st</sup>, or more frequently if events or changes in circumstances indicate that they might be impaired. We recognized no impairment of our intangible assets in the current or prior year-to-date periods. We amortize intangible assets with definite lives over their estimated useful lives, using the straight-line method.

PROPERTY AND EQUIPMENT: Property and equipment is shown net of accumulated depreciation of \$89.8 million at March 31, 2008.

VALUATION OF TANGIBLE LONG-LIVED ASSETS: We assess the impairment of tangible long-lived assets whenever events or changes in circumstances indicate that the net recorded amount may not be recoverable. The following factors could trigger an impairment review: significant underperformance relative to historical or projected future cash flows; significant changes in the manner of use of the assets or the strategy for the overall business; or significant negative industry trends. When we determine that the net recorded amount of tangible long-lived assets may not be recoverable, we measure impairment based on the excess of the assets' net recorded amount over the estimated fair value. No impairment of tangible long-lived assets was recognized in the current or prior year-to-date periods.



**Table of Contents**

**INCOME TAXES:** We calculate the provision for federal income taxes based on our estimate of the effective tax rate for the full fiscal year. As part of the process of preparing the financial statements, we estimate income taxes in each jurisdiction in which we operate. This involves estimating the actual current tax liability and assessing temporary differences in recognition of income for tax and accounting purposes. These differences result in deferred tax assets and liabilities that we include in our balance sheet. We must then assess the likelihood that the deferred tax assets will be recovered from future taxable income. If we determined we would not be able to realize all or part of our net deferred tax assets in the future, an increase to the valuation allowance would be charged to the income tax provision in that period. Likewise, if we determined we would be able to realize our deferred tax assets in the future in excess of the net recorded amount, a decrease to the valuation allowance would decrease the tax provision in that period. We assess the need for a deferred tax asset valuation allowance quarterly. Our valuation allowance was unchanged from the prior year-to-date period at \$0.4 million at March 31, 2008.

Effective October 1, 2007, we adopted Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes ( FIN 48 ). See Note K for further discussion and related disclosures.

**SHARE-BASED COMPENSATION:** We account for share-based compensation in accordance with the fair value recognition provisions of SFAS No. 123(R), Share-based Payment. We estimate the grant-date fair value of options using the Black-Scholes-Merton option-pricing model and amortize that fair value to compensation expense on a straight-line basis over the options vesting periods.

**SEGMENTS:** We account for our operations in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. We manage our business operations and internal reporting as three reportable segments. Prior to October 1, 2007, we had two reportable segments. Effective October 1, 2007, we reorganized as three reportable segments. See Note L for further discussion and separate data for each segment.

**RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS:** In September 2006, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 157, Fair Value Measurements. Among other requirements, SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosure about the use of fair value to measure assets and liabilities. We must adopt SFAS No. 157 in our fiscal year ending September 30, 2009. We are currently evaluating the impact, if any, of SFAS No. 157 on our financial position and results of operations. It will not impact our cash flows.

**Note C: Acquisitions**

On October 22, 2007, we completed the acquisition of twenty Mexico pawnshops from MMFS Intl., S.A. de C.V, a subsidiary of Mister Money Holdings, Inc. for \$15.4 million cash and direct transaction costs. The estimated fair values of the assets acquired and liabilities assumed are preliminary, and may be refined within a year of the acquisition. The initial valuation of \$15.3 million increased to \$15.4 million in the current quarter due to additional professional fees related to the acquisition. The increase was recorded as an increase to goodwill. In the current quarter, we also refined our estimated fair value of the non-compete agreement, which increased the non-compete agreement by \$0.4 million, and decreased goodwill by an offsetting amount.

**Table of Contents**

The purchase price is preliminarily allocated as follows, including the adjustments discussed above (*in thousands*):

|                                      |               |
|--------------------------------------|---------------|
| Current assets:                      |               |
| Pawn loans                           | \$ 3,230      |
| Pawn service charges receivable, net | 224           |
| Inventory, net                       | 940           |
| Deferred tax asset                   | 41            |
| Prepaid expenses and other assets    | 40            |
| <br>Total current assets             | <br>4,475     |
| <br>Property and equipment           | <br>800       |
| Non-compete agreement                | 2,000         |
| Goodwill                             | 8,128         |
| Other assets, net                    | 131           |
| <br>Total assets                     | <br>\$ 15,534 |
| <br>Liabilities:                     |               |
| Accrued liabilities                  | \$ (30)       |
| Customer deposits                    | (65)          |
| <br>Total liabilities                | <br>(95)      |
| <br>Net assets acquired              | <br>\$ 15,439 |

The results of the acquired stores have been consolidated with our results since their acquisition. Pro forma results of operations have not been presented because the acquisition was not material in relation to our consolidated financial position or results of operations.

On March 17, 2008, we announced our agreement to acquire up to 100%, but not less than 70%, of the equity ownership of Value Financial Services, Inc., a pawn store chain based in Florida, for approximately \$100 million, subject to our due diligence review. On April 28, 2008, we amended the agreement to extend the due diligence period to May 13, 2008 and the expected closing date to June 26, 2008, among other related changes.

**Note D: Earnings Per Share**

We compute basic earnings per share on the basis of the weighted average number of shares of common stock outstanding during the period. We compute diluted earnings per share on the basis of the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options, warrants and restricted stock awards.

Components of basic and diluted earnings per share are as follows (*in thousands, except per share amounts*):

|  | Three Months Ended |            | Six Months Ended |            |
|--|--------------------|------------|------------------|------------|
|  | March 31,          |            | March 31,        |            |
|  | 2008               | 2007       | 2008             | 2007       |
| Net income (A)   | \$ 13,016          | \$ 10,196  | \$ 25,571        | \$ 19,957  |
| <br>Weighted average outstanding shares of common stock<br>(B) | <br>41,382         | <br>41,002 | <br>41,360       | <br>40,773 |
|  | 1,846              | 2,443      | 1,881            | 2,574      |

Dilutive effect of stock options, warrants, and restricted stock

|  |         |         |         |         |
|--|---------|---------|---------|---------|
| Weighted average common stock and common stock equivalents (C) | 43,228  | 43,445  | 43,241  | 43,347  |
| Basic earnings per share (A/B)                                 | \$ 0.31 | \$ 0.25 | \$ 0.62 | \$ 0.49 |
| Diluted earnings per share (A/C)                               | \$ 0.30 | \$ 0.23 | \$ 0.59 | \$ 0.46 |

Anti-dilutive options, warrants and restricted stock grants have been excluded from the computation of diluted earnings per share because the assumed proceeds upon exercise, as defined by SFAS No. 123(R), were greater than the cost to re-acquire the same number of shares at the average market price, and therefore the effect would be anti-dilutive.

**Table of Contents****Note E: Investment in Unconsolidated Affiliate**

At March 31, 2008, we owned 16,298,875 common shares of Albemarle & Bond Holdings, plc ( A&B ), or approximately 29.95% of A&B's total outstanding shares. The investment is accounted for using the equity method. Since A&B's fiscal year ends three months prior to ours, we report the income from this investment on a three-month lag. A&B files interim and annual financial reports for its fiscal periods ending December 31 and June 30. The income reported for our current year-to-date period ended March 31, 2008 represents our percentage interest in the results of A&B's operations from July 1, 2007 to December 31, 2007, including the results of 26 stores A&B acquired from a competitor on July 12, 2007.

On July 1, 2007, A&B discontinued use of U.K. GAAP and adopted International Financial Reporting Standards, or IFRS. The prior year figures shown below are restated on IFRS for comparability to the current year presentation. Below is summarized financial information for A&B's most recently reported results (*using average exchange rates for the periods indicated*):

|                               | Six Months Ended December<br>31, |          |
|-------------------------------|----------------------------------|----------|
|                               | 2007                             | 2006     |
|                               | <i>(in thousands)</i>            |          |
| Turnover (gross revenues)     | \$50,660                         | \$32,669 |
| Gross profit                  | 36,574                           | 23,447   |
| Profit after tax (net income) | 7,230                            | 5,239    |

**Note F: Contingencies**

Currently and from time to time, we are defendants in legal and regulatory actions. While we cannot determine the ultimate outcome of these actions, after consultation with counsel, we believe their resolution will not have a material adverse effect on our financial condition, results of operations or liquidity. However, we cannot give any assurance as to their ultimate outcome.

In May 2007, the State of Texas filed suit against EZCORP, Inc. and our Texas affiliates in state district court in Bexar County alleging violations of the Texas Identity Theft statute, Deceptive Trade Practices Act, and a provision of the Business and Commerce Code by allegedly failing to safeguard and properly dispose of customers' sensitive personal information. In late May 2007, we voluntarily entered into an Agreed Temporary Injunction regarding the safeguarding and disposal of the information. We have reviewed and enhanced our information security policies to address the State's concerns. We are currently in discussions with the State to reach an amicable resolution of this matter, but can give no assurance that an amicable resolution will be reached prior to the October 20, 2008 scheduled jury trial date.

The Florida Office of Financial Regulation has filed an administrative action against us alleging that our Florida credit service organization business model used in eleven stores adjoining EZPAWN locations violates state usury law. On March 25, 2008, an administrative law judge issued a Recommended Order finding against us and recommending that the Florida Office of Financial Regulation issue a cease and desist order against our ongoing credit services operations in Florida. We expect the Florida Office of Financial Regulation to issue a final order in this matter by May 31, 2008. We intend to appeal any decision and have filed a Motion for Stay Pending Appeal with the Florida Office of Financial Regulation. No ruling on the Motion for Stay has been issued. We cannot give any assurance as to the ultimate outcome of this matter.

**Note G: Comprehensive Income**

Comprehensive income includes net income and other revenues, expenses, gains and losses that are excluded from net income but are included as a component of total stockholders' equity. Comprehensive income for the current quarter and current year-to-date periods ended March 31, 2008 was \$12.9 million and \$25.9 million. For the comparable 2007 periods, comprehensive income was \$10.8 million and \$21.0 million, respectively. The difference between comprehensive income and net income results primarily from the effect of foreign currency translation adjustments determined in accordance with SFAS No. 52, Foreign Currency Translation. At March 31, 2008, the accumulated balance of foreign currency activity excluded from net income was \$4.4 million, net of tax of \$1.5 million. The net



\$2.9 million is presented as Accumulated other comprehensive income in the current quarter balance sheet.

**Table of Contents****Note H: Long-term Debt**

While we had no debt at March 31, 2008 and 2007, we have a \$40.0 million revolving credit facility secured by our assets, which matures October 1, 2009. For any borrowed funds, we may choose a Eurodollar rate plus 100 to 200 basis points (depending on the leverage ratio) or the agent bank's base rate. On the unused amount of the revolving facility, we pay a commitment fee of 25 to 30 basis points depending on the leverage ratio calculated at the end of each quarter. Terms of the agreement require, among other things, that we meet certain financial covenants. We were in compliance with all covenants at March 31, 2008. Payment of dividends and additional debt are allowed but restricted.

**Note I: Goodwill and Other Intangible Assets**

The following table presents the balance of each major class of indefinite-lived intangible asset at the specified dates:

|               | March<br>31,<br>2008 | March 31,<br>2007     | September 30,<br>2007 |
|---------------|----------------------|-----------------------|-----------------------|
|               |                      | <i>(In thousands)</i> |                       |
| Pawn licenses | \$ 1,549             | \$ 1,549              | \$ 1,549              |
| Goodwill      | 24,422               | 768                   | 16,211                |
| Total         | \$ 25,971            | \$ 2,317              | \$ 17,760             |

The following table presents the gross carrying amount and accumulated amortization for each major class of definite-lived intangible asset at the specified dates:

|                          | March 31, 2008     |                             | March 31, 2007        |                             | September 30, 2007 |                             |
|--------------------------|--------------------|-----------------------------|-----------------------|-----------------------------|--------------------|-----------------------------|
|                          | Carrying<br>Amount | Accumulated<br>Amortization | Carrying<br>Amount    | Accumulated<br>Amortization | Carrying<br>Amount | Accumulated<br>Amortization |
|                          |                    |                             | <i>(In thousands)</i> |                             |                    |                             |
| License application fees | \$ 345             | \$ (304)                    | \$ 345                | \$ (273)                    | \$ 345             | \$ (288)                    |
| Real estate finders fees | 556                | (336)                       | 556                   | (319)                       | 556                | (327)                       |
| Non-compete agreements   | 2,917              | (569)                       | 398                   | (288)                       | 898                | (324)                       |
| Total                    | \$ 3,818           | \$ (1,209)                  | \$ 1,299              | \$ (880)                    | \$ 1,799           | \$ (939)                    |

Total amortization expense from definite-lived intangible assets for the current quarter and year-to-date periods ended March 31, 2008 was approximately \$152,000 and \$268,000. For the comparable 2007 periods, amortization expense was approximately \$17,000 and \$35,000. The following table presents our estimate of amortization expense for definite-lived intangible assets for each of the five succeeding fiscal years as of October 1, 2007 (*in thousands*):

| Fiscal Year | Amortization Expense |
|-------------|----------------------|
| 2008        | \$555                |
| 2009        | \$563                |
| 2010        | \$548                |
| 2011        | \$541                |
| 2012        | \$509                |
| Thereafter  | \$162                |

As acquisitions and dispositions occur in the future, amortization expense may vary from these estimates.

**Table of Contents****Note J: Common Stock, Warrants, Options, and Share-based Compensation**

Our income includes the following share-based compensation expense, determined in accordance with the fair value provisions of SFAS No. 123(R):

|   | Three Months Ended<br>March 31, |        | Six Months Ended<br>March 31, |          |
|---|---------------------------------|--------|-------------------------------|----------|
|   | 2008                            | 2007   | 2008                          | 2007     |
|   | <i>(in thousands)</i>           |        |                               |          |
| Gross compensation cost                           | \$ 1,068                        | \$ 914 | \$ 1,924                      | \$ 1,664 |
| Income tax benefit                                | (331)                           | (315)  | (599)                         | (535)    |
| Share-based compensation cost, net of tax benefit | \$ 737                          | \$ 599 | \$ 1,325                      | \$ 1,129 |

Stock option and warrant exercises resulted in the issuance of 55,166 shares of Class A Non-voting Common Stock in the current quarter for total proceeds of \$64,000. For the current year-to-date period, 91,699 shares of Common Stock were issued for total proceeds of \$147,000.

**Note K: Adoption of a New Accounting Principle for Income Taxes**

Effective October 1, 2007, we adopted Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes ( FIN 48 ). To be recognized in the financial statements, FIN 48 requires that a tax position is more-likely-than-not to be sustained upon examination, based on the technical merits of the position. In making the determination of sustainability, we must presume the appropriate taxing authority with full knowledge of all relevant information will examine tax positions. FIN 48 also prescribes how the benefit should be measured, including the consideration of any penalties and interest. It requires that the new standard be applied to the balances of tax assets and liabilities as of the beginning of the period of adoption and that a corresponding adjustment be made to the opening balance of equity. As a result of the adoption of FIN 48, we recognized a \$106,000 liability, including \$8,600 of penalties and interest, for unrecognized state income tax benefits net of federal taxes, and recorded this as a cumulative adjustment to our beginning equity at October 1, 2007. This balance has not been adjusted since adoption. We will record future changes in FIN 48 tax liabilities and related interest and penalties as federal income tax expense on our statement of operations and in federal income taxes payable on our balance sheet.

Below is a reconciliation of the beginning and ending unrecognized tax benefits for the current year-to-date period (*in thousands*):

|  |    |     |
|--|----|-----|
| Unrecognized tax benefits at September 30, 2007          | \$ |     |
| Addition upon initial adoption of FIN 48 October 1, 2007 |    | 106 |
| Additions based on current year tax positions            |    |     |
| Reductions based on settlements with taxing authorities  |    |     |
| Reductions due to lapse in statute of limitations        |    |     |
| Unrecognized tax benefits at March 31, 2008              | \$ | 106 |

We are subject to U.S. and Mexican income taxes as well as various other state and local jurisdictions. With few exceptions, we are no longer subject to examinations by tax authorities for years before the tax year ended September 30, 2003. The statutes of limitations related to our recorded liability expire between June 15, 2009 and June 15, 2011.

**Table of Contents****Note L: Operating Segment Information**

We manage our business and internal reporting as three reportable segments with operating results reported separately for each segment. Prior to October 1, 2007, we had two reportable segments. Effective October 1, 2007, we broke our previously immaterial EZPAWN Mexico operations into a reportable segment separate from other pawn operations, and have restated prior year amounts on a comparable basis. The three reportable segments are:

**EZPAWN U.S. Operations:** This segment offers pawn loans and related sales in our 294 U.S. EZPAWN stores and offers signature loans in six U.S. EZMONEY stores and 73 of our U.S. EZPAWN stores.

**EZPAWN Mexico Operations:** This segment offers pawn loans and related sales in 26 pawn stores in Mexico.

**EZMONEY Operations:** This segment operates only in the United States and offers signature loans in 456 of our EZMONEY stores.

There are no inter-segment revenues, and the amounts below were determined in accordance with the same accounting principles used in our consolidated financial statements. The following tables present operating segment information:

|   | EZPAWN<br>U.S.<br>Operations | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
|---|------------------------------|--------------------------------|-----------------------|--------------|
|   | <i>(in thousands)</i>        |                                |                       |              |
| <b>Three Months Ended March 31, 2008:</b> |                              |                                |                       |              |
| Revenues:                                 |                              |                                |                       |              |
| Sales                                     | \$ 59,747                    | \$ 1,583                       | \$                    | \$ 61,330    |
| Pawn service charges                      | 20,720                       | 1,065                          |                       | 21,785       |
| Signature loan fees                       | 672                          |                                | 29,494                | 30,166       |
| Other                                     | 341                          | 3                              |                       | 344          |
| Total revenues                            | 81,480                       | 2,651                          | 29,494                | 113,625      |
| Cost of goods sold                        | 35,784                       | 947                            |                       | 36,731       |
| Net revenues                              | 45,696                       | 1,704                          | 29,494                | 76,894       |
| Operating expenses:                       |                              |                                |                       |              |
| Operations expense                        | 23,521                       | 889                            | 13,111                | 37,521       |
| Signature loan bad debt                   | 167                          |                                | 6,465                 | 6,632        |
| Total direct expenses                     | 23,688                       | 889                            | 19,576                | 44,153       |
| Store operating income                    | \$ 22,008                    | \$ 815                         | \$ 9,918              | \$ 32,741    |
| <b>Three Months Ended March 31, 2007:</b> |                              |                                |                       |              |
| Revenues:                                 |                              |                                |                       |              |
| Sales                                     | \$ 50,019                    | \$ 13                          | \$                    | \$ 50,032    |
| Pawn service charges                      | 16,548                       | 8                              |                       | 16,556       |
| Signature loan fees                       | 792                          |                                | 21,921                | 22,713       |
| Other                                     | 342                          |                                |                       | 342          |
| Total revenues                            | 67,701                       | 21                             | 21,921                | 89,643       |

Edgar Filing: EZCORP INC - Form 10-Q

|                         |           |         |          |           |
|-------------------------|-----------|---------|----------|-----------|
| Cost of goods sold      | 30,367    | 7       |          | 30,374    |
| Net revenues            | 37,334    | 14      | 21,921   | 59,269    |
| Operating expenses:     |           |         |          |           |
| Operations expense      | 21,501    | 58      | 9,545    | 31,104    |
| Signature loan bad debt | 148       |         | 2,768    | 2,916     |
| Total direct expenses   | 21,649    | 58      | 12,313   | 34,020    |
| Store operating income  | \$ 15,685 | \$ (44) | \$ 9,608 | \$ 25,249 |

11

---

**Table of Contents**

|   | EZPAWN<br>U.S.<br>Operations | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
|---|------------------------------|--------------------------------|-----------------------|--------------|
|   | <i>(in thousands)</i>        |                                |                       |              |
| <b>Six Months Ended March 31, 2008:</b> |                              |                                |                       |              |
| Revenues:                               |                              |                                |                       |              |
| Sales                                   | \$ 113,948                   | \$ 2,889                       | \$                    | \$ 116,837   |
| Pawn service charges                    | 42,710                       | 1,983                          |                       | 44,693       |
| Signature loan fees                     | 1,481                        |                                | 62,213                | 63,694       |
| Other                                   | 703                          | 4                              |                       | 707          |
| Total revenues                          | 158,842                      | 4,876                          | 62,213                | 225,931      |
| Cost of goods sold                      | 68,552                       | 1,720                          |                       | 70,272       |
| Net revenues                            | 90,290                       | 3,156                          | 62,213                | 155,659      |
| Operating expenses:                     |                              |                                |                       |              |
| Operations expense                      | 47,029                       | 1,721                          | 25,842                | 74,592       |
| Signature loan bad debt                 | 539                          |                                | 15,763                | 16,302       |
| Total direct expenses                   | 47,568                       | 1,721                          | 41,605                | 90,894       |
| Store operating income                  | \$ 42,722                    | \$ 1,435                       | \$ 20,608             | \$ 64,765    |
| <b>Six Months Ended March 31, 2007:</b> |                              |                                |                       |              |
| Revenues:                               |                              |                                |                       |              |
| Sales                                   | \$ 98,998                    | \$ 14                          | \$                    | \$ 99,012    |
| Pawn service charges                    | 34,508                       | 10                             |                       | 34,518       |
| Signature loan fees                     | 1,704                        |                                | 45,404                | 47,108       |
| Other                                   | 692                          |                                |                       | 692          |
| Total revenues                          | 135,902                      | 24                             | 45,404                | 181,330      |
| Cost of goods sold                      | 60,188                       | 9                              |                       | 60,197       |
| Net revenues                            | 75,714                       | 15                             | 45,404                | 121,133      |
| Operating expenses:                     |                              |                                |                       |              |
| Operations expense                      | 43,166                       | 120                            | 19,206                | 62,492       |
| Signature loan bad debt                 | 484                          |                                | 8,460                 | 8,944        |
| Total direct expenses                   | 43,650                       | 120                            | 27,666                | 71,436       |
| Store operating income                  | \$ 32,064                    | \$ (105)                       | \$ 17,738             | \$ 49,697    |

Edgar Filing: EZCORP INC - Form 10-Q

The following table reconciles store operating income, as shown above, to our consolidated income before income taxes:

|  | Three Months Ended<br>March 31, |           | Six Months Ended<br>March 31, |           |
|--|---------------------------------|-----------|-------------------------------|-----------|
|  | 2008                            | 2007      | 2008                          | 2007      |
|  | <i>(in thousands)</i>           |           |                               |           |
| Consolidated store operating income              | \$ 32,741                       | \$ 25,249 | \$ 64,765                     | \$ 49,697 |
| Administrative expenses                          | 9,829                           | 7,968     | 19,734                        | 15,495    |
| Depreciation and amortization                    | 3,119                           | 2,401     | 5,946                         | 4,699     |
| Interest income                                  | (137)                           | (567)     | (194)                         | (881)     |
| Interest expense                                 | 75                              | 83        | 156                           | 147       |
| Equity in net income of unconsolidated affiliate | (1,118)                         | (820)     | (2,165)                       | (1,465)   |
| Loss on sale / disposal of assets                | 81                              |           | 243                           | 24        |
| Consolidated income before income taxes          | \$ 20,892                       | \$ 16,184 | \$ 41,045                     | \$ 31,678 |

**Table of Contents**

The following table presents separately identified segment assets:

|  | EZPAWN<br>U.S.<br>Operations | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
|--|------------------------------|--------------------------------|-----------------------|--------------|
|  | <i>(in thousands)</i>        |                                |                       |              |
| <b>Assets at March 31, 2008:</b>                     |                              |                                |                       |              |
| Pawn loans   | \$ 53,243                    | \$ 3,458                       | \$                    | \$ 56,701    |
| Payday loans, net                                    | 392                          |                                | 4,898                 | 5,290        |
| Inventory, net                                       | 34,484                       | 1,515                          |                       | 35,999       |
| Total separately identified recorded segment assets  | \$ 88,119                    | \$ 4,973                       | \$ 4,898              | \$ 97,990    |
|  |                              |                                |                       |              |
| Brokered loans outstanding from unaffiliated lenders | \$ 339                       | \$                             | \$ 19,877             | \$ 20,216    |
| <b>Assets at March 31, 2007:</b>                     |                              |                                |                       |              |
| Pawn loans   | \$ 43,074                    | \$ 35                          | \$                    | \$ 43,109    |
| Payday loans, net                                    | 436                          |                                | 2,878                 | 3,314        |
| Inventory, net                                       | 28,566                       | 83                             |                       | 28,649       |
| Total separately identified recorded segment assets  | \$ 72,076                    | \$ 118                         | \$ 2,878              | \$ 75,072    |
|  |                              |                                |                       |              |
| Brokered loans outstanding from unaffiliated lenders | \$ 411                       | \$                             | \$ 16,490             | \$ 16,901    |
| <b>Assets at September 30, 2007:</b>                 |                              |                                |                       |              |
| Pawn loans   | \$ 60,602                    | \$ 140                         | \$                    | \$ 60,742    |
| Payday loans, net                                    | 457                          |                                | 4,357                 | 4,814        |
| Inventory, net                                       | 37,749                       | 193                            |                       | 37,942       |
| Total separately identified recorded segment assets  | \$ 98,808                    | \$ 333                         | \$ 4,357              | \$ 103,498   |
|  |                              |                                |                       |              |
| Brokered loans outstanding from unaffiliated lenders | \$ 477                       | \$                             | \$ 22,834             | \$ 23,311    |

Brokered loans are not recorded as an asset on our balance sheet, as we do not own a participation in the loans made by independent lenders. We monitor the principal balance of these loans, as our credit service fees and bad debt are directly related to their volume due to the letters of credit we issue on these loans. The balance shown above is the gross principal balance of the loans outstanding.



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

The discussion in this section contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those discussed in this section and throughout this report.

**Second Quarter Ended March 31, 2008 vs. Second Quarter Ended March 31, 2007**

The following table presents selected, unaudited, consolidated financial data for our three-month periods ended March 31, 2008 and 2007 (the current quarter and prior year quarter):

|                      | Three Months Ended March<br>31, |           | Percentage<br>Change |
|----------------------|---------------------------------|-----------|----------------------|
|                      | 2008                            | 2007      |                      |
|                      | <i>(in thousands)</i>           |           |                      |
| Net revenues:        |                                 |           |                      |
| Sales                | \$ 61,330                       | \$ 50,032 | 22.6%                |
| Pawn service charges | 21,785                          | 16,556    | 31.6%                |
| Signature loan fees  | 30,166                          | 22,713    | 32.8%                |
| Other                | 344                             | 342       | 0.6%                 |
| Total revenues       | 113,625                         | 89,643    | 26.8%                |
| Cost of goods sold   | 36,731                          | 30,374    | 20.9%                |
| Net revenues         | \$ 76,894                       | \$ 59,269 | 29.7%                |
| Net income           | \$ 13,016                       | \$ 10,196 | 27.7%                |

**Six Months Ended March 31, 2008 vs. Six Months Ended March 31, 2007**

The following table presents selected, unaudited, consolidated financial data for our six-month periods ended March 31, 2008 and 2007 (the current and prior year-to-date periods):

|                      | Six Months Ended March<br>31, |            | Percentage<br>Change |
|----------------------|-------------------------------|------------|----------------------|
|                      | 2008                          | 2007       |                      |
|                      | <i>(in thousands)</i>         |            |                      |
| Net revenues:        |                               |            |                      |
| Sales                | \$ 116,837                    | \$ 99,012  | 18.0%                |
| Pawn service charges | 44,693                        | 34,518     | 29.5%                |
| Signature loan fees  | 63,694                        | 47,108     | 35.2%                |
| Other                | 707                           | 692        | 2.2%                 |
| Total revenues       | 225,931                       | 181,330    | 24.6%                |
| Cost of goods sold   | 70,272                        | 60,197     | 16.7%                |
| Net revenues         | \$ 155,659                    | \$ 121,133 | 28.5%                |
| Net income           | \$ 25,571                     | \$ 19,957  | 28.1%                |

**Table of Contents**

Consolidated signature loan data (combined payday loan and credit service activities) are as follows:

|  | Three Months Ended            |           | Six Months Ended  |           |
|--|-------------------------------|-----------|-------------------|-----------|
|  | March 31,<br>2008             | 2007      | March 31,<br>2008 | 2007      |
|  | <i>(Dollars in thousands)</i> |           |                   |           |
| Fee revenue  | \$ 30,166                     | \$ 22,713 | \$ 63,694         | \$ 47,108 |
| Bad debt:  |                               |           |                   |           |
| Net defaults, including interest on brokered loans           | 6,489                         | 3,260     | 15,524            | 8,660     |
| Insufficient funds fees, net of collections                  | 235                           | 172       | 595               | 457       |
| Change in valuation allowance                                | (123)                         | (599)     | 14                | (300)     |
| Other related costs  | 31                            | 83        | 169               | 127       |
| Net bad debt   | 6,632                         | 2,916     | 16,302            | 8,944     |
| Fee revenue less bad debt                                    | \$ 23,534                     | \$ 19,797 | \$ 47,392         | \$ 38,164 |
| Average signature loan balance outstanding during period (a) | \$ 28,417                     | \$ 21,079 | \$ 28,365         | \$ 21,045 |
| Signature loan balance at end of period (a)                  | \$ 25,506                     | \$ 20,215 | \$ 25,506         | \$ 20,215 |
| Participating stores at end of period                        | 535                           | 449       | 535               | 449       |
| Signature loan bad debt, as a percent of fee revenue         | 22.0%                         | 12.8%     | 25.6%             | 19.0%     |
| Net default rate (a) (b)                                     | 4.2%                          | 2.9%      | 4.8%              | 3.7%      |

(a) Signature loan balances include payday loans (net of valuation allowance) recorded on our balance sheet and the principal portion of active brokered loans outstanding from unaffiliated lenders, the balance of which is not included on our balance sheet.

(b) Principal defaults net of collections, as a percentage of

signature loans  
made and  
renewed.

15

---

**Table of Contents****Overview**

We lend or provide credit services to individuals who do not have cash resources or access to credit to meet their short-term cash needs. As of March 31, 2008, we offer pawn loans in our 294 domestic pawn stores and 26 Mexico pawn stores. Pawn loans are non-recourse loans collateralized by tangible personal property. At these stores, we also sell merchandise, primarily collateral forfeited from our pawn lending operations, to customers looking for good value. In 462 EZMONEY stores and 73 of our domestic EZPAWN stores open March 31, 2008, we offer short-term non-collateralized loans, often called payday loans, or fee-based credit services to customers seeking loans (collectively, signature loans).

We manage our business as three segments. The EZPAWN U.S. Operations segment offers pawn related activities in all 294 domestic EZPAWN stores, and offers signature loans in 73 of our domestic EZPAWN stores and six EZMONEY stores. The EZPAWN Mexico Operations segment offers pawn related activities in 26 Mexico pawn stores. The EZMONEY Operations segment offers signature loans in 456 EZMONEY stores, and accounts for approximately 98% of our signature loan revenues. The following tables present store data by operating segment:

|   | Three Months Ended March 31, 2008 |                                |                       |              |
|---|-----------------------------------|--------------------------------|-----------------------|--------------|
|   | EZPAWN<br>U.S.<br>Operations      | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
| Stores in operation:                            |                                   |                                |                       |              |
| Beginning of period                             | 300                               | 25                             | 442                   | 767          |
| New openings                                    |                                   | 1                              | 17                    | 18           |
| Acquired  |                                   |                                |                       |              |
| Sold, combined, or closed                       |                                   |                                | (3)                   | (3)          |
| End of period                                   | 300                               | 26                             | 456                   | 782          |
| Average number of stores during the period      | 300                               | 25                             | 448                   | 773          |
|   |                                   |                                |                       |              |
|   | Six Months Ended March 31, 2008   |                                |                       |              |
|   | EZPAWN<br>U.S.<br>Operations      | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
| Stores in operation:                            |                                   |                                |                       |              |
| Beginning of period                             | 300                               | 4                              | 427                   | 731          |
| New openings                                    |                                   | 2                              | 34                    | 36           |
| Acquired  |                                   | 20                             |                       | 20           |
| Sold, combined, or closed                       |                                   |                                | (5)                   | (5)          |
| End of period                                   | 300                               | 26                             | 456                   | 782          |
| Average number of stores during the period      | 300                               | 22                             | 440                   | 761          |
| Composition of ending stores:                   |                                   |                                |                       |              |
| EZPAWN United States                            | 294                               |                                |                       | 294          |
| EZPAWN Mexico                                   |                                   | 26                             |                       | 26           |
| EZMONEY signature loan stores adjoining EZPAWNs | 6                                 |                                | 163                   | 169          |

|                                       |               |     |    |     |     |
|---------------------------------------|---------------|-----|----|-----|-----|
| EZMONEY signature loan stores         | free standing |     |    | 293 | 293 |
| Total stores in operation             |               | 300 | 26 | 456 | 782 |
| Total stores offering signature loans |               | 79  |    | 456 | 535 |
|                                       |               | 16  |    |     |     |

---

**Table of Contents**

|  | Three Months Ended March 31, 2007 |                                |                       |              |
|--|-----------------------------------|--------------------------------|-----------------------|--------------|
|  | EZPAWN<br>U.S.<br>Operations      | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
| Stores in operation:                               |                                   |                                |                       |              |
| Beginning of period                                | 286                               | 1                              | 334                   | 621          |
| New openings                                       |                                   | 1                              | 30                    | 31           |
| Acquired   |                                   |                                |                       |              |
| Sold, combined, or closed                          |                                   |                                | (1)                   | (1)          |
| End of period                                      | 286                               | 2                              | 363                   | 651          |
| Average number of stores during the period         | 286                               | 2                              | 345                   | 633          |
|  |                                   |                                |                       |              |
|  | Six Months Ended March 31, 2007   |                                |                       |              |
|  | EZPAWN<br>U.S.<br>Operations      | EZPAWN<br>Mexico<br>Operations | EZMONEY<br>Operations | Consolidated |
| Stores in operation:                               |                                   |                                |                       |              |
| Beginning of period                                | 286                               |                                | 328                   | 614          |
| New openings                                       |                                   | 2                              | 37                    | 39           |
| Acquired   |                                   |                                |                       |              |
| Sold, combined, or closed                          |                                   |                                | (2)                   | (2)          |
| End of period                                      | 286                               | 2                              | 363                   | 651          |
| Average number of stores during the period         | 286                               | 1                              | 339                   | 626          |
| Composition of ending stores:                      |                                   |                                |                       |              |
| EZPAWN United States                               | 280                               |                                |                       | 280          |
| EZPAWN Mexico                                      |                                   | 2                              |                       | 2            |
| EZMONEY signature loan stores adjoining<br>EZPAWNs | 6                                 |                                | 158                   | 164          |
| EZMONEY signature loan stores free standing        |                                   |                                | 205                   | 205          |
| Total stores in operation                          | 286                               | 2                              | 363                   | 651          |

Total stores offering signature loans 86 363 449

We earn pawn service charge revenue on our pawn lending. While allowable service charges vary by state and loan size, a majority of our U.S. pawn loans earn 20% per month, or 240% annually. Our average U.S. pawn loan amount typically ranges between \$80 and \$100 but varies depending on the valuation of each item pawned. The total U.S. loan term, consisting of the primary term and grace period, ranges between 60 and 120 days. In Mexico, a majority of our pawn loans earn pawn service charges of 13% to 14% net of applicable taxes, and the total loan term is 45 days. In our pawnshops, we acquire inventory for retail sales through pawn loan forfeitures and, to a lesser extent, through purchases of customers merchandise. The gross profit on sales of inventory depends primarily on our assessment of

the resale value at the time the property is either accepted as loan collateral or purchased. Improper assessment of the resale value in the lending or purchasing process can result in lower margins or reduced marketability of the merchandise.

At March 31, 2008, 278 of our 456 EZMONEY stores and 49 of our 294 domestic pawn stores offered credit services to customers seeking loans from unaffiliated lenders. We do not participate in any of the loans made by the lenders, but earn a fee for helping customers obtain credit and for enhancing customers' creditworthiness by providing letters of credit. We also offer a free service to all credit service customers to improve or establish their credit histories by reporting their payments to an external credit-reporting agency.

In connection with our credit services, the unaffiliated lenders offer customers two types of loans. In all 278 EZMONEY stores and 49 EZPAWN stores offering credit services, customers can obtain short-term loans, with principal amounts up to \$1,500 but averaging \$550. Terms of these short-term loans are generally less than 30 days, averaging about 18 days, with due dates corresponding with the customers' next payday. We typically earn a fee of 20% of the loan amount for our short-term loan credit services. In 72 EZMONEY stores offering credit services, customers can obtain longer-term installment loans from the unaffiliated lenders. The installment loans typically

**Table of Contents**

carry terms of about five months with ten equal installment payments due on customers' paydays. Installment loan principal amounts range from \$1,525 to \$3,000, but average about \$2,100. With each installment payment, we earn a fee of 10% of the initial loan amount. At March 31, 2008, short-term loans comprised 98% of the balance of loans brokered through our credit services, and installment loans comprised the remaining 2%.

We earn payday loan fee revenue on our payday loans. In 24 pawn stores and 184 EZMONEY stores, we make payday loans subject to state law. The average payday loan amount is approximately \$435 and the term is generally less than 30 days, averaging about 18 days. We typically charge a fee of 15% to 22% of the loan amount for a 7 to 23-day period.

On June 18, 2007, we completed the acquisition of fifteen pawnshops and one payday loan store from Jumping Jack Cash, a competitor in Colorado for \$23.2 million of cash and direct transaction costs. Results of the acquired stores are included in our consolidated results from the date of acquisition.

On October 22, 2007, we completed the acquisition of twenty Mexico pawnshops from MMFS Intl., S.A. de C.V., a subsidiary of Mister Money Holdings, Inc. for \$15.4 million cash and direct transaction costs. Results of the acquired stores are included in our consolidated results from the date of acquisition.

On March 17, 2008, we announced our agreement to acquire up to 100%, but not less than 70%, of the equity ownership of Value Financial Services, Inc. for approximately \$100 million, subject to our due diligence review. Value Financial Services currently owns and operates 65 pawn stores in Florida, Tennessee, and Georgia, including one opened since our announcement of the planned acquisition. On April 28, 2008, we amended the agreement to extend the due diligence period to May 13, 2008 and the expected closing date to June 26, 2008, among other related changes. The remainder of this discussion and analysis excludes the potential impact of this pending acquisition, as its completion is not yet assured.

In the current quarter, the EZPAWN U.S. Operations segment contributed \$6.3 million greater store operating income compared to the prior year quarter, primarily from an increase in same store pawn service charges, the same store gross profit from gold scrapping, and the contribution from 15 Colorado pawn stores acquired in June 2007. The EZPAWN Mexico Operations segment improved its store operating income by \$0.9 million, primarily due to the acquisition of twenty stores in October 2007. Our EZMONEY Operations segment contributed \$0.3 million greater store operating income, comprised of higher fees net of bad debt, offset by higher operating costs. After an increase in administrative expenses and depreciation and less material changes in other items, our consolidated net income improved to \$13.0 million in the current quarter from \$10.2 million in the prior year quarter.



**Table of Contents****Results of Operations****Second Quarter Ended March 31, 2008 vs. Second Quarter Ended March 31, 2007**

The following discussion compares our results of operations for the quarter ended March 31, 2008 (the current quarter) to the quarter ended March 31, 2007 (the prior year quarter). The discussion should be read with the accompanying financial statements and related notes.

**EZPAWN U.S. Operations Segment**

The following table presents selected financial data for the EZPAWN U.S. Operations segment:

|   | Three Months Ended March<br>31, |           |
|---|---------------------------------|-----------|
|   | 2008                            | 2007      |
|   | <i>(Dollars in thousands)</i>   |           |
| Sales   | \$ 59,747                       | \$ 50,019 |
| Pawn service charges  | 20,720                          | 16,548    |
| Signature loan fees   | 672                             | 792       |
| Other   | 341                             | 342       |
| Total revenues  | 81,480                          | 67,701    |
| Cost of goods sold  | 35,784                          | 30,367    |
| Net revenues  | 45,696                          | 37,334    |
| Operating expenses:   |                                 |           |
| Operations expense  | 23,521                          | 21,501    |
| Signature loan bad debt   | 167                             | 148       |
| Total store operating expenses  | 23,688                          | 21,649    |
| Store operating income  | \$ 22,008                       | \$ 15,685 |
| Other data:   |                                 |           |
| Gross margin on sales   | 40%                             | 39%       |
| Annualized inventory turnover   | 3.8x                            | 3.8x      |
| Average pawn loan balance per pawn store at quarter end                                 | \$ 181                          | \$ 154    |
| Average inventory per pawn store at quarter end   | \$ 117                          | \$ 102    |
| Average yield on pawn loan portfolio (a)  | 150%                            | 150%      |
| Pawn loan redemption rate   | 81%                             | 80%       |
| Average signature loan balance per store offering signature loans at quarter end<br>(b) | \$ 9                            | \$ 10     |

(a) Average yield on pawn loan portfolio is calculated as annualized pawn service charge revenue for the period divided by the

average pawn  
loan balance  
during the  
period.

- (b) Signature loan  
balances include  
payday loans  
(net of valuation  
allowance)  
recorded on our  
balance sheet  
and the  
principal portion  
of active  
brokered loans  
outstanding  
from  
unaffiliated  
lenders, the  
balance of  
which is not  
included on our  
balance sheet.

Our current quarter U.S. pawn service charge revenue increased 25%, or \$4.2 million from the prior year quarter to \$20.7 million. This increase was due to a 17%, or \$2.9 million increase in same store pawn service charges and a \$1.3 million increase in pawn service charges at acquired stores. The same store improvement was due primarily to a higher average pawn loan balance, with the yield relatively unchanged. We have periodically raised our loan values on gold jewelry in response to increases in gold market values and similar changes by our competitors, including three increases over the last year. This contributed about \$2.0 million to the increase in U.S. pawn service charges in the current quarter.

**Table of Contents**

The table below presents our sales volume, gross profit, and gross margins in the EZPAWN U.S. Operations segment:

|   | Three Months Ended March     |         |
|---|------------------------------|---------|
|   | 2008                         | 2007    |
|   | 31,                          |         |
|   | <i>(Dollars in millions)</i> |         |
| Merchandise sales                       | \$ 43.3                      | \$ 39.5 |
| Jewelry scrapping sales                 | 16.4                         | 10.5    |
| Total sales                             | \$ 59.7                      | \$ 50.0 |
| Gross profit on merchandise sales       | \$ 17.0                      | \$ 15.9 |
| Gross profit on jewelry scrapping sales | \$ 7.0                       | \$ 3.7  |
| Gross margin on merchandise sales       | 39.2%                        | 40.3%   |
| Gross margin on jewelry scrapping sales | 42.6%                        | 35.4%   |
| Overall gross margin                    | 40.1%                        | 39.3%   |

The current quarter's merchandise gross profit increased \$1.1 million from the prior year quarter to \$17.0 million. This was due to additional sales from the fifteen pawn stores acquired in June 2007 and a four percent same store sales increase, partially offset by a 1.1 percentage point decrease in gross margins to 39.2%. The decrease in gross margins was the result of higher levels of discounting merchandise.

The current quarter's gross profit on jewelry scrapping sales increased \$3.3 million from the prior year quarter to \$7.0 million. This was due to a \$5.9 million increase in jewelry scrapping sales on 19% more volume and a 7.2 percentage point improvement in margins. The proceeds refiners pay us for jewelry has increased in the last year in response to higher gold values. We also increased the amount we loan on jewelry and pay to purchase jewelry from customers, increasing the cost of these items. The net effect of these factors comprises most of the improvement in gross profit from jewelry scrapping sales in the current quarter.

Merchandise and jewelry scrapping sales volume is heavily dependent on inventory available for sale, or beginning inventory on hand plus pawn loan forfeitures and inventory purchases. Inventory available for sale in the current quarter was 17% higher than in the prior year quarter, largely due to same store pawn loan growth and the related increase in loan forfeitures and the June 2007 acquisition of fifteen pawn stores. Total merchandise sales for the quarter were 10% above the prior year quarter.

The segment's signature loan contribution, or fee revenue less bad debt, decreased \$0.1 million in the current quarter compared to the prior year quarter due to lower fee revenues on a lower average loan balance, combined with an increase in signature loan bad debt from 18.7% of fees in the prior year quarter to 24.9% in the current quarter. Operations expense improved to 51% of net revenues (\$23.5 million) in the current quarter from 58% of net revenues (\$21.5 million) in the prior year quarter as operating expenses grew at a slower pace than the segment's net revenues. In the current quarter, the \$8.4 million greater net revenue from U.S. pawn activities, partially offset by the \$2.0 million higher operations expense and \$0.1 million lower contribution from signature loans resulted in a \$6.3 million overall increase in store operating income from the EZPAWN U.S. Operations segment compared to the prior year quarter. For the current quarter, the EZPAWN U.S. Operations segment made up 67% of consolidated store operating income compared to 62% in the prior year quarter.

**Table of Contents****EZPAWN Mexico Operations Segment**

The following table presents selected financial data for the EZPAWN Mexico Operations segment:

|   | Three Months Ended March<br>31, |         |
|---|---------------------------------|---------|
|   | 2008                            | 2007    |
|   | <i>(Dollars in thousands)</i>   |         |
| Sales   | \$ 1,583                        | \$ 13   |
| Pawn service charges                                    | 1,065                           | 8       |
| Signature loan fees                                     |                                 |         |
| Other   | 3                               |         |
| Total revenues  | 2,651                           | 21      |
| Cost of goods sold                                      | 947                             | 7       |
| Net revenues  | 1,704                           | 14      |
| Operating expenses:                                     |                                 |         |
| Operations expense                                      | 889                             | 58      |
| Signature loan bad debt                                 |                                 |         |
| Total store operating expenses                          | 889                             | 58      |
| Store operating income                                  | \$ 815                          | \$ (44) |
| Other data:   |                                 |         |
| Gross margin on sales                                   | 40%                             | 46%     |
| Annualized inventory turnover                           | 2.7x                            | 0.7x    |
| Average pawn loan balance per pawn store at quarter end | \$ 133                          | \$ 18   |
| Average inventory per pawn store at quarter end         | \$ 58                           | \$ 42   |
| Average yield on pawn loan portfolio (a)                | 136%                            | 188%    |

(a) Average yield on pawn loan portfolio is calculated as annualized pawn service charge revenue for the period divided by the average pawn loan balance during the period.

In the prior year quarter, our EZPAWN Mexico Operations segment included the results from our first two stores opened in the first and second quarters of fiscal 2007. The current quarter results include results from those stores, the twenty stores acquired October 22, 2007, and the four additional stores opened since the end of the prior year quarter. The table below presents our sales volume, gross profit, and gross margins in the EZPAWN Mexico Operations segment:

|   | Three Months Ended March<br>31, |       |
|---|---------------------------------|-------|
|   | 2008                            | 2007  |
|   | <i>(Dollars in thousands)</i>   |       |
| Merchandise sales                       | \$ 1,374                        | \$ 13 |
| Jewelry scrapping sales                 | 209                             |       |
| Total sales                             | \$ 1,583                        | \$ 13 |
| Gross profit on merchandise sales       | \$ 551                          | \$ 6  |
| Gross profit on jewelry scrapping sales | \$ 85                           | \$    |
| Gross margin on merchandise sales       | 40.1%                           | 46.2% |
| Gross margin on jewelry scrapping sales | 40.7%                           | N/A   |
| Overall gross margin                    | 40.2%                           | 46.2% |

The current quarter's merchandise gross profit increased to \$0.6 million on \$1.4 million of sales due to new and acquired stores. Gross margins on merchandise sales were 40.1%.

The current quarter's gross profit on jewelry scrapping sales was \$0.1 million on \$0.2 million of proceeds. Gross margins on jewelry scrapping sales were 40.7%.

**Table of Contents**

Operations expense was 52% of segment net revenues (\$0.9 million) in the current quarter. Operating expenses exceeded net revenues in the prior year quarter during the start-up period of our Mexico operations.

In the current quarter, the \$1.7 million greater net revenue from Mexico pawn activities, partially offset by the \$0.8 million higher operations expense resulted in a \$0.9 million overall increase in store operating income from the EZPAWN Mexico Operations segment compared to the prior year quarter. For the current quarter, the EZPAWN Mexico Operations segment made up three percent of consolidated store operating income, compared to a small loss in the start-up period in the prior year quarter.

**EZMONEY Operations Segment**

The following table presents selected financial data for the EZMONEY Operations segment:

|  | Three Months Ended March<br>31, |           |
|--|---------------------------------|-----------|
|  | 2008                            | 2007      |
|  | <i>(Dollars in thousands)</i>   |           |
| Signature loan fees  | \$ 29,494                       | \$ 21,921 |
| Signature loan bad debt  | 6,465                           | 2,768     |
| Fee revenue less bad debt  | 23,029                          | 19,153    |
| Operations expense   | 13,111                          | 9,545     |
| Store operating income   | \$ 9,918                        | \$ 9,608  |
| Other data:  |                                 |           |
| Signature loan bad debt as a percent of signature loan fees  | 21.9%                           | 12.6%     |
| Average signature loan balance per store offering signature loans at quarter end   |                                 |           |
| (a)  | \$ 54                           | \$ 53     |
| (a) Signature loan balances include payday loans (net of valuation allowance) recorded on our balance sheet and the principal portion of active brokered loans outstanding from unaffiliated lenders, the balance of which is not included on our balance sheet. |                                 |           |

The segment's signature loan contribution, or fees less bad debt, increased \$3.9 million, or 20% compared to the prior year quarter. The primary drivers of the increased contribution were the higher average loan balances at existing stores and the addition of new stores, resulting in a 35% increase in the current quarter signature loan fee revenue. Signature loan bad debt increased \$3.7 million to 21.9% of related fees in the current quarter compared to 12.6% in the prior year quarter. We believe the current macro-economic pressures on our customers, their employment, and general access to cash to repay their debts was the primary cause of our increased difficulty in collecting bad debt in the quarter. For the past several years, we also have sold our bad debt, on a weekly basis, to third parties after 60 days of internal collection efforts, but saw market rates for debt sales decline in the current quarter. We are now continuing to work our bad debt past 60 days and employ a combination of in-house collections, third party debt sales, and testing several new ancillary collection techniques.

Operations expense increased \$3.6 million in the current quarter to \$13.1 million, but remained unchanged from the prior year quarter at 44% of segment net revenues. The dollar increase was from additional labor, rent, and other costs at new and existing stores. In the current quarter, operations expense was \$29,300 per average store, compared to \$27,700 in the prior year quarter.

In the current quarter, the \$3.9 million increase in signature loan fees net of bad debt and \$3.6 million greater operations expense resulted in a \$0.3 million net increase in store operating income from the EZMONEY Operations segment. For the current quarter, the EZMONEY Operations made up 30% of consolidated store operating income compared to 38% in the prior year quarter.

**Table of Contents****Other Items**

The items discussed below affect our consolidated financial results, but are not allocated between segments. Administrative expenses in the current quarter were \$9.8 million compared to \$8.0 million in the prior year quarter, or 12.8% of net revenues compared to 13.4% in the prior year quarter. The increase was due primarily to a \$0.8 million increase in administrative labor and benefits as we build the infrastructure to support our continued growth and a \$0.7 million increase in professional fees.

Depreciation and amortization expense was \$3.1 million in the current quarter, compared to \$2.4 million in the prior year quarter. Depreciation on assets placed in service, primarily related to new EZMONEY stores and acquired pawn stores, exceeded the reduction from assets that became fully depreciated or were retired in the period. We experienced increased amortization of intangible assets acquired with the two acquisitions since the end of the prior year quarter. We earned \$0.1 million of interest income on our invested cash in the current quarter, for an annualized rate of return of 3.1%. In the comparable prior year quarter, we earned \$0.6 million of interest income on our invested cash, yielding 5.1%.

Our \$0.1 million interest expense in the current and prior year quarter was comprised mostly of the amortization of deferred financing costs and the commitment fee on our line of credit, as we had no debt in either period.

Our equity interest in the earnings of Albemarle & Bond increased \$0.3 million in the current quarter to \$1.1 million. The increase was a result of A&B's continued same store improvement in earnings, the additional income A&B earned from the 26 stores it acquired in July 2007, and our incremental investment in A&B in July 2007.

The current quarter income tax expense was \$7.9 million (37.7% of pretax income) compared to \$6.0 million (37.0% of pretax income) for the prior year quarter. The increase in effective tax rate between these periods is due to anticipated higher state taxes.

Consolidated operating income for the current quarter improved \$4.9 million over the prior year quarter to \$19.8 million. Contributing to this were the \$6.3 million, \$0.9 million and \$0.3 million increases in store operating income in our EZPAWN U.S., EZPAWN Mexico and EZMONEY Operations segments, partially offset by the \$1.9 million increase in administrative expenses. After a \$0.7 million increase in depreciation and amortization and a \$1.9 million increase in income taxes and other smaller items, net income improved to \$13.0 million in the current quarter from \$10.2 million in the prior year quarter.



**Table of Contents****Six Months Ended March 31, 2008 vs. Six Months Ended March 31, 2007**

The following discussion compares our results of operations for the six months ended March 31, 2008 to the six months ended March 31, 2007. The discussion should be read with the accompanying financial statements and related notes.

**EZPAWN U.S. Operations Segment**

The following table presents selected financial data for the EZPAWN U.S. Operations segment:

|  | Six Months Ended March 31,    |           |
|--|-------------------------------|-----------|
|  | 2008                          | 2007      |
|  | <i>(Dollars in thousands)</i> |           |
| Sales  | \$ 113,948                    | \$ 98,998 |
| Pawn service charges   | 42,710                        | 34,508    |
| Signature loan fees  | 1,481                         | 1,704     |
| Other  | 703                           | 692       |
| <br>   |                               |           |
| Total revenues   | 158,842                       | 135,902   |
| Cost of goods sold   | 68,552                        | 60,188    |
| <br>   |                               |           |
| Net revenues   | 90,290                        | 75,714    |
| Operating expenses:  |                               |           |
| Operations expense   | 47,029                        | 43,166    |
| Signature loan bad debt  | 539                           | 484       |
| <br>   |                               |           |
| Total store operating expenses   | 47,568                        | 43,650    |
| <br>   |                               |           |
| Store operating income   | \$ 42,722                     | \$ 32,064 |
| <br>   |                               |           |
| Other data:  |                               |           |
| Gross margin on sales  | 40%                           | 39%       |
| Annualized inventory turnover  | 3.5x                          | 3.5x      |
| Average pawn loan balance per pawn store at quarter end                              | \$ 181                        | \$ 154    |
| Average inventory per pawn store at quarter end                                      | \$ 117                        | \$ 102    |
| Average yield on pawn loan portfolio (a)   | 148%                          | 149%      |
| Pawn loan redemption rate  | 79%                           | 78%       |
| Average signature loan balance per store offering signature loans at quarter end (b) | \$ 9                          | \$ 10     |

(a) Average yield on pawn loan portfolio is calculated as annualized pawn service charge revenue for the period divided by the average pawn loan balance during the

period.

- (b) Signature loan balances include payday loans (net of valuation allowance) recorded on our balance sheet and the principal portion of active brokered loans outstanding from unaffiliated lenders, the balance of which is not included on our balance sheet.

Our current year-to-date U.S. pawn service charge revenue increased 24%, or \$8.2 million from the prior year to \$42.7 million. This increase was due to a 16%, or \$5.5 million increase in same store pawn service charges and \$2.7 million of pawn service charges at acquired stores. The same store improvement was due primarily to a higher average pawn loan balance, partially offset by a one percentage point lower yield. We have periodically raised our loan values on gold jewelry in response to increases in gold market values and similar changes by our competitors, including three increases over the last year. This contributed about \$3.8 million to the increase in U.S. pawn service charges in the current year-to-date period.

**Table of Contents**

The table below presents our sales volume, gross profit, and gross margins in the EZPAWN U.S. Operations segment:

|   | Six Months Ended March<br>31, |             |
|---|-------------------------------|-------------|
|   | 2008                          | 2007        |
|   | <i>(Dollars in millions)</i>  |             |
| Merchandise sales                       | \$ 82.7                       | \$ 77.4     |
| Jewelry scrapping sales                 | 31.2                          | 21.6        |
| <br>Total sales                         | <br>\$ 113.9                  | <br>\$ 99.0 |
| <br>Gross profit on merchandise sales   | <br>\$ 32.8                   | <br>\$ 31.2 |
| Gross profit on jewelry scrapping sales | \$ 12.6                       | \$ 7.6      |
| <br>Gross margin on merchandise sales   | <br>39.6%                     | <br>40.4%   |
| Gross margin on jewelry scrapping sales | 40.4%                         | 35.1%       |
| Overall gross margin                    | 39.8%                         | 39.2%       |

The current year-to-date period's merchandise gross profit increased \$1.6 million from the prior year-to-date period to \$32.8 million. This was due to \$4.5 million of additional sales from the fifteen pawn stores acquired in June 2007 and a one percentage point increase in same store sales, partially offset by a decrease of 0.8 of a percentage point in gross margins to 39.6%.

The current year-to-date period's gross profit on jewelry scrapping sales increased \$5.0 million from the prior year-to-date period to \$12.6 million. This was due to a \$9.6 million increase in jewelry scrapping sales on 12% more volume and a 5.3 percentage point improvement in margins. The jewelry scrapping sales include the current year-to-date period sale of approximately \$0.3 million of loose diamonds removed from scrapped jewelry, compared to approximately \$0.5 million in the prior year-to-date period. The proceeds refiners pay us for jewelry has increased in the last year in response to higher gold values. We also increased the amount we loan on jewelry and pay to purchase jewelry from customers, increasing the cost of these items. The net effect of these factors comprises most of the improvement in gross profit from jewelry scrapping sales in the current year-to-date period.

The segment's signature loan contribution, or fee revenue less bad debt, decreased \$0.3 million in the current year-to-date period due to lower fee revenues on a lower average loan balance, combined with an increase in signature loan bad debt from 28.4% of fees in the prior year-to-date period to 36.4% in the current year-to-date period.

Operations expense improved to 52% of net revenues (\$47.0 million) in the current year-to-date period from 57% of net revenues (\$43.2 million) in the prior year-to-date period as operating expenses grew at a slower pace than the segment's net revenues.

In the current year-to-date period, the \$14.8 million greater net revenue from U.S. pawn activities, partially offset by the \$3.8 million higher operations expense and \$0.3 million lower contribution from signature loans resulted in a \$10.7 million overall increase in store operating income from the EZPAWN U.S. Operations segment compared to the prior year-to-date period. For the current year-to-date period, the EZPAWN U.S. Operations segment made up 66% of consolidated store operating income compared to 65% in the prior year-to-date period.

**Table of Contents****EZPAWN Mexico Operations Segment**

The following table presents selected financial data for the EZPAWN Mexico Operations segment:

|   | Six Months Ended March<br>31, |          |
|---|-------------------------------|----------|
|   | 2008                          | 2007     |
|   | <i>(Dollars in thousands)</i> |          |
| Sales   | \$ 2,889                      | \$ 14    |
| Pawn service charges                                    | 1,983                         | 10       |
| Signature loan fees                                     |                               |          |
| Other   | 4                             |          |
| <br>  |                               |          |
| Total revenues  | 4,876                         | 24       |
| Cost of goods sold                                      | 1,720                         | 9        |
| <br>  |                               |          |
| Net revenues  | 3,156                         | 15       |
| Operating expenses:                                     |                               |          |
| Operations expense                                      | 1,721                         | 120      |
| Signature loan bad debt                                 |                               |          |
| <br>  |                               |          |
| Total store operating expenses                          | 1,721                         | 120      |
| <br>  |                               |          |
| Store operating income                                  | \$ 1,435                      | \$ (105) |
| <br>  |                               |          |
| Other data:   |                               |          |
| Gross margin on sales                                   | 41%                           | 36%      |
| Annualized inventory turnover                           | 1.9x                          | 0.4x     |
| Average pawn loan balance per pawn store at quarter end | \$ 133                        | \$ 18    |
| Average inventory per pawn store at quarter end         | \$ 58                         | \$ 42    |
| Average yield on pawn loan portfolio (a)                | 138%                          | 127%     |

September 30, 2015 and 2014

Note 5 – Investments (continued)

During the year ended September 30, 2015, the Plan's investments, including gains and losses on investments bought and sold, as well as held during each period, appreciated in value as follows:

|   |           |
|---|-----------|
| Stable value common collective trust fund     | \$20,275  |
| Other common collective trust funds           | 22,576    |
| Bancorp common stock                          | 269,180   |
| <br>  |           |
| Net appreciation in fair value of investments | \$312,031 |

The Stable value common collective trust fund is administrated by MetLife. The average yield and crediting interest rates were approximately 2.0% and 2.6%, respectively for the Plan year 2015. The average yield and crediting interest rates were approximately 1.8% and 2.4%, respectively for the Plan year 2014.

Note 6 – Related Party Note Payable

The Plan's term loan agreement with Bancorp (a related party) maturing March 31, 2019, has an interest rate of 8.5 percent and annual payments of \$588,870. The note is guaranteed by the Company and remains partially collateralized by unallocated shares of Bancorp common stock.

Note 7 – Employer Contributions

The Company is obligated to make contributions in cash to the Plan for the ESOP component, which, when aggregated with the Plan's dividends and interest earnings, equal the amount necessary to enable the Plan to make its regularly scheduled payments of principal and interest on the term loan. In addition, the Company is obligated to make an annual safe-harbor contribution of three percent of eligible compensation into the 401(k) component which totaled \$312,985 for the year ended September 30, 2015. At the discretion of the Board of Directors, the Company may make an additional profit sharing contribution to the 401(k) component of the Plan. For the year ended September 30, 2015, there was no such discretionary contribution.

Note 8 – Risks and Uncertainties

The Plan invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in the value of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported on the statement of net assets available for benefits.

## Notes to Financial Statements

---

 Timberland Bank Employee Stock Ownership and 401(k) Plan  
 September 30, 2015 and 2014

## Note 9 – Fair Value of Investments

The authoritative guidance established a three-tiered fair value hierarchy that prioritizes inputs to valuation techniques in fair value calculations. The three levels of inputs are defined as follows:

Level 1 – unadjusted quoted prices for identical assets or liabilities in active markets accessible by the Company.

Level 2 – inputs that are observable in the marketplace other than those inputs classified as Level 1

Level 3 – inputs that are unobservable in the marketplace and significant to the valuation

The guidance on fair value of financial instruments requires the Plan to maximize the use of observable inputs and minimize the use of unobservable inputs. If a financial instrument uses inputs that fall in different levels of the hierarchy, the instrument will be categorized based upon the lowest level of input that is significant to the fair value calculation.

The following table summarizes the balances of assets measured at fair value on a recurring basis at September 30, 2015 and 2014:

| 2015                                       | Fair Value          |                    |                  | Total               |
|--|---------------------|--------------------|------------------|---------------------|
|  | Level 1             | Level 2            | Level 3          |                     |
| <b>Available for Sale Securities</b>       |                     |                    |                  |                     |
| Bancorp common stock                       | \$10,478,413        | \$--               | \$--             | \$10,478,413        |
| Stable value common collective trust funds | --                  | --                 | 968,624          | 968,624             |
| Other common collective trust funds        | --                  | 8,940,649          | --               | 8,940,649           |
| <b>Total</b>                               | <b>\$10,478,413</b> | <b>\$8,940,649</b> | <b>\$968,624</b> | <b>\$20,387,686</b> |

| 2014                                       | Fair Value          |                    |                  | Total               |
|--|---------------------|--------------------|------------------|---------------------|
|  | Level 1             | Level 2            | Level 3          |                     |
| <b>Available for Sale Securities</b>       |                     |                    |                  |                     |
| Bancorp common stock                       | \$10,809,560        | \$--               | \$--             | \$10,809,560        |
| Stable value common collective trust funds | --                  | --                 | 711,865          | 711,865             |
| Other common collective trust funds        | --                  | 9,579,589          | --               | 9,579,589           |
| <b>Total</b>                               | <b>\$10,809,560</b> | <b>\$9,579,589</b> | <b>\$711,865</b> | <b>\$21,101,014</b> |

## Note 10 – Subsequent Events

On October 2, 2015 the plan administrator changed from Pentegra Retirement Services to LT Trust and the trustees changed from Reliance Trust Company and Pentegra Trust Company to LT Trust.



## Notes to Financial Statements

---

 Timberland Bank Employee Stock Ownership and 401(k) Plan  
 September 30, 2015 and 2014

## Note 11 – Reconciliation of Financial Statements to Form 5500

The following is a reconciliation of differences between net assets available for benefits per the financial statements to the Form 5500 for the year ended September 30, 2015:

|   | Account<br>Balance per<br>Financial<br>Statements | Variance    | Balance per<br>Form 5500 |
|---|---|-------------|--------------------------|
| Cash and cash equivalents   | \$38,040  | \$1,536,749 | \$1,574,789              |
| Common collective trust funds   | 9,909,273   | (1,560,747) | 8,348,526                |
| Adjustment from fair value to<br>contract value of fully benefit<br>responsive investment contracts | (23,998 )   | 23,998      | --                       |
| Total   | \$9,923,315                                       | \$--        | \$9,923,315              |

The following is a reconciliation of differences between net assets available for benefits per the financial statements to the Form 5500 for the year ended September 30, 2014:

|   | Account<br>Balance per<br>Financial<br>Statements | Variance    | Balance per<br>Form 5500 |
|---|---|-------------|--------------------------|
| Cash and cash equivalents   | \$44,551  | \$1,617,397 | \$1,661,948              |
| Common collective trust funds   | 10,291,454  | (1,618,954) | 8,672,500                |
| Adjustment from fair value to<br>contract value of fully benefit<br>responsive investment contracts | (1,557 )  | 1,557       | --                       |
| Total   | \$10,334,448                                      | \$--        | \$10,334,448             |

The Plan's Administrator has classified the Plan's State Street Global Advisors Common Collective Trust Short Term Investment Fund as a cash equivalent for reporting on the Form 5500. This investment has been classified as an investment for financial statement reporting purpose.



Supplemental  
Schedule

## Schedule H, Line 4i - Schedule of Assets (Held at End of Year)

Timberland Bank Employee Stock Ownership and 401(k) Plan  
September 30, 2015

EIN: 20-5645878

Plan #: 002

| (a) and (b)<br>Identity of Issue,<br>Borrower, Lessor<br>or Similar Party | (c)<br>Description of Investment, Including<br>Maturity Date, Rate of Interest,<br>Collateral, Par or Maturity Value | (d)<br>Cost | (e)<br>Current<br>Value |
|---|--|-------------|-------------------------|
| Stable Value Common Collective Trust Fund                                 |  |             |                         |
| MetLife   | Pentegra Stable Value Fund, at fair value  | \$ *        | \$ 968,624              |
| Employer Stock  |  |             |                         |
| **Timberland Bancorp, Inc.  | Common Stock – 678,182 Shares  | 5,082,974   | 7,385,402               |
| **Timberland Bancorp, Inc.  | Common Stock – 284,023 Shares  | *           | 3,093,011               |
|   |  |             | 10,478,413              |
| Other Common Collective Trust Funds                                       |  |             |                         |
| State Street Global Advisors  | Common Collective Trust Short Term Investment Fund   | *           | 1,536,749               |
| State Street Global Advisors  | Russell 2000 Index SL Series Fund – Class A  | *           | 1,105,649               |
| State Street Global Advisors  | S&P 500 Flagship SL Series Fund – Class A  | *           | 1,086,599               |
| State Street Global Advisors  | Moderate Strategic Balanced SL Fund  | *           | 984,834                 |
| State Street Global Advisors  | Aggressive Strategic Balanced SL Fund  | *           | 754,439                 |
| State Street Global Advisors  | Daily EAFE Index SL Series Fund – Class T  | *           | 549,738                 |
| State Street Global Advisors  | Russell Large Cap Value Index NL SF CL A   | *           | 418,566                 |
| State Street Global Advisors  | S&P Midcap Index SL Series Fund – Class A  | *           | 364,652                 |
| State Street Global Advisors  | NASDAQ 100 Index Non-Lending Fund Series A   | *           | 353,067                 |
| State Street Global Advisors  | Russell Large Cap Growth Index NL SF CL A  | *           | 316,643                 |
| State Street Global Advisors  | Passive Bond Market Index SL Series Fund A   | *           | 278,767                 |
| State Street Global Advisors  | REIT Index Non-Lending Series Fund – Class A   | *           | 241,684                 |



Schedule H, Line 4i - Schedule of Assets (Held at End of Year) (continued)  
 Timberland Bank Employee Stock Ownership and 401(k) Plan

September 30, 2015

EIN: 20-5645878

Plan #: 002

| (a) and (b)<br>Identity of Issue,<br>Borrower, Lessor<br>or Similar Party | (c)<br>Description of Investment, Including<br>Maturity Date, Rate of Interest,<br>Collateral, Par or Maturity Value | (d)<br>Cost | (e)<br>Current<br>Value |
|---|--|-------------|-------------------------|
| Other Common Collective Trust Funds (continued)                           |  |             |                         |
| State Street Global Advisors  | Long US Treasury Index SL Series<br>Fund Class A   | *           | 199,726                 |
| State Street Global Advisors  | Conservative Strategic Balanced SL<br>Fund   | *           | 177,958                 |
| State Street Global Advisors  | Target Retirement Fund 2025  | *           | 149,988                 |
| State Street Global Advisors  | Target Retirement Fund 2020  | *           | 111,716                 |
| State Street Global Advisors  | Target Retirement Fund 2015  | *           | 111,573                 |
| State Street Global Advisors  | Target Retirement Fund 2035  | *           | 86,898                  |
| State Street Global Advisors  | Target Retirement Fund 2045  | *           | 60,973                  |
| State Street Global Advisors  | Target Retirement Fund 2055  | *           | 18,802                  |
| State Street Global Advisors  | Target Retirement Fund 2030  | *           | 13,180                  |
| State Street Global Advisors  | Target Retirement Fund 2040  | *           | 11,171                  |
| State Street Global Advisors  | Target Retirement Fund 2050  | *           | 6,433                   |
| State Street Global Advisors  | Target Retirement Income Fund  | *           | 844                     |
|   |  |             | 8,940,649               |
|   |  |             | \$20,387,686            |

\* Historical cost not required for participant-directed accounts.

\*\*Represents a party-in-interest

