

# REDKNEE

**REDKNEE SOLUTIONS INC.**  
***MANAGEMENT'S DISCUSSION AND ANALYSIS***  
**FOR THE THIRD QUARTER ENDED JUNE 30, 2012**

**DATED: August 8, 2012**

## SCOPE OF ANALYSIS

The following discussion and analysis (“MD&A”) should be read in conjunction with the Unaudited Interim Condensed Consolidated Financial Statements for the three and nine-months ended June 30, 2012, which we prepared in accordance with International Financial Reporting Standards (“IFRS”) and with our Annual Consolidated Financial Statements for the year ended September 30, 2011, which we prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). The transition to IFRS required a restatement of the Company’s fiscal 2011 financial information from its original Canadian GAAP basis to IFRS as noted in Note 12 to the interim condensed consolidated financial statements. Readers of the MD&A should refer to “Changes in Accounting Policies” below, and Note 12 of the accompanying interim condensed consolidated financial statements, for a discussion of IFRS and its impact on the Company’s financial statements.

Financial information for periods prior to October 1, 2010 have not been restated for the changes in accounting policies resulting from the adoption of IFRS. For the purposes of this MD&A, the term “Canadian GAAP” refers to Canadian generally accepted accounting principles for the Company before the adoption of IFRS.

Certain information included herein is forward-looking and based upon assumptions and anticipated results that are subject to uncertainties. Should one or more of these uncertainties materialize or should the underlying assumptions prove incorrect, actual results may vary significantly from those expected. See “Forward-Looking Statements” and “Risks and Uncertainties”. The interim condensed consolidated financial statements and the MD&A have been reviewed by Redknee’s Audit Committee and approved by its Board of Directors.

Effective October 1, 2011, the functional currencies of the Company and its subsidiaries were changed from the Canadian dollar to the U.S. dollar. The changes in functional currencies were a result of the increased influence of the U.S. dollar on the economic environment in which the companies operate and the increased reliance on U.S. dollar financing. The financial reporting presentation currency of the Company was also changed to U.S. dollar.

Unless otherwise indicated, all dollar amounts are expressed in U.S. dollars. In this document, “we,” “us,” “our,” “Company” and “Redknee” all refer to Redknee Solutions Inc. collectively with its subsidiaries.

## ADDITIONAL INFORMATION

Additional information relating to the Company including our most recently completed Annual Information Form (“AIF”) is available on SEDAR at [www.sedar.com](http://www.sedar.com) and on the Company’s web-site at [www.redknee.com](http://www.redknee.com).

## FORWARD-LOOKING STATEMENTS

Certain statements in this document may constitute “forward-looking” statements which involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. When used in this document, such statements use such words as “may”, “will”, “expect”, “continue”, “believe”, “plan”, “intend”, “would”, “could”, “should”, “anticipate” and other similar terminology. These statements reflect current assumptions and expectations regarding future events and operating performance and speak only as of the date of this document. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to vary significantly from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under the “Risk Factors” section of the Company’s the most recently filed AIF. Although the forward-looking statements contained in this document are based upon what we believe are reasonable assumptions, we cannot assure investors that our actual results will be consistent with these forward-looking statements. We assume no obligation to update or revise these forward-looking statements to reflect new events or circumstances, except as required by securities law.

## OVERVIEW

Redknee Solutions Inc. was incorporated on March 29, 1999 and commenced operations in July, 1999. Redknee is a leading provider of revenue generating software products, solutions and services to some of the largest network operators throughout the world, including wireless, wireline, broadband and satellite. Redknee delivers solutions in the areas of converged billing, interconnect billing, customer care, real-time rating, charging and policy management for voice, messaging and next generation data services to more than 90 network operators in over 50 countries. The Company’s software products allow its wireless, multi-play and alternate service providers to extend and enhance their capabilities and service offerings, enabling them to introduce new revenue through the introduction of network-based services, including call and subscriber management, multimedia messaging information services and location aware services. In addition, the Company’s software products also manage and analyze, in real time, complex and critical network operations, such as service provisioning, network management and customer care, as well as provide real-time rating, charging and billing.

Redknee solutions enable operators to monetize the value of each transaction, while personalizing the subscriber experience to meet mainstream and individual market segmentation requirements. The Company segments its operations in three main geographic areas namely:

1. APAC – Asia Pacific
2. Americas – North America, South America and Caribbean
3. EMEA – Europe, the Middle East and Africa.

Redknee’s end-to-end real-time converged billing solution provides wireless, multi-play and alternate service providers with the agility to drive a unique user experience, increase profitability and support any new product or business model. Redknee’s converged billing platform supports the following solutions:

**Redknee's Real-time Converged Billing** – Redknee's award-winning cloud-enabled real-time converged billing platform provides the marketing agility to support service providers achieve their business objectives. Redknee delivers the benefits of a highly scalable converged billing and customer care platform, including real-time unified billing, rating and charging for the operator's data, voice, and messaging services; advanced customer care capabilities with the Microsoft Dynamics CRM framework; real-time subscriber promotions and loyalty programs; and transparent and flexible self-care options for prepaid, postpaid and hybrid subscribers.

**Redknee's Mobile Virtual Network Solution** – Redknee's Mobile Virtual Network Solution provides a cloud-based end-to-end converged billing solution for Mobile Network Operators ("MNOs"), Mobile Virtual Network Enablers ("MVNEs") and Mobile Virtual Network Operators ("MVNOs") to launch quickly to the market. Redknee's out-of-the-box solution offers a low risk business model that enables MNOs to launch a second brand, MVNEs to accelerate their growth strategies and MVNOs to improve their differentiation in the market.

**Redknee's Wholesale Settlement** – Redknee's Wholesale Settlement is a cloud-based solution that provides operators with greater visibility into network transactions in order to achieve converged settlement and accurate interconnect billing. Redknee's solution helps service providers maximize the value of their network with a comprehensive and cost-effective interconnect, wholesale, roaming, MVNO, franchise management and content settlement software solution

## **SELECTED CONSOLIDATED FINANCIAL INFORMATION**

The following table sets out selected consolidated financial information of Redknee for the periods indicated. Each investor should read the following information in conjunction with those financial statements and related notes. The operating results for any past period are not necessarily indicative of results for any future period. The selected financial information set out below has been derived from the consolidated financial statements.

<b>Consolidated Statement of Operations</b>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
(all amounts in thousands of US\$, except per share amounts)	<b>June 30</b>		<b>June 30</b>	
<b>(unaudited)</b>	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
<b>Revenue</b>				
Software, services and other	\$ 8,975	\$ 8,703	\$ 25,590	\$ 27,979
Support	5,872	5,477	17,329	15,813
	<b>14,847</b>	<b>14,180</b>	<b>42,919</b>	<b>43,792</b>
<b>Cost of revenue</b>	4,245	5,483	13,425	15,764
<b>Gross profit</b>	<b>10,602</b>	<b>8,697</b>	<b>29,494</b>	<b>28,028</b>
<b>Operating expenses</b>				
Sales and marketing	4,069	4,028	11,169	11,219
General and administrative	2,470	3,467	6,491	8,545
Research and development	1,998	3,451	7,144	9,870
	<b>8,537</b>	<b>10,946</b>	<b>24,804</b>	<b>29,634</b>
<b>Income (loss) from operations</b>	<b>2,065</b>	<b>(2,249)</b>	<b>4,690</b>	<b>(1,606)</b>
Foreign exchange gain (loss)	(210)	251	(217)	(621)
Other income (expense)	-	290	(14)	536
Finance income	31	36	72	117
Finance costs	(79)	(168)	(297)	(435)
<b>Income (loss) before income taxes</b>	<b>1,807</b>	<b>(1,840)</b>	<b>4,234</b>	<b>(2,009)</b>
Income taxes	69	64	214	245
<b>Net Income (loss) for the period</b>	<b>\$ 1,738</b>	<b>\$ (1,904)</b>	<b>\$ 4,020</b>	<b>\$ (2,254)</b>
<b>Income (loss) per Common Share</b>				
Basic	\$ 0.03	(0.03)	\$ 0.06	(0.04)
Diluted	\$ 0.03	(0.03)	\$ 0.06	(0.04)
<b>Weighted average number of common shares</b>				
Basic (thousands)	64,142	64,195	64,253	64,155
Diluted (thousands)	65,104	64,195	65,120	64,155

Balance Sheet Data \$US Thousands (unaudited)	As at June 30,	As at September 30,
	2012	2011
Cash, Cash Equivalents and Restricted Cash	20,345	15,665
Goodwill and Intangible Assets	11,104	11,615
Total Assets	60,475	54,903
Accounts Payable and Accrued Liabilities	7,735	7,733
Long-Term Debt and Other LT liabilities	4,598	5,329
Shareholders' Equity	31,846	27,874

## CURRENT PERIOD OPERATING RESULTS

### Revenue

The following tables set forth the Company's revenues by type and as a percentage of total revenue for the periods indicated:

\$US Thousands (unaudited)	Three Months Ended		Nine Months Ended	
	June 30		June 30	
	2012	2011	2012	2011
Software & Services	8,753	8,174	24,160	24,849
Support	5,872	5,477	17,329	15,813
Third Party Software & Hardware	222	529	1,430	3,130
<b>Total</b>	<b>14,847</b>	<b>14,180</b>	<b>42,919</b>	<b>43,792</b>

Percentage of Total Revenue (unaudited)	Three Months Ended		Nine Months Ended	
	June 30		June 30	
	2012	2011	2012	2011
Software & Services	59%	58%	56%	57%
Support	40%	38%	41%	36%
Third Party Software & Hardware	1%	4%	3%	7%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

The Company recognizes revenue from the sale of software licenses, including initial licenses, capacity increases and/or upgrades; professional services; third party hardware and software components and customer support contracts. For the three-month period ended June 30, 2012, the Company's revenue increased by 5% from \$14.2 million for the same period in fiscal 2011 to \$14.8 million in fiscal 2012. The increase in revenue is primarily due to increases in software upgrades and support revenue. For the nine-month period ended June 30, 2012, the Company's revenue decreased by 2% from \$43.8 million for the same period in fiscal 2011 to \$42.9 million in fiscal 2012. The decrease in revenue is primarily due to a decrease in the third party revenues, partially offset by increased support revenues.

### *Software and Services Revenue*

Software and services revenue consists of fees earned from the licensing and deployment of software products to our customers, as well as the revenues resulting from consulting and training services contracts related to the software products.

Software and services revenue for Q3 2012 increased by 7% to \$8.8 million, or 59% of total revenue, compared to \$8.2 million, or 58% of total revenue for the same period last year. The increase is primarily due to an increase in software upgrades and initial deployments in the Americas region which is partially offset by a decrease in license expansions in the EMEA region. For the nine-month period ended June 30, 2012, the Company's software and services revenue decreased marginally by 3% from \$24.9 million, or 57% of total revenue in fiscal 2011 to \$24.2 million, or 56% of total revenue in fiscal 2012.

### *Support Revenue*

Support revenue consists of revenue from our customer support, subscription and maintenance contracts. These recurring revenue agreements allow customers to receive technical support and upgrades in the case of subscription agreements. Support revenue is generated from such agreements relative to current year sales and the renewal of existing agreements for software licenses sold in prior periods. Typically, support contracts commence for a period of one or more years upon completion of acceptance testing and then renew annually thereafter.

Support and subscription revenue for Q3 2012 grew by 7% to \$5.9 million, or 40% of total revenue, compared to \$5.5 million, or 38% of total revenue, for the same period last year. For the nine-month period ended June 30, 2012, the Company's support and subscription revenue increased by 10% from \$15.8 million, or 36% of total revenue in fiscal 2011 to \$17.3 million, or 41% of total revenue in fiscal 2012. The increase is primarily due to the addition of support revenue from contract renewals as well as additional support revenue resulting from license expansions and completed projects.

### *Third Party Software and Hardware Revenue*

Third-party software and hardware revenue consists of revenue from the sale of other vendor's hardware and software components as part of Redknee's solutions, including server platforms, database software and other ancillary components.

Third-party software and hardware revenue for Q3 2012 decreased by 58% to \$0.2 million, or 1% of total revenue, compared to \$0.5 million, or 4% of total revenue, for the same period last year. For the nine-month period ended June 30, 2012, the Company's third-party software and hardware revenue decreased by 54% from \$3.1 million, or 7% of total revenue for the same period in fiscal 2011 to \$1.4 million, or 3% of total revenue in fiscal 2012. The decreased third party revenue is associated with fewer customer requirements for third party hardware and software components.

*Revenue by Geography*

Revenue is attributed to geographic locations based on the location of the customer. The following tables set forth revenues by main geographic area and as a percentage of total revenue for the periods indicated:

\$US Thousands (unaudited)	Three Months Ended		Nine Months Ended	
	June 30		June 30	
	2012	2011	2012	2011
Asia and Pacific Rim	3,682	2,635	8,580	10,679
North America, South America and Caribbean	6,034	4,772	17,886	13,745
Europe, the Middle East and Africa	5,131	6,773	16,453	19,368
<b>Total</b>	<b>14,847</b>	<b>14,180</b>	<b>42,919</b>	<b>43,792</b>

Percentage of Total Revenue (unaudited)	Three Months Ended		Nine Months Ended	
	June 30		March 31,	
	2012	2011	2012	2011
Asia and Pacific Rim	25%	19%	20%	24%
North America, South America and Caribbean	40%	33%	42%	32%
Europe, the Middle East and Africa	35%	48%	38%	44%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

For Q3 2012, revenue from the APAC region increased by 40% to \$3.7 million, or 25% of total revenue, compared to \$2.6 million, or 19% of total revenue for the same period last year. The increase is mainly due to increase in software upgrades and license expansions along with support revenue. For the nine-month period ended June 30, 2012, the revenue from the APAC region decreased by 20% to \$8.6 million, or 20% of total revenue, compared to \$10.7 million, or 24% of total revenue for the same period last year. The decrease in revenue primarily relates to fewer license expansions year-to-date and initial deployment revenue recognized year over year.

For Q3 2012, revenue from the Americas region increased by 26% to \$6.0 million, or 40% of total revenue, compared to \$4.8 million or 33% of total revenue last year. For the nine-month period ended June 30, 2012, the revenue from the Americas region increased by 30% from \$13.8 million for the same period in fiscal 2011 to \$17.9 million in fiscal 2012. This increase was mostly due to software upgrades and increased initial deployment sales of real-time converged billing solutions to new customers.

For Q3 2012, revenue from the EMEA region decreased by 24% to \$5.1 million, or 35% of total revenue, compared to \$6.8 million, or 48% of total revenue last year. For the nine-month period ended June 30, 2012, the revenue from the EMEA region decreased by 15% from \$19.4 million for the same period in fiscal 2011 to \$16.5 million in fiscal 2012. This decrease in revenue is primarily due to reduced professional services revenue in the period.

### **Cost of Revenue and Gross Margin**

Cost of revenue consists of the expense of personnel providing professional services to implement and provide post sales technical support for our solutions, and the costs of third party hardware and software components sold as part of Redknee's solution. In addition, it includes an allocation of certain direct and indirect costs attributable to these activities.

For the third quarter of fiscal 2012, cost of revenue decreased 23% to \$4.3 million from \$5.5 million incurred for the same period in 2011. For the nine-month period ended June 30, 2012, cost of revenue decreased 15% to \$13.4 million from \$15.8 million incurred for the same period in 2011. The decrease is mostly attributed to costs associated with deferral of certain direct recoverable costs related to the deployment of term license projects and reduced headcount compared to same period in 2011.

The gross margin for the third quarter of fiscal 2012 has increased to 71% compared to 61% for the third quarter of 2011. For the nine-month period ended June 30, 2012, the gross margin was 69% compared to 64% for the same period in 2011. The increase in gross margin for the period relates to the change in mix of the revenues recorded, with a lower percentage of sales of third-party components recorded throughout the 2012 fiscal year, which generally carry the lowest gross margins and the deferral of certain direct recoverable costs related to the deployment of term license projects.

### **Operating Expenses**

Total operating expenses, excluding amortization, in the third quarter of fiscal 2012 decreased 21% to \$8.3 million (56% of revenue) from \$10.5 million (74% of revenue) in the third quarter of fiscal 2011. Total operating expenses, excluding amortization, for the nine-month period ended June 30, 2012 decreased 15% to \$24.1 million (56% of revenue) from \$28.3 million (65% of revenue) for the same period in 2011. The decrease is mostly due to deferral of certain direct recoverable costs associated with the deployment of term license projects and reduced compensation and other costs associated with reduced headcount year over year.

The following tables set forth total operating expenses by function and as a percentage of total revenue for the periods indicated:

\$US Thousands (unaudited)	Three Months Ended		Nine Months Ended	
	June 30		June 30	
	2012	2011	2012	2011
Sales and Marketing	4,069	4,028	11,169	11,219
General and Administrative	2,470	3,467	6,491	8,545
Research and Development	1,998	3,451	7,144	9,870
<b>Total Operating Expenses</b>	<b>8,537</b>	<b>10,946</b>	<b>24,804</b>	<b>29,634</b>
<i>Excluding Amortization</i>	<i>8,305</i>	<i>10,505</i>	<i>24,104</i>	<i>28,293</i>

Percentage of Total Revenue (unaudited)	Three Months Ended		Nine Months Ended	
	June 30		June 30	
	2012	2011	2012	2011
Sales and Marketing	27%	28%	26%	26%
General and Administrative	17%	25%	15%	19%
Research and Development	13%	24%	17%	23%
<b>Total Operating Expenses</b>	<b>57%</b>	<b>77%</b>	<b>58%</b>	<b>68%</b>
<i>Excluding Amortization</i>	<i>56%</i>	<i>74%</i>	<i>56%</i>	<i>65%</i>

### *Sales and Marketing Expenses*

Sales and Marketing (“S&M”) expenses consist primarily of salaries, variable compensation costs and other personnel costs, travel, advertising, marketing and conference costs plus the allocation of certain overhead costs to support the Company’s sales and marketing activities including amortization.

For the third quarter of fiscal 2012, S&M expenditures increased slightly to \$4.1M compared to \$4.0 million for the same period last year. As a percentage of total revenue, S&M expenses decreased to 27% compared to 28% for the same period last year. For the nine-month period ended June 30, 2012, S&M expenditures remained almost constant at \$11.2M compared to the same period last year. As a percentage of total revenue, S&M expenses remained flat at 26% compared to the same period last year.

### *General and Administrative Expenses*

General and administrative (“G&A”) expenses consist of the Company’s support activities such as finance, human resources, information technology, and professional costs associated with tax, accounting, and legal expenditures. Certain overhead costs such as facilities, communications and computer costs are allocated to G&A and the other departments on a per headcount basis including amortization.

For the third quarter of fiscal 2012, general and administrative expenditures decreased by 29% to \$2.5 million from \$3.5 million. As a percentage of total revenue, G&A expenses decreased to 17% compared to 25% for the same period last year. For the nine-month period ended June 30, 2012, general and administrative expenditures decreased by 24% to \$6.5 million from \$8.5 million. As a percentage of total revenue, G&A expenses decreased to 15% compared to 19% for the same period

last year. The decrease is mostly due to reduced compensation and other costs associated with reduced headcount year over year and one-time items recorded in third quarter of 2011 relating to allowance for doubtful accounts and severance.

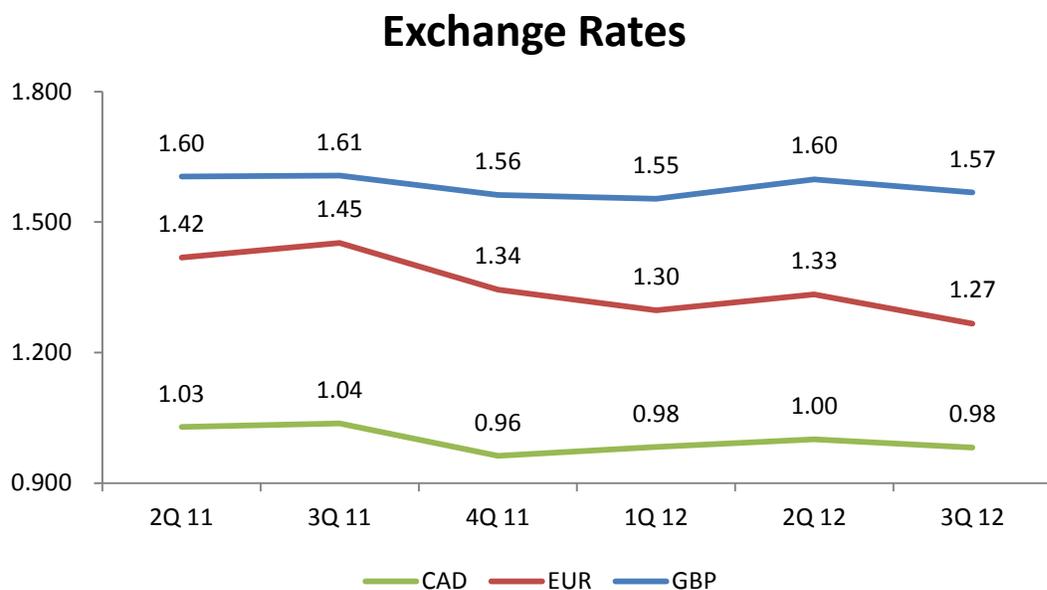
**Research and Development Expenses**

Research and development expenses consist primarily of personnel costs associated with product management and the development and testing of new products plus the allocation of certain overhead costs including amortization. Research and development expenses are reduced by investment tax credits (“ITCs”) recognized during the year.

For the third quarter of fiscal 2012, R&D expenditures decreased by 42% to \$2.0 million compared to \$3.5 million for the same period last year. As a percentage of total revenue, R&D expenditures decreased to 13% for Q3 2012 from 24% in Q3 2011. For the nine-month period ended June 30, 2012, R&D expenditures decreased by 28% to \$7.1 million compared to \$9.9 million for the same period last year. As a percentage of total revenue, R&D expenditures decreased to 17% compared to 23% for the same period last year. The decrease is mostly due to deferral of certain direct recoverable costs associated with the deployment of term license projects and reduced compensation expenses and other costs associated with reduced headcount year over year.

**Foreign Exchange Gain/Loss**

We operate internationally and have foreign currency risks related to our revenue, operating expenses, assets and liabilities denominated in currencies other than the U.S. dollar. Consequently, we believe movements in the foreign currencies in which we transact could significantly affect future net earnings. Currently, we do not use hedging techniques to mitigate such currency risks. The graph below displays the change in rates relative to the U.S. dollar.



Source: Bank of Canada

For the third quarter ended June 30, 2012, the Company recognized a foreign currency exchange loss of \$0.2 million, compared to a foreign currency exchange gain of \$0.3 million in the same period of fiscal 2011. The third quarter loss in fiscal 2012 was primarily due to the U.S. dollar strengthening against the Euro and British Pound.

For the nine-month period ended June 30, 2012, the Company recognized a foreign currency exchange loss of \$0.2 million, compared to a foreign currency exchange loss of \$0.6 million in the same period of fiscal 2011. The change in functional currency to U.S. dollar has reduced the Company's exposure to the volatility of U.S. dollar over the last nine months, hence a reduced foreign exchange loss.

### **Finance Costs**

The interest expense of \$0.1 million recorded in Q3 2012 and \$0.3 million for the nine-months ended June 30, 2012 was mainly associated with the Company's use of a credit facility available from Export Development Corporation ("EDC") for up to an aggregate principal amount of \$10.0 million. During the fourth quarter of fiscal 2010, the Company borrowed against this credit facility to complete the acquisition of Nimbus. As at June 30, 2012, the amounts drawn totaled \$5.7 million.

### **Stock-Based Compensation**

Stock options granted during the third quarter ended June 30, 2012 totaled nil (2011 – nil). Stock options granted during the nine-months ended June 30, 2012 totaled nil (2011 – 648,125). The stock-based compensation relating to the Company's stock options, deferred share unit plan and restricted shares under the restricted share plan during the third quarter of fiscal 2012 was \$0.2 million compared to \$0.1 million in the same period last year. The stock-based compensation relating to the Company's stock options, deferred share unit plan and restricted shares under the restricted share plan during the nine-months ended June 30, 2012 and 2011 was \$0.7 million and \$0.6 million respectively.

### **Income Taxes**

The current income tax provision is management's estimate of current taxes owing by the Company's foreign subsidiaries.

## **SUMMARY OF RESULTS**

All financial results are in thousands, unless otherwise stated, with the exception of per share amounts. The table below provides summarized information for our eight most recently completed quarters:

		<i>IFRS (1)</i>	<i>IFRS (1)</i>	<i>IFRS (1) (3)</i>	<i>IFRS (1) (3)</i>	<i>IFRS (1) (3)</i>	<i>IFRS (1) (3)</i>	<i>(1) (2) (3)</i>
<b>\$ Thousands (unaudited)</b>	<b>3Q 12</b>	<b>2Q 12</b>	<b>1Q 12</b>	<b>4Q 11</b>	<b>3Q 11</b>	<b>2Q 11</b>	<b>1Q 11</b>	<b>4Q 10</b>
Revenue	\$14,847	\$14,108	\$13,964	\$14,034	\$14,180	\$16,013	\$13,600	\$12,507
Net Income (Loss)	\$ 1,739	\$ 1,332	\$ 949	\$ (70)	\$ (1,903)	\$ 431	\$ (783)	\$ 253
Basic Income (Loss) per Share	\$ 0.03	\$ 0.02	\$ 0.01	\$ 0.00	\$ (0.03)	\$ 0.01	\$ (0.01)	\$ 0.00
Diluted Income (Loss) per Share	\$ 0.03	\$ 0.02	\$ 0.01	\$ 0.00	\$ (0.03)	\$ 0.01	\$ (0.01)	\$ 0.00
Weighted average shares outstanding – Basic	64,142	64,410	64,222	64,198	64,195	64,158	63,941	62,309
Weighted average shares outstanding - Diluted (4)	65,104	65,304	65,098	64,198	64,195	65,800	63,941	64,608

- 1) Effective October 1, 2011, the Company's functional and presentation currency changed from Canadian dollars to the U.S. dollar. Comparative financial information for periods prior to October 1, 2011 has been translated from the Canadian dollar to the U.S. dollar at the October 1, 2011 spot rate.
- 2) Prepared using accounting policies consistent with Canadian GAAP. Financial information in this MD&A for periods prior to October 1, 2010 have not been restated for changes in accounting policies on adoption of IFRS. Refer to Changes in Accounting Policies below, and to Note 12 of the accompanying interim consolidated financial statements, for a discussion of IFRS and its impact on the Company's financial statements
- 3) As part of finalizing the contingent consideration payment relating to the Nimbus acquisition, the Company determined that it had not recorded certain restricted share units ("RSUs") granted to Nimbus employees at the acquisition date. These RSUs were contingently issuable on certain non-market performance criteria and were linked to continuing employment. Comparative amounts have been recast for this immaterial correction.
- 4) In prior periods where net income was negative, options were considered to be anti-dilutive for the calculation of Fully Diluted Earnings per Share ("FDEPS").

## LIQUIDITY AND CAPITAL RESOURCES

The Company's objective in managing capital is to ensure sufficient liquidity to drive its organic growth, fund operations and undertake selective acquisitions, while at the same time taking a conservative approach toward financial leverage and management of financial risk. The Company currently funds its operations, changes in non-cash working capital and capital expenditures from internally generated cash flows and cash on hand.

The table below outlines a summary of cash inflows and outflows by activity.

Statement of Cash Flows Summary (\$ US Thousands) (Unaudited)	Three Months ended		Nine Months ended	
	June 30,		June 30,	
	2012	2011	2012	2011
Cash inflows and (outflows) by activity:				
Operating activities	2,440	(3,789)	9,150	(3,348)
Investing activities	(950)	807	(1,414)	(270)
Financing activities	(1,157)	914	(3,073)	(1,464)
Effect of foreign currency exchange rate changes on cash and cash equivalents	114	170	84	(179)
Net cash inflows (outflows)	447	(1,898)	4,747	(5,261)
Cash and cash equivalents, beginning of period	19,180	14,676	14,880	18,038
Cash and cash equivalents, end of period	19,627	12,778	19,627	12,778

Key Ratios	June, 30	September, 30
	2012	2011
Working Capital	\$20,504	\$18,087
Day Sales Outstanding	82	90

\*The Company uses Working Capital and Days Sales Outstanding in Accounts Receivable as measures to enhance comparisons between periods. These terms do not have a standardized meaning under IFRS and are not necessarily comparable to similar measures presented by other companies. The calculation of each of these items is more fully described below.

### Cash from Operating Activities

Cash provided by operating activities was \$2.4 million in the three months ended June 30, 2012, compared to the cash used in operating activities of \$3.8 million for the same period last year. This is mostly attributed to net income of \$1.7 million along with an increase in deferred revenue. Cash provided by operating activities was \$9.2 million in the nine months ended June 30, 2012, compared to use of \$3.3 million for the same period last year. This is mostly attributed to net income of \$4.0 million, as well as a decrease in accounts receivable and an increase in deferred revenue.

The Company's Days Sales Outstanding in Accounts Receivable ("DSO") was 82 days as at June 30, 2012 compared to 90 days as at March 31, 2012 and 90 days as of September 30, 2011. Redknee calculates DSO based on the annualized revenue and the trailing four quarterly average accounts receivable balance.

Working capital represents the Company's current assets less its current liabilities. The Company's working capital balance increased to \$20.5 million as at June 30, 2012 from \$18.1 million as at September 30, 2011. This increase is mainly attributed to an increase in cash and cash equivalents of \$4.7 million, an increase in unbilled revenue of \$1.3 million, a decrease in loans payable of \$1.5 million offset by an increase in deferred revenue of \$3.7 million and decrease in accounts receivable of \$2.0 million.

### Cash from Financing Activities

In the third quarter of fiscal 2012, cash used for financing activities was \$1.2 million compared to cash provided of \$0.9 million for the same period last year. In the first nine months of fiscal 2012, cash used

for financing activities was \$3.1 million compared to \$1.5 million in 2011. The use of cash represented repayment of loans and purchase of common shares in the open market to satisfy the delivery of common shares under the equity-based compensation plans.

### **Cash from Investing Activities**

Cash used for investing activities during the quarter ended June 30, 2012 was \$0.9 million compared to cash provided by investing activities of \$0.8 million in 2011. Cash used for investing activities during the nine months ended June 30, 2012 was \$1.4 million compared to \$0.3 million in 2011. The use of cash is mainly due to the payment of contingent consideration relating to Nimbus acquisition and purchase of capital assets.

### **GOODWILL**

Goodwill is derived as the difference between the purchase price of Nimbus on August 12, 2010 and the sum of the fair value of the net assets acquired.

### **COMMITMENTS AND CONTRACTUAL OBLIGATIONS**

#### **Long Term Debt and Credit Facilities**

As at June 30, 2012, the Company has a credit facility with Export Development Canada for up to an aggregate principal amount of \$10.0 million to assist in financing (i) one or more acquisitions and/or (ii) working capital requirements.

The Company borrowed against this credit facility for the Nimbus acquisition. As at June 30, 2012, \$5.7 million remains outstanding and is repayable semi-annually over the next four years. Interest on this credit facility is LIBOR plus 4% and is payable semi-annually after the first specified repayment date. Accounts receivable, chattel paper, documents of title, equipment, intangible assets, inventory and securities are pledged as security for the credit facility.

Certain financial and non-financial covenants exist under the agreement, which, if interpreted to be violated by the lender, could result in the amounts borrowed being due and payable to the lender on demand. The Company is in compliance with its debt covenants as at June 30, 2012.

### **MANAGEMENT OF CAPITAL**

The Company's objective in managing capital is to ensure sufficient liquidity to pursue its growth strategy, fund research and development and undertake selective acquisitions, while at the same time taking a conservative approach toward financial leverage and management of financial risk. The Company's capital is composed of share capital and credit used plus credit available under certain credit facilities, which assist in financing (i) acquisitions and/or (ii) working capital requirements. The Company's primary uses of capital are financing its operations, increases in non-cash working capital, capital expenditures, debt repayments and acquisitions. The Company currently funds these requirements from cash flows from operations, cash raised through past share issuances, and lines available under certain credit facilities. The Company's objectives when managing capital are to ensure that the Company will continue to have enough liquidity so it can provide services to its

customers and increase shareholder value. Management monitors its compliance with financial and non-financial covenants imposed by loan agreements on a quarterly basis. The Company has complied with all externally imposed capital requirements.

## **DISCLOSURE CONTROLS AND PROCEDURES**

Our management, under the supervision and with the participation of our CEO and CFO, has designed and evaluated the effectiveness of the Company's internal controls over financial reporting ("ICFR") as at September 30, 2011 to provide reasonable assurance that our financial reporting is reliable and that our consolidated financial statements were prepared in accordance with GAAP. Management has concluded that ICFR, as defined in NI 52-109 and using the Committee of Sponsoring Organization of the Treadway Commission ("COSO") Framework are effective as at September 30, 2011.

## **ACCOUNTING CHANGES AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

In February 2008, the Canadian Accounting Standards Board announced the mandatory adoption of IFRS for publicly accountable entities in Canada for fiscal periods beginning on or after January 1, 2011. Accordingly, this is the third quarter in which we have provided unaudited consolidated quarterly financial information in accordance with IFRS, including comparative figures for 2011.

The Company has adopted IFRS effective October 1, 2010 ("the transition date") and has prepared its opening IFRS statement of financial position as of that date. Prior to the adoption of IFRS, the Company prepared its financial statements in accordance with Canadian GAAP. The Company's consolidated financial statements for the year ending September 30, 2012 will be the first annual financial statements of the Company that comply with IFRS.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in note 12 of the Interim Condensed Consolidated Financial Statements for the three month period ended December 31, 2011. This note includes reconciliations from Canadian GAAP to IFRS of equity and comprehensive income of the comparative periods and of equity at the date of transition.

In October 2010, the IASB issued IFRS 9, Financial Instruments ("IFRS 9"). IFRS 9 which replaces IAS 39, Financial Instruments: Recognition and Measurement, establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful info to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows. This new standard is effective for the Company's interim and annual consolidated financial statements commencing January 1, 2013. The Company is assessing the impact of this new standard on its consolidated financial statements.

## **Change in Functional and Presentation Currency**

Until September 30, 2011, the Company's functional currency was the Canadian dollar and was the U.S. dollar for certain subsidiaries. Effective October 1, 2011, the functional currency of the Company and certain subsidiaries was changed from the Canadian dollar to the U.S. dollar. Effective October 1, 2011, the parent company and all subsidiaries have a functional currency of U.S. dollars. The change

in functional currency was a result of the increased influence of the U.S. dollar on the economic environment in which the companies operate and the increased reliance on U.S. dollar financing.

Unless otherwise stated, all comparative information in these consolidated financial statements for periods prior to October 1, 2011 have been translated from Canadian dollars to U.S. dollars at the October 1, 2011 spot rate.

The effect of the change in functional and presentation currency is explained in Note 12 to the accompanying interim condensed consolidated financial statements.

## **CHANGES IN ACCOUNTING STANDARDS**

### **Transition to International Financial Reporting Standards**

#### ***Overview***

IFRS replaced the existing Canadian GAAP for the Company, effective for its fiscal 2012 interim and annual financial statements. Accordingly, the Company is applying accounting policies consistent with IFRS beginning with its interim condensed consolidated financial statements for the quarter ended December 31, 2011.

The adoption of IFRS resulted in changes to the Corporation's accounting policies. The accounting policies described in note 2 of the Company's first quarter interim condensed consolidated financial statements have been applied consistently to all periods presented in the financial statements and in the preparation of an opening IFRS statement of financial position as at October 1, 2010, except for the application of certain first-time adoption exemptions. The changes in accounting policy have not been applied to any information within this MD&A for periods prior to October 1, 2010.

The impact of the transition from Canadian GAAP to IFRS is explained in detail in Note 12 to the accompanying interim condensed consolidated financial statements.

#### ***First-time adoption of IFRS***

The first-time adoption of IFRS generally requires retrospective application of the resulting changes in accounting policies. Subject to certain optional exemptions and mandatory exceptions, the Company has applied the changes in accounting policies resulting from the adoption of IFRS retrospectively in the preparation of its opening IFRS statement of financial position as at October 1, 2010, the Company's transition date.

The impact of first-time adoption of IFRS on the Company's opening IFRS statement of financial position is described in detail in Note 12 to the accompanying interim condensed consolidated financial statements.

### *Impact of Adopting IFRS on Redknee's Financial Statements*

The adoption of IFRS resulted in changes to the Corporation's accounting policies, and has resulted in changes to the recognition and measurement of transactions and balances. The impact of adopting IFRS on the Corporation's financial statements is described in detail in Note 12 to the accompanying interim condensed consolidated financial statements.

The following summarizes the significant changes to the Company's accounting policies on adoption of IFRS, and the effect on the Company's opening IFRS statement of financial position at October 1, 2010:

a) *Business Combinations and Goodwill*

(i) Acquisitions on or after October 1, 2010:

Acquisitions of businesses are accounted for using the acquisition method. The acquiree's identifiable assets and liabilities are recognized at their fair values at the date of acquisition. Acquisition related transaction costs are expensed as incurred. The fair value of contingent consideration considered part of consideration transferred is included in the total purchase price on the acquisition date. Contingent consideration classified as equity is not re-measured subsequent to acquisition date (other than for measurement period adjustments) and its subsequent settlement is accounted for within equity. Contingent consideration that is liability classified and falls within the scope of IAS 39 is re-measured to fair value at each reporting date until the contingency is resolved, with changes in fair value recorded in other income.

Goodwill is recognized as the excess of purchase price over fair value of the net identifiable assets of acquired businesses. Goodwill is not subject to amortization and is measured at cost less accumulated impairment losses.

(ii) Acquisitions prior to October 1, 2010:

As part of the transition to IFRS, the Company elected to restate only those business combinations that occurred on or after October 1, 2010. In respect of acquisitions prior to October 1, 2010, goodwill represents the amount recognized under Canadian GAAP.

The allocation of the purchase price to the net assets acquired may be adjusted to reflect new information obtained about facts and circumstances that existed at the acquisition date, up to a maximum of twelve months following the date of acquisition. Changes to the allocation of the purchase price during this measurement period are recognized retrospectively.

As a result of applying this change in accounting policy prospectively from the transition date, the Company recognized a liability at October 1, 2010 for contingent consideration related to the acquisition of Nimbus.

*b) Share-based compensation*

The Company issues stock options, restricted share units ("RSUs") and performance share units ("PSUs") pursuant to several share-based compensation plans. Stock options, RSUs and PSUs are settled with common shares of the Company. Compensation cost is measured based on the grant date fair value of the award and recognized net of estimated forfeitures over the vesting period with a corresponding credit to contributed surplus. For awards with graded vesting, the fair value of each tranche is recognized over its respective vesting period. At the end of each reporting period, the Company re-assesses its estimates of the number of awards that are expected to vest and recognizes the impact of the revisions in the period.

The Company has a deferred share unit ("DSUs") plan. The plan allows for settlement of DSUs by cash or other assets. The fair value of the Company's DSUs is recognized using the graded vesting method. Since the DSUs will be settled in cash or other assets, the fair value of the vested DSUs is revalued each quarter until the settlement date. The Company has recognized a liability in the consolidated statements of financial position for the total fair value of the vested DSUs included in other long-term liabilities.

These changes resulted in a change in the measurement of contributed surplus at October 1, 2010.

*c) Impairment*

At each reporting date the Company's non-financial assets, other than goods in transit and deferred tax assets, are reviewed at each reporting date to determine whether there is an indication that those assets are impaired. If such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment, if any. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in the statement of operations. For the purposes of assessing for indications of impairment and impairment testing, assets that do not have largely independent cash inflows are grouped into cash-generating units. Cash-generating units are the smallest identifiable groups of assets having independent cash inflows. The recoverable amount of goodwill is estimated and compared to the carrying value on an annual basis at September 30 whether or not there is an indication the goodwill is impaired.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted at a rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is reversed if there is a change in the estimates used to determine the recoverable amount, with the exception of impairment losses on goodwill, which are not reversed. When an impairment loss is reversed, the carrying amount of the asset is increased to the revised estimate of its recoverable amount so that the increased carrying amount does not exceed what the carrying amount would have been had no impairment losses been recognized for the asset in prior years.

These changes in accounting policy did not have an impact on the Company's financial statements at October 1, 2010.

*d) Financial statement presentation*

IFRS requires that expenses on the statement of operations be presented either by nature or by function. Under Canadian GAAP, the Company's statement of operations was presented with a combination of expenses by nature and by function. This change in presentation resulted in amortization and depreciation being allocated to the functional line items within the statement of operations under IFRS. This change had no impact on consolidated statement of financial position or on total comprehensive income.

***Reconciliation of Canadian GAAP to IFRS***

Note 12 to the accompanying interim condensed consolidated financial statements provide reconciliations of comparative information from the previously reported Canadian GAAP to IFRS, and the impact of the change in functional and presentation currency. Also included are reconciliations of comparative consolidated statements of financial position and statement of operations from Canadian GAAP to IFRS and the translation to U.S. dollar.

**PATENT PORTFOLIO**

As part of Redknee's commitment to Research and Development ("R&D") to maintain its position as a key industry innovator in the real-time OSS/BSS software space, the Company currently has a portfolio of over 100 filed and over 35 granted. To date we have not initiated any action with respect to assertions and/or claims of patent infringement.

**OUTSTANDING SHARE DATA**

The current number of common shares outstanding, including treasury stock of 568,906, as at June 30, 2012 is 64,443,404. In addition, there were 4,879,378 stock options outstanding with exercise prices ranging from \$0.23 to \$2.16 per share.

**CAPITAL STOCK**

On March 8, 2012, the Company announced a normal course issuer bid ("NCIB") under which it may purchase up to 4,701,696 of its common shares. The purchases may commence on March 12, 2012 and will terminate on March 11, 2013 or on such earlier date as the Company may complete its purchases pursuant to the notice of intention to make a normal course issuer bid filed with the Toronto Stock Exchange ("TSX"). Purchases will be made on the open market by the Company through the facilities of the TSX in accordance with TSX requirements. The prices that the Company will pay for any purchased common shares will be the market price of such shares on the TSX at the time of acquisition. As of June 30, 2012, the Company has not purchased any common shares under this NCIB.

During the quarter ended June 30, 2012, the Company paid \$714,608 to the trustee to purchase 568,906 of the Company's common shares in the open market to satisfy the delivery of common shares under the equity-based compensation plans. The Company classified these shares as treasury stock until they are delivered pursuant to the awards.

**RISK FACTORS**

As previously discussed, many factors could cause the actual results of Redknee to differ materially from the results, performance, achievements or developments expressed or implied by such forward-looking statements, including, without limitation, each of the following factors, which are further discussed in the section of the Company's AIF entitled Risk Factors.

Factors such as:

- Currency fluctuations may adversely affect the Company
- Software Defects
- Customer Credit Risk
- Defects in components or design of the Company's solutions could result in significant costs to the Company and could impair its ability to sell its solutions
- The Company's lengthy and variable sales cycle makes it difficult for it to predict its operating results
- The Company relies on a small number of customers for a large percentage of its revenue
- Technological Change
- Economic and geopolitical uncertainty may negatively affect the Company
- Maintaining Business Relationships
- Product Liability
- System Failures and Breaches of Security

We caution that period-to-period comparison of results of operations is not necessarily meaningful and should not be relied upon as any indication of future performance.

**ADDITIONAL INFORMATION**

Additional information, including the quarterly and annual consolidated financial statements, annual information form, management proxy circular and other disclosure documents may be examined by accessing the SEDAR website at [www.sedar.com](http://www.sedar.com).