

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 1999

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM
_____ TO _____

Commission file number 000-24389

VASCO Data Security International, Inc.
(Exact Name of Registrant as Specified in Its Charter)

DELAWARE 36-4169320
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

1901 South Meyers Road, Suite 210
Oakbrook Terrace, Illinois 60181
(Address of Principal Executive Offices)(Zip Code)

Registrant's telephone number, including area code: (630) 932-8844

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 X No

As of May 14, 1999, 24,647,005 shares of the Company's Common Stock, \$.001 par value per share ("Common Stock"), were outstanding.

VASCO Data Security International, Inc.
Form 10-Q
For The Three Months Ended March 31, 1999

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PART I. FINANCIAL INFORMATION

This report contains the following trademarks of the Company, some of which are registered: VASCO, VACMan Server and VACMan/CryptaPak and Digipass.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

VASCO Data Security International, Inc.
Consolidated Balance Sheets

	December 31, 1998 ----	March 31, 1999 ---- (Unaudited)
ASSETS		
Current assets:		
Cash	\$ 1,523,075	\$ 1,346,217
Accounts receivable, net of allowance for doubtful accounts of \$55,000 and \$62,000 in 1998 and 1999	3,376,218	2,751,483
Inventories, net	1,272,327	1,341,837
Prepaid expenses	692,326	711,391
Deferred income taxes	83,000	83,000
Other current assets	277,322	255,099
	-----	-----
Total current assets	7,224,268	6,489,027
Property and equipment		
Furniture and fixtures	580,427	582,076
Office equipment	468,975	501,226
	-----	-----
	1,049,402	1,083,302
Accumulated depreciation	(691,806)	(727,252)
	-----	-----
	357,596	356,050
Goodwill, net of accumulated amortization of \$327,000 and \$359,000 in 1998 and 1999	575,211	542,983
Other assets	943,821	1,227,301
	-----	-----
Total assets	\$ 9,100,896	\$ 8,615,361
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Current maturities of long-term debt	\$ 6,528,867	\$ 6,327,435
Accounts payable	1,144,506	1,821,234
Customer deposits	519,585	270,148
Other accrued expenses	2,117,599	2,374,946
	-----	-----
Total current liabilities	10,310,557	10,793,763
Long-term debt, including stockholder note of \$5,000,000 in 1998 and 1999	8,435,903	8,433,132

Stockholders' equity (deficit):		
Common stock, \$.001 par value -		
75,000,000 shares authorized;		
20,805,697 shares issued and		
outstanding in 1998; 21,186,716		
shares issued and outstanding in 1999	20,806	21,187
Additional paid-in capital	9,797,068	9,969,062
Accumulated deficit	(19,550,419)	(20,554,525)
Accumulated other comprehensive income-		
cumulative translation adjustment	86,981	(47,258)
	-----	-----
Total stockholders' equity (deficit)	(9,645,564)	(10,611,534)
	-----	-----
Total liabilities and stockholders'		
equity (deficit)	\$ 9,100,896	\$ 8,615,361
	=====	=====

See accompanying notes to consolidated financial statements.

VASCO Data Security International, Inc.
Consolidated Statements of Operations
(Unaudited)

	For the Quarter Ended March 31,	
	1998	1999
	----	----
Net revenues	\$ 2,612,967	\$ 4,308,543
Cost of goods sold	1,221,823	1,835,858
Gross profit	1,391,144	2,472,685
Operating costs:		
Sales and marketing	882,613	1,325,719
Research and development	437,434	703,749
General and administrative	575,789	859,015
Total operating costs	1,895,836	2,888,483
Operating loss	(504,692)	(415,798)
Interest expense	(209,570)	(223,448)
Other expense, net	(14,462)	(60,679)
Loss before income taxes	(728,724)	(699,925)
Provision for income taxes	9,374	304,181
Net loss available to common stockholders	\$ (738,098)	\$ (1,004,106)
Basic and diluted net loss per common share	\$ (0.04)	\$ (0.05)
Weighted average common shares outstanding	20,510,308	21,010,633

See accompanying notes to consolidated financial statements.

VASCO Data Security International, Inc.
Consolidated Statements of Comprehensive Income
(Unaudited)

For the Quarter ended March 31,
1998 1999
----- -----

Comprehensive income:		
Net loss	\$ (738,098)	\$ (1,004,106)
Other comprehensive loss - cumulative translation adjustment	(170,243)	(134,239)
	-----	-----
Comprehensive loss	\$ (908,341)	\$ (1,138,345)
	=====	=====

See accompanying notes to consolidated financial statements.

VASCO Data Security International, Inc.
Consolidated Statements of Cash Flows
(Unaudited)

For the Quarter Ended
March 31,
1998 1999
----- -----

Cash flows from operating activities:		
Net loss	\$ (738,098)	\$ (1,004,106)
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	251,486	249,056
Interest paid in shares of common stock	-	78,750
Gain on sale of fixed assets	-	(14,862)
Changes in current assets and current liabilities:		
Accounts receivable, net	417,434	624,735
Inventories, net	(200,166)	(69,510)
Other current assets	(16,942)	3,058
Accounts payable	789,406	676,728
Customer deposits	(27,397)	(249,437)
Other accrued expenses	23,732	257,347
	-----	-----
Net cash provided by operations	499,455	551,759
	-----	-----
Cash flows from investing activities:		
Additions to property and equipment	(125,922)	(33,800)
	-----	-----
Net cash used in investing activities	(125,922)	(33,800)
	-----	-----
Cash flows from financing activities:		
Prepayment of royalties	-	(450,000)
Proceeds from exercise of stock options	115,347	63,625
Repayment of debt	(20,386)	(204,203)
	-----	-----
Net cash provided by (used in) financing activities	94,961	(560,578)
	-----	-----
Effect of exchange rate changes on cash	(170,243)	(134,239)
	-----	-----
Net increase (decrease) in cash	298,251	(176,858)
Cash, beginning of period	1,897,666	1,523,075
	-----	-----
Cash, end of period	\$ 2,195,917	\$ 1,346,217
	=====	=====
Supplemental disclosure of cash flow information:		
Interest paid	\$ 20,764	55,230
Income taxes paid	\$ -	3,945

See accompanying notes to consolidated financial statements.

VASCO Data Security International, Inc.
Notes to Consolidated Financial Statements

Note 1 - Basis of Presentation

The accompanying unaudited consolidated financial statements include the accounts of VASCO Data Security International, Inc. and its subsidiaries (collectively, the "Company") and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission regarding interim financial reporting. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements and should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 1998.

In the opinion of management, the accompanying unaudited consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements, and include all adjustments, consisting only of normal recurring adjustments, necessary for the fair presentation of the results of the interim periods presented. The operating results for the interim periods presented are not necessarily indicative of the results expected for a full year.

Note 2 - Exchange Offer

VASCO Data Security International, Inc. ("VDSI Inc.") was organized in 1997 as a subsidiary of VASCO Corp., a Delaware corporation ("VASCO Corp."). Pursuant to an exchange offer ("Exchange Offer") by VDSI Inc. for securities of VASCO Corp. that was completed March 11, 1998, VDSI Inc. acquired 97.7% of the outstanding common stock of VASCO Corp. Consequently, VASCO Corp. became a subsidiary of VDSI Inc., with certain VASCO Corp. shareholders holding the remaining 2.3% of the VASCO Corp. common stock representing a minority interest. On October 28, 1998, VASCO Corp. was merged with and into the Company and VASCO Corp. ceased to exist.

Note 3 - Subsequent Events

On April 14, 1999, the Company completed a private placement of Common Stock in the amount of \$11.5 million. The transaction represented a sale of the Company's Common Stock to European institutional investors at a price of \$3.50 per share. A total of 3,285,714 shares of Common Stock were issued as a part of this transaction.

On May 3, 1999, the Company announced that it has acquired the global assets of SecureWare, a prominent French security software firm. SecureWare's focus is on developing security solutions for every leading operating system - including Windows NT, UNIX, IBM's S/390 and AS/400, Tandem, Digital, Stratus, Hewlett-Packard, and Sun Solaris, among others. The purchase price of \$1.5 million was paid in a combination of cash and common stock.

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

VDSI Inc. designs, develops, markets and supports open standards-based hardware and software security systems which manage and secure access to data.

The following discussion is based upon VDSI Inc.'s consolidated results of operations for the three months ended March 31, 1999 as compared to VASCO Corp.'s consolidated results of operations for the three months ended March 31, 1998. See Note 2 - Exchange Offer. References to the Company or VDSI Inc. represent the consolidated entity.

Cautionary Statement for Purposes of the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995

This Quarterly Report on Form 10-Q, including the "Management's Discussion and Analysis of Financial Condition and Results of Operations," contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 concerning, among other things, the prospects, developments and business strategies for the Company and its operations, including the development and marketing of certain new products and the anticipated future growth in certain markets in which the Company currently markets and sells its products or anticipates selling and marketing its products in the future. These forward-looking statements (i) are identified by their use of such terms and phrases as "expected," "expects," "believe," "believes," "will," "anticipated," "emerging," "intends," "plans," "could," "may," "estimates," "should," "objective," and "goals" and (ii) are subject to risks and uncertainties and represent the Company's present expectations or beliefs concerning future events. The Company cautions that the forward-looking statements are qualified by important factors that could cause actual results to differ materially from those in the forward-looking statements, including (a) risks of general market conditions, including demand for the Company's products and services, competition and price levels and the Company's historical dependence on relatively few products, certain suppliers and certain key customers, and (b) risks inherent to the computer and network security industry, including rapidly changing technology, evolving industry standards, increasing numbers of patent infringement claims, changes in customer requirements, price competitive bidding, changing government regulations and potential competition from more established firms and others. Therefore, results actually achieved may differ materially from expected results included in, or implied by these statements.

Comparison of Three Months Ended March 31, 1998 and March 31, 1999

The following discussion and analysis should be read in conjunction with the Company's Consolidated Financial Statements for the three months ended March 31, 1998 and 1999.

Revenues

The Company's consolidated revenues for the three months ended March 31, 1999 were \$4,309,000, an increase of \$1,696,000, or 65%, as compared to the three months ended March 31, 1998. This increase can be attributed to continued strong performance from international operations as well as increased demand for the Company's authentication products, including the introduction of two new authentication products, the Digipass 600 and Digipass 700.

Cost of Goods Sold

The Company's consolidated cost of goods sold for the three months ended March 31, 1999 was \$1,836,000, an increase of \$614,000, or 50%, as compared to the three months ended March 31, 1998. This increase is consistent with the increase in revenues for the period. The Company continues to benefit from efficiencies in the manufacturing process, as well as the increasing demand for products with a more favorable cost structure.

Gross Profit

The Company's consolidated gross profit for the three months ended March 31, 1999 was \$2,473,000, an increase of \$1,082,000, or 78%, as compared to the three months ended March 31, 1998. This represents a consolidated gross margin of 57%, as compared to 53% for the same period of 1998. This increase can be attributed to efficiencies in the design of the products, which resulted in reduced third-party manufacturing costs, as well as favorable variances as a result of increased volumes.

Sales and Marketing Expenses

Consolidated sales and marketing expenses for the three months ended March 31, 1999 were \$1,326,000, an increase of \$443,000, or 50%, over the three months ended March 31, 1998. The increase is attributed to the continued expansion the Company's worldwide sales force and network of distributors, and an increase in marketing activities to existing as well as new vertical and geographic markets.

Research and Development

Consolidated R&D costs for the three months ended March 31, 1999 were \$704,000, an increase of \$266,000, or 61%, as compared to the three months ended March 31, 1998. The increase is due to the addition of R&D personnel, in both the U.S. and Europe, as well as the development and launch of two enhanced versions of its VACMan access control server, and two new authentication devices - the Digipass 600 and Digipass 700.

General and Administrative Expenses

Consolidated general and administrative expenses for the three months ended March 31, 1999 were \$859,000, an increase of \$283,000, or 49%, compared to the three months ended March 31, 1998. This increase is due to legal fees incurred in connection with two lawsuits, both of which were settled during the first quarter.

Interest Expense

Consolidated interest expense for the three months ended March 31, 1999 was \$223,000, compared to \$210,000, an increase of 7% over the same period of 1998. This increase can be attributed to an increased borrowing base during 1999. As reported previously, the Company completed a private placement of common stock during April 1999, a portion of the proceeds of which were used to decrease the debt of the Company.

Operating Loss

The Company's consolidated operating loss for the three months ended March 31, 1999 was \$1,004,000, compared to the consolidated operating loss of \$738,000 for the three months ended March 31, 1998. This increase, in part, is due to legal fees incurred in connection with two lawsuits, both of which were settled during the first quarter, as well as the increased efforts and activities in both sales and marketing as well as R&D.

Liquidity and Capital Resources

The Company's cash and cash equivalents were \$1,346,000 at March 31, 1999, which is a decrease of approximately \$177,000 from \$1,523,000 at December 31, 1998. As of March 31, 1999, the Company had negative working capital of \$4,305,000. During the first quarter of 1999, the Company used the cash provided by operations principally for working capital needs.

Capital expenditures during the first three months of 1999 were \$34,000 and consisted primarily of computer equipment.

In April 1999, the Company completed a private placement on Common Stock in the amount of \$11.5 million. The transaction represented a sale of the Company's Common Stock to European institutional investors at a price of \$3.50 per share. A total of 3,285,714 shares of Common Stock were issued as a part of this transaction. The Company believes that its current cash balances and anticipated cash generated from operations will be sufficient to meet its anticipated cash needs through June 2000. Continuance of the Company's operations beyond June 2000, however, will depend on the Company's ability to obtain adequate financing. The Company has entered into engagement letters with Artesia Bank and Bank Degroof for a possible future public offering.

The Company intends to seek acquisitions of businesses, products and technologies that are complementary or additive to those of the Company. On May 3, 1999, the Company announced that it has acquired the global assets of SecureWare, a prominent French security software firm. SecureWare's focus is on developing security solutions for every leading operating system - including Windows NT, UNIX, IBM's S/390 and AS/400, Tandem, Digital, Stratus, Hewlett-Packard, and Sun Solaris, among others. There can be no assurance, however, that any additional acquisitions will be made.

Year 2000 Considerations

Many existing computer systems and software products are coded to accept only two digit entries in the date code field with respect to year. With the year 2000 less than one year away, the date code field in these systems and products must be adjusted to allow for a four digit year of otherwise modified so that they recognize "00" to indicate the year 2000 rather than the year 1900. Based upon its current assessments, which are based in part on certain representations of third party service and product providers, the Company does not expect that it will experience a significant disruption of its operations as a result of the Year 2000.

The Company plans to continue to identify, assess and to resolve all material Year 2000 issues by the end of 1999. The Company is developing contingency plans to address significant internal and external Year 2000 issues as they are identified. These contingency plans are expected to be complete by the end of 1999. Even with the effort to address the Year 2000 issue made by the Company to date, there can be no assurance that the systems of other entities on which the Company relies, including the Company's internal systems and proprietary software, will be remediated in a timely fashion, or that a failure to remediate by another entity and/or the Company, would not have a material effect on the Company's results of operations.

The Company has incurred approximately \$150,000 to date in addressing Year 2000 issues, and believes that no additional material expenses will be incurred related to the Year 2000 issue. The Company has completed its assessment of products and mission critical systems for Year 2000 readiness and believes no material expenses will be incurred in the future.

Additionally, the Company believes that the purchasing patterns of customers and potential customers may be affected by the Year 2000 issues as companies expend significant resources to upgrade their current software systems for Year 2000 compliance. This, in turn, could result in reduced funds available to be spent on other technology applications, such as those offered by the Company, which could have a material adverse effect on the Company's business and results of operations.

Quantitative and Qualitative Disclosures about Market Risk

There have been no material changes in the Company's market risk during the three-month period ended March 31, 1999. For additional information refer to Item 7A in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1998.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On April 6, 1999, Security Dynamics Technologies, Inc., RSA Data Security, Inc., the Company and VASCO Data Security, Inc. announced settlement on confidential terms of the claims that each of the companies had raised in litigation filed last year.

Item 2. Changes in Securities. None.

Item 3. Defaults upon Senior Securities. None.

Item 4. Submission of Matters to a Vote of Securityholders. None.

Item 5. Other Information. None.

Item 6. Exhibits and Reports on Form 8-K

a) The following exhibits are filed with this Form 10-Q or incorporated by reference as set forth below:

Exhibit Number	Description
-----	-----
27	Financial Data Schedule.

(b) Reports on Form 8-K

No reports on Form 8-K have been filed by the Company during the quarter ended March 31, 1999.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, on May 14, 1999.

VASCO Data Security International, Inc.

/s/ T. Kendall Hunt

T. Kendall Hunt
Chairman of the Board, Chief Executive
Officer and President

/s/ Gregory T. Apple

Gregory T. Apple
Vice President and Treasurer
(Principal Financial Officer and
Principal Accounting Officer)

EXHIBIT INDEX

Exhibit Number	Description
-----	-----
27	Financial Data Schedule.

3-MOS
DEC-31-1999
MAR-31-1999
1,346,217
0
2,813,483
62,000
1,341,837
6,489,027
1,083,302
727,252
8,615,361
10,793,763
0
0
21,187
(10,632,721)
8,615,361
4,308,543
4,308,543
1,835,858
2,888,483
60,679
0
223,448
(699,925)
304,181
(1,004,106)
0
0
0
(1,004,106)
(0.05)
(0.04)