MTBC

Third Quarter 2015 Earnings

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CORPORATE PARTICIPANTS

Mahmud Haq – *Chairman and Chief Executive Officer*

Stephen Snyder – *President and Director*

Bill Korn – *Chief Financial Officer*

Amritpal Deol – *General Counsel*

PRESENTATION

Operator
Good morning and welcome to the MTBC Third Quarter 2015 Earnings Conference Call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on your telephone keypad. To withdraw your question, please press star then two. Please note this event is being recorded.

I would now like to turn the conference over to Amritpal Deol, General Counsel. Please go ahead.

Amritpal Deol
Good morning, everyone. Welcome to the MTBC 2015 third quarter conference call. On today's call are Mahmud Haq, our Chairman and Chief Executive Officer; Stephen Snyder, our President and Director; and Bill Korn, our Chief Financial Officer.

Before we begin, I would like to remind you that many of our comments may contain forward-looking statements, which are made pursuant to the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve a number of risks and uncertainties that could cause our actual results to differ materially. These statements reflect our opinions only as of the date of this presentation and we undertake no obligation to revise these forward-looking statements in light of new information or future events. Please refer to our press release and our reports filed with the Securities and Exchange Commission, where you will find factors that could cause actual results to differ materially from these forward-looking statements.

With that said, I'll now turn the call over to the President of MTBC, Mr. Stephen Snyder. Steve?

Stephen Snyder
Thank you, Amrita, and thank you, everyone, for joining us for our third quarter 2015 highlights call. We are very pleased to report a number of important accomplishments during this quarter. First, we are pleased to have closed our Series A Preferred Stock offering on November 9, 2015, which generated gross proceeds of $5.1 million. The proceeds of this offering, combined with our closing of a $10 million credit facility from Opus Bank in September, have provided us with the growth capital we need to take MTBC to the next level.

Our additional growth capital comes at a strategic time as the industry is undergoing significant changes that we believe present MTBC with attractive growth opportunities. One such significant change came in October, which marked a pivotal time for the healthcare industry with the mandatory conversion from the legacy code sets, known as ICD-9, to the far more complex ICD-10 code sets. We were very pleased to see that our years of preparation, our software enhancements, and comprehensive provider training campaign allowed our clients to seamlessly transition to ICD-10, while extending the reach of our mobile health platform throughout the broader physician community.

Our ICD-10 converter app has been downloaded more than 65,000 times and it has received glowing reviews, while surging through the rankings to become the most popular ICD-10 converter app available in the Apple App Store and elsewhere in the web. Beyond promoting our brand, we have leveraged this transition to significantly increase our electronic claim capture percentage within our medical billing client base and, as a result, we are even better positioned to further increase operational efficiency and scale as we grow. We have also begun to put our growth capital to work. We have recently on-boarded three new sales team members and are continuing to work in identifying and closing appropriate acquisition targets. We expect to begin to see some of the early fruits of these efforts during the first quarter of 2016.

I'll now turn the call over to Bill Korn, our Chief Financial Officer, to provide you with a detailed review of our third quarter financial results and provide additional information on our financings. Bill?

Bill Korn
Thank you, Steve. Here are the financial highlights. Total revenue for the three months ended September 30, 2015 was $5.6 million compared to $6 million in the same period last year, a decrease of 6.7%. Total revenue for the nine months ended September 30, 2015 was $17.7 million compared to $11.2 million in the same period last year, an increase of 58%. This growth was primarily attributed to our acquisitions made at the time of last year's IPO.

While we achieved a 19% reduction in our total operating costs compared to third quarter 2014, our limited capital during the third quarter limited our ability to invest in activities to grow the business sufficiently to offset the loss in revenue in the quarter.

Adjusted EBITDA in the third quarter was a negative $184,000 compared to negative $878,000 in the third quarter a year ago, a 79% improvement. As our US headcount dropped from 275 employees on September 30, 2014 to 73 on September 30, 2015, our US payroll cost dropped by $65,000 per month or 55% from September 2014 to September 2015, while our cost in Pakistan increased by less than $100,000 a month. We spent approximately $120,000 on payroll and benefits during the third quarter for employees who are no longer with us as our US headcount continues to decrease. That reduced cost will drop to our bottom line starting in the fourth quarter. We are achieving overall reduction of our expense profile, closing offices and reducing third party software and other expenses.

Our non-GAAP adjusted net income was ($397,000) or ($0.04) per share compared to the non-GAAP adjusted net income of ($1.6 million) or ($0.15) per share in third quarter 2014. This is a 75% improvement from third quarter of last year. Our GAAP net loss in the quarter was $1.2 million or $0.13 per share compared to a GAAP net loss of $2.8 million or $0.34 per share in the third quarter of 2014. The $1 million difference between adjusted EBITDA and the GAAP loss reflects $1.1 million of non-cash depreciation and amortization expense, primarily related to purchased intangible assets, $173,000 of stock-based compensation, $151,000 of integration and transaction costs associated with acquisitions and other deals, $70,000 of net interest expense, offset by $52,000 of foreign currency gains, $52,000 of net tax benefit and a $367,000 decrease in the value of the contingent consideration liability.

This $367,000 gain from the reduction in the fair value of contingent consideration is primarily due to the decline in the price of the company's stock, as the value of the shares which are part of the purchase price from these 2014 acquisitions is now less. In addition, it went down as we accounted for shares that we do not anticipate will be earned from these 2014 acquisitions. The gain from contingent consideration must be included in our GAAP earnings each quarter but we've excluded this gain from non-GAAP adjusted EBITDA and non-GAAP adjusted net income since it is non-cash and might be reversed in a future quarter if the stock price moves higher.

We are reaching agreements with each of the three companies we acquired at the time of the IPO on the change in the actual revenue for each of the companies for the 12 months after their purchase compared to the revenue in the year before each acquisition. When the adjustment and purchase price are agreed upon with each company, the number of shares will be fixed and the value of the shares will move from a liability account to equity and there will be no further change to the value of the purchase price for each of these companies.

We made two small acquisitions during the third quarter 2015 and in both cases we paid 5% of the companies' trailing revenues upfront, and will make cash payments for 36 months based on the actual revenues we collect. Together with estimated total contingent consideration of approximately $1 million for these two companies, this amount will be adjusted based on actual and forecast revenues each quarter.

As of September 30, 2015, MTBC's cash balance was approximately $1.6 million compared to approximately $1 million on December 31, 2014.

I am pleased to report that MTBC completed its public offering of 204,000 shares of 11% Series A Cumulative Redeemable Perpetual Preferred Stock at a price of $25 per share. In addition, MTBC has granted the underwriters a 45-day option to purchase an additional 30,600 shares of Series A Preferred Stock. These shares represent a new class of security, with an 11% annual dividend payable monthly, starting in December, and a $25 liquidation preference.

The shares are not convertible. They have no stated maturity, and will not be subject to a sinking fund or mandatory redemption. Shares of Series A Preferred Stock will remain outstanding indefinitely unless we decide to redeem the shares, which can occur at the Company's option at any time after five years or within 120 days of a change of control.

MTBC's Series A Preferred Stock is trading on the NASDAQ Capital Market under the ticker symbol MTBCP. Chardan Capital Markets, LLC acted as lead book-running manager and Boenning & Scattergood, Inc. acted as joint book-running manager for the offering. Boenning and Chardan did an amazing job completing this offer.

Upon completion of the offering, Opus Bank, which provided a $10 million credit facility with a 5% annual interest rate to MTBC in September 2015, agreed to release an additional portion of the credit facility. Initially, Opus Bank released a $2 million revolving line of credit, plus a term loan of $4 million, which was used to repay outstanding debts, including an expiring line of credit with TD Bank. Opus will release another $2 million term loan this month. The final $2 million portion of the facility may become available during 2016 upon satisfaction of certain criteria.

We intend to use the proceeds from the preferred stock offering, as well as our credit facility with Opus Bank, to grow the business. This includes acquisitions of revenue cycle management or healthcare IT businesses, as well as expansion of sales and marketing activities. We spent approximately 1% of revenue on sales and marketing during the third quarter, and the availability of this capital will allow this to increase. Proceeds may also be used for working capital and general corporate purposes.

Based on our year-to-date revenue and current expectation for the fourth quarter of 2015, we're revising our revenue and earnings guidance. Because our preferred stock offering took longer than expected, until this week we have not had the capital available to invest in growth, acquisitions, revenue share partnerships or organic sales and marketing.

As a result, we are revising our full-year 2015 revenue guidance to $23 million. Adjusted EBITDA guidance for the year is revised to be between a $750,000 and $1 million loss and adjusted net income per share is revised to be between ($0.15) and ($0.20) per share for the year.

Please note that our business is cyclically lower during the first quarter because our revenue is based on the timing of payments to doctors and many people have health insurance with an annual deductible. Since insurance payments are down during first quarter, so is our revenue, and it is possible that we may have negative adjusted EBITDA during the first quarter 2016.

Our sales and marketing spending year-to-date is under 2% of revenue, which was a major contributor to decreased revenue for the year and more significantly will limit our growth during the beginning of next year.

With the successful closing of our Series A Preferred Stock and the Opus Bank credit facility, our balance sheet is now stronger than it has ever been in the company's history. We will begin investing in organic growth and acquisitions, which leaves us poised for growth in 2016.

That concludes my review of MTBC's third quarter financial results and I'll now turn the call over to our Chairman and Chief Executive Officer Mahmud Haq for some closing remarks. Mahmud?

Mahmud Haq
Thank you, Bill. The third quarter marked a major milestone for MTBC. For the first time, as Bill said, in our history we have seen that we are well capitalized to execute on our growth strategy. During our first year as a public company, we focused on integrating the three acquisitions we made at the time of the IPO. Now with the capital raised, we will be focused on growing the business, while improving the margin. I want to thank both our common and preferred shareholders for their belief in MTBC.

I would also like to thank all of our team members in the US, Poland, and Pakistan for their hard work and dedication, as well as Opus Bank and our underwriters Chardan and Boenning, who have done an amazing job in getting the preferred deal done. Finally, I want to thank our physician customers for trusting us to help manage their practice.

We will now open the call for questions. Operator?

QUESTIONS AND ANSWERS

Operator
Thank you. We will now begin the question and answer session. To ask a question, you may press star then one on your touchtone phone. If you're using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star then two. At this time, we will pause momentarily to assemble our roster.

Our first question comes from Paul Nouri of Noble Equity Fund. Please go ahead.

Paul Nouri
Hi, good morning.

Mahmud Haq
Good morning.

Paul Nouri
Sales have been declining sequentially for a few quarters and I think it is in the fourth quarter year-over-year sales are going to be down more than 20%. Can you talk to us about what's been going on in the business that, and at least it looks like you have been losing a lot of customers, at what point the bleed will stop?

Mahmud Haq

Okay. Thanks, Paul. Paul, what has happened as we have discussed in the past is we made a decision to integrate because for the last one year we've been trying to integrate all these prior acquisitions, we've made a decision about a couple of quarters ago that we will reduce the offices to make the company profitable. There have been losses, which are roughly about 12% a year in the industry.

At this point these numbers that you are talking about are basically the losses that were incurred in the second quarter and this is the aftermath, the tail end of that. Going forward, we believe that the businesses that we acquired at the time of IPO has stabilized. And as we mentioned, now we'll be focused on growing the business. Almost the entire third quarter was spent on getting this preferred deal done. And we believe that at this point the losses have trimmed down and we are comfortable with our forecast, going forward, of growth.

Paul Nouri
Okay. And now that you do have additional capital, how much more resources do you see directing towards selling and marketing and is it a matter of having hiring more salespeople or what kind of initiatives will you be putting in place?

Stephen Snyder
That's a good question Paul. We're going to be really focusing on two different parts of the strategy. One of course will be organic growth, so we've hired three new sales team members. As Bill mentioned, historically our sales and marketing expenditure has been very minimal, but we're really ramping up that team and focusing that team on organic growth where we see a significant amount of opportunity in the small to medium sized practices. On a parallel track though, we're still continuing to vet and to identify billing companies who can be good partners or acquisition targets. So, that'll be another key part of the strategy.

Paul Nouri
Okay. And then final question, the operating loss is around $1.3 million this quarter. Do you see this as a trough and you can keep improving from here or with some of the growth investments you're talking about might increase the loss a little bit in the short-term?

Bill Korn
Yes. Paul, when I look at the operating loss $1.1 million of the $1.3 million is the non-cash charge for amortizing the intangibles that come from acquisitions and from depreciation. So, in some respects, looking at that number, it's an accounting number, it doesn't really impact our cash flow and that's really why we tend to look more at the adjusted EBITDA and the adjusted net income.

And having said that, I expect to see our operating loss continue to decrease, I expect to see our adjusted EBITDA and our net income turn from losses to positive numbers through a combination of activities. As I mentioned, we continue to rationalize our cost structure, so there were employees and there were offices that we were paying for at the beginning of third quarter that were no longer with us by the end of third quarter.

So, even if we did nothing else, you'd start to see the expenses go down, but in fact we have continued to focus on reducing costs, while at the same time focusing on starting to ramp up marketing and sales. So there'll be a little bit of extra spending in the marketing and sales arena, but there'll also be decreased spending in G&A and direct operating costs. So net-net, I expect to see the operating loss continue to decrease over time.

Paul Nouri

Okay. Thank you.

Operator
Our next question is from Keay Nakae of Chardan. Please go ahead.

Keay Nakae
Yes, thanks Bill, just continuing on that same topic, as we look at Q4 operating expense, you mentioned the costs that are coming out due to the reduction in employees, but you are also adding a couple, so net-net what's the impact in Q4?

Bill Korn
So, net I expect to see our operating costs continue to decrease and, yes, we've added a couple of people, but the number of people that we reduced has actually been a lot more than the number of people that we have brought on. We've also taken a couple of folks who were focused on integrating the acquisitions during the first three quarters of the year and moved them into sales and marketing focused roles.

Again, my experience is you almost never see a company spending 1% of revenue on marketing and sales. You're going to see us start spending more, like any other company, but the good news is as we spend on marketing and sales you'll start to see new customers coming on board, which will allow the top line to grow. So, we think it's a good trade-off.

Keay Nakae
Okay. My second question relates to the investment in organic growth, so what do you guys consider to be the low-hanging fruit in that area that you could perhaps capture?

Stephen Snyder
We see a lot of opportunity, Keay, in the smaller practice end of the market, the practices that have not yet adopted any technology and are continuing, for instance, to try to capture charges, even with ICD-10, trying to capture charges in a manual way. We think that that is a losing battle long-term and we've developed our platform and we've leveraged our human resources in such a way that we're able to provide smooth onramps for those practices that have resisted technology. So, we really see the most significant opportunities in the smaller practices.

Keay Nakae
Okay. And if we think about acquiring businesses in the manner that you had in the past with a little bit more capital to spend in that area, what's out there and how soon could you add those types of assets as you've done historically?

Mahmud Haq
Keay, we believe that in the fourth quarter we will be acquiring with this capital. We are in discussions with a number of smaller companies and, as you know, in our space right now, HealthFusion was purchased by NextGen earlier this month. HealthFusion is almost identical to our size and our technology. They were purchased by NextGen for $165 million, roughly a five plus multiple of revenue. So, I think there's a lot of activity. People are realizing that without the cloud EHR offering, this landscape is changing. So, we believe that there'll be a number of these smaller companies who will come to the same conclusion and they'll be available for acquisition for us. We expect to complete one or two acquisitions in the first quarter 2016.

Keay Nakae
Okay. And just in terms of your investment discipline, given the market environment right now, are

these practices businesses you can acquire at less than 1X revenue, is that a goal?

Mahmud Haq
Yes.

Keay Nakae
Give us some thoughts on that.

Mahmud Haq
Right, and I think for the ones that we are focusing on, the smaller ones, the multiple as I mentioned, for companies like us and HealthFusion with technology and a back office, the multiples are different, but for these smaller mom-and-pop type companies I think the multiples are still usually one or below, and that's off revenue. That's what we plan to pay going forward.

Keay Nakae
Okay. And then in terms of, just going back to the early question on maintaining revenue at the currently owned assets, respecting the fact that you had the reduction in Q2, it still looks like, if we look at your numbers, a sequential decline Q3 to Q4, so help us understand that in terms of your guidance of $23 million.

Bill Korn
Because our business is virtually all recurring revenue coming from existing clients, if a client is with you on July 1st but they're not there on September 30th you will have received some revenue from them during Q3 but you won't receive any revenue in Q4. And we have enough history to see that people don't tend to go to the doctor during Thanksgiving, they don't tend to go to the doctor during Christmas, so we factor all that into our forecast.

Keay Nakae
Okay. And then and just finally in terms of expected interest expense, you're going to get the second tranche of $2 million, how should we be thinking, then, of the quarterly interest expense?

Bill Korn
Yes, so our loan with Opus Bank is at a 5% interest rate. So, obviously that's really competitive. In some respects, the fact that we're getting this $2 million tranche of term debt means that we can take the $2 million revolver and use it the right way, which is basically money sitting there for a rainy day. So, the net effect is the total amount borrowed may not be dramatically different, and therefore the interest expense won't be dramatically changed. So, you could look at it and say $4 million of term plus $2 million, so now I have $6 million outstanding at 5% interest; not a bad deal for a company of our size.

Mahmud Haq
And Keay, the first year for Opus on the term loan is interest only, basically.

Bill Korn
Right.

Mahmud Haq
And a year out, we start making the payments on this.

Bill Korn
Right, a year out we will start amortizing the principal.

Keay Nakae
Okay. Thanks, that's all I had.

Mahmud Haq
Okay, I think to finish up Keay, as you know that 60% of our common stock is owned by the insiders and we are running the company like it's our own money. We have been very prudent with the interest, with Opus that's what Bill mentioned at 5%, we got $10 million roughly at 5% and we raised another $5 million at 11%, Bill, our weighted average cost is about—

Bill Korn
It's about 7% now.

Mahmud Haq
About 7%, Keay, which is very competitive for a company of our size and the transaction that we went through putting companies together. We feel that at this point we are very well positioned when we look at HealthFusion getting five times multiple with opportunity in the marketplace with the capital that we have now. We have never felt more confident that we will execute our plan in the quarters to come.

Operator
As a reminder, if you'd like to ask a question, please press star then one at this time. We are showing no further questions. This does conclude our question and answer session. I'd like to turn the conference back over for any closing remarks.

CONCLUSION

Amritpal Deol
Thank you, Emily. Thank you, everyone, for joining the MTBC third quarter results conference call.

Mahmud Haq
Thank you.

Operator
The conference is now concluded. Thank you for attending today's presentation, you may now disconnect.