MTBC

Fourth Quarter 2016 Earnings

March 31, 2017 at 8:30 AM Eastern

CORPORATE PARTICIPANTS

Shruti Patel - *General Counsel*

Mahmud Haq - *Chairman and Chief Executive Officer*

Stephen Snyder - *President and Director*

Bill Korn - *Chief Financial Officer*

PRESENTATION

Operator
Good morning and welcome to the MTBC Fourth Quarter 2016 Earnings Conference Call. All participants will be in 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 Shruti Patel, General Counsel. Please go ahead.

Shruti Patel
Good morning, everyone. Welcome to the MTBC 2016 Fourth Quarter Conference Call. On today's call are Mahmud Haq, our Chairman and Chief Executive Officer; Stephen Snyder, our President and a 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 Chairman and CEO of MTBC, Mr. Mahmud Haq. Mahmud?

Mahmud Haq
Thank you, Shruti, and thank you for joining us on our fourth quarter 2016 call. We are pleased to announce a 65% growth in revenue over fourth quarter 2015 and third quarter 2016 and our third consecutive quarter of quarter-over-quarter revenue growth. We are greatly encouraged by the growth opportunities provided by our recent acquisition of MediGain and look forward to delivering strong revenue and EBITDA growth in 2017.

As previously announced on October 3, 2016, MTBC achieved a corporate milestone in its acquisition of substantially all of the assets of MediGain, LLC, a Texas-based medical billing company, and its subsidiary, Millennium Practice Management, LLC, a New Jersey-based medical billing company, together known as MediGain.

Expected to be accretive to shareholders in 2017, the acquisition reflects the strategic nature of MTBC's acquisition-based growth strategy.

I would now like to turn the call over to our President, Steve Snyder, to discuss this exciting deal in more detail. Steve?

Stephen Snyder
Thank you, Mahmud. As Mahmud mentioned, we are pleased to have acquired MediGain during the fourth quarter of last year. As a result of this acquisition, we have expanded our customer

base and have on-boarded talented team members from MediGain who are helping us further enhance our operational capabilities and successfully leverage growth opportunities.

During the six months since closing the MediGain transaction, we have significantly reduced MediGain's operating costs, while improving their processes and ability to grow and to retain customer relationships. Moreover, our combined sales team has leveraged our corporate synergies to accelerate organic growth. As we move forward, we expect to continue improving operating margins throughout 2017 while continuing to also deliver outstanding technology solutions and services to our new and existing customers.

I'll now turn the call over to Bill Korn, our Chief Financial Officer, who will provide you with a detailed review of our full-year and fourth quarter financial results. Bill?

Bill Korn
Thanks, Steve. We are pleased to report that revenues for the three months ended December 31, 2016 were $8.8 million compared to $5.4 million in the same period of 2015, which represents 65% revenue growth. The increase was primarily a result of the MediGain acquisition, which occurred on October 3, 2016.

Our fourth quarter 2016 GAAP net loss was $4 million, or 46% of net revenue, compared to a GAAP net loss of $802,000 for the fourth quarter of 2015. The increase in the net loss is primarily the result of planned short-term increases in operating expenses related to the acquisition and integration of MediGain. Fourth quarter revenue increased by $3.5 million, or 65%, while direct operating costs increased from $2.4 million in the fourth quarter of 2015 to $6.1 million in the fourth quarter of 2016, and G&A increased $2.6 million to $4.3 million.

On October 3, the day we purchased MediGain, we began reducing expenses. For example, four subcontractor firms represented $750,000 of the fourth quarter 2016 direct operating expense, and as of today, we have transitioned all of the work from these four subcontractor firms to our employees. These transitions significantly reduced our operating expenses while improving performance. We have also been deploying our experienced team and our technology to reduce personnel and related operating expenses. Finally, we have reduced the facilities costs associated with MediGain by approximately 70%.

The GAAP net loss for the fourth quarter was $0.42 per share, calculated using the net loss attributable to common shareholders divided by the weighted average number of common shares outstanding.

Non-GAAP adjusted net income for fourth quarter was negative $1.3 million or negative $0.12 per share, compared to the non-GAAP adjusted net income of $121,000 in the same period of 2015. Non-GAAP adjusted net income per share is calculated using the end-of-period common shares outstanding, including shares which are part of contingent consideration.

Adjusted EBITDA for the fourth quarter was negative $814,000 or negative 9.2% of revenue compared to adjusted EBITDA of positive $312,000 or 5.8% of revenue in fourth quarter 2015.

Turning to the full year, MTBC's revenues for the year ended December 31, 2016 were $24.5 million compared to $23.1 million in 2015, an increase of 6%.

The GAAP net loss for the year ended December 31, 2016 was $8.8 million, 36% of net revenue, or $0.95 per share, compared to a GAAP net loss of $4.7 million in 2015. The net loss for 2016 includes $5.1 million of non-cash depreciation and amortization expense, primarily the result of amortizing purchased intangible assets. The increase in the cash portion of the net loss is primarily the result of an increase in operating expenses due to the acquisition of MediGain during fourth quarter 2016.

Non-GAAP adjusted net income for the year ended December 31, 2016 was negative $2 million or negative $0.19 per share compared to non-GAAP adjusted net income of negative $1.4 million in 2015.

Adjusted EBITDA for the year-ended December 31, 2016 was negative $605,000 or negative 2.5% of revenue compared to adjusted EBITDA of negative $675,000 or negative 2.9% of revenue in 2015. The difference of $8.2 million between adjusted EBITDA and the GAAP net loss in the year 2016 reflects $5.1 million of non-cash amortization and depreciation expense, $1.9 million of stock-based compensation, $1 million of integration and transaction costs related to recent acquisitions, $197,000 of provision for taxes, and $646,000 of net interest expense, offset by a $716,000 decrease in the contingent consideration liability.

Management believes that our non-GAAP metrics are closer to reflecting our cash flow, and we will focus on driving positive adjusted EBITDA during 2017.

I'd like to talk for a minute about our cash balance and liquidity. As of December 31, 2016, the Company had $3.5 million in cash, our stockholders' equity was approximately $7.1 million, and our accumulated deficit was approximately $17.9 million. The Company had a working capital deficiency of approximately $7.4 million, the majority of which is attributable to the balance of the MediGain purchase price.

MTBC purchased MediGain on October 3, 2016 by acquiring MediGain's debt to Prudential Insurance for $7 million and immediately foreclosing on MediGain's assets, including customer relationships, accounts receivable, fixed assets, and intellectual property. We paid Prudential $2 million up front and still owe Prudential $5 million, of which $3 million is now due.

In order to satisfy our existing obligations, management believes additional funding will be necessary, which might be in the form of sales of additional shares of our Series A Preferred Stock, our common stock, or some other instrument. We may seek additional capital from public or private offerings or may elect to borrow additional amounts under new credit lines or from other sources. If the Company issues equity or debt securities to raise additional funds, our existing stockholders may experience dilution; we may incur significant financing costs, and the new equity or debt securities may have rights, preferences, and privileges senior to those of existing shareholders.

Management concluded that without additional financing there would be doubt about the Company's ability to continue as a going concern within a year after the date the financial statements were issued. As a result, the audit report included in MTBC's Annual Report on Form 10-K, to be filed this afternoon, will contain a going concern emphasis-of-matter paragraph.

The Company anticipates full-year 2017 revenue will be approximately $30 million to $31 million, which represents growth of 22% to 27% over 2016 revenue. In large measure, this is the result of the MediGain acquisition, which occurred on October 3, 2016 and will contribute to the full-year of 2017 instead of just a single quarter. We expect adjusted EBITDA to be $2 million to $2.5 million for full-year 2017, anticipating that the first quarter will be slightly negative due to planned integration expenses, but each successive quarter will be positive and reflect growth. Our prospects for growth and profitability have never been stronger.

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

Mahmud Haq
Thank you, Bill. We are excited by the revenue growth we reported in fourth quarter 2016. The integration of MediGain into our business is going very well and we anticipate this will give us the scale we need to generate adjusted EBITDA starting with Q2 of 2017. MTBC has never been in a stronger position and we look forward to giving you future updates on our progress.

I would like to thank our team members for their hard work and dedication. Finally, I want to thank the physician customers for trusting us to help manage their practices.

We will now open the call to questions. Operator?

QUESTIONS AND ANSWERS

Operator
We will now begin the question-and-answer session. To ask a question, you may press star, then one on your telephone keypad. If you are using a speaker phone, 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.

The first question comes from Keay Nakae of Chardan. Please go ahead. Mr. Nakea, your line is open. Please go ahead with your question.

Keay Nakae
Yes. Thank you. I want to talk about the operating expense. So, sequentially in the quarter, you have direct operating expense of about $3.5 million, and G&A of $1.7 million. So, how do we think about these numbers going forward as you try to whittle down the operating expense of MediGain?

Bill Korn
Yes. That's a good question, Keay. The good news is we took a lot of actions during fourth quarter to reduce expenses. For example, on the day of the acquisition, MediGain had four subcontract firms, and clients weren't terribly pleased with the work that was being done by those firms. The good news is as we move work to our employees, customers found they were getting better results, getting better reimbursement from insurance; so customer satisfaction went up, and our costs went down dramatically.

So, what you'll see in Q1 of 2017, you'll see the tailing off of those subcontractor expenses, and then as you move into Q2, you'll see that subcontractor expenses are essentially gone. So, again, as a point of reference, in Q4 the subcontractor firms were roughly $750,000 and by the time you get to Q2 of 2017, that number is $0.

In addition, we picked up a very strong team from MediGain in Sri Lanka. We've actually expanded that office a little bit. The cost in Sri Lanka is very similar to the cost of our team in Pakistan; so we're relying more on people who are our employees in both countries. We're looking at work that's being done by US employees and our model is to think about what can be automated, and that which can't be automated, how do we provide the best work most cost effectively. So, again, what you'll see is reduction in payroll expense that hits both direct operating costs and G&A. You'll see those numbers reduced in Q1 of 2017 and you'll see further reductions in Q2 and going forward.

Finally, we've looked at the employees who have the strong relationships with the clients. We looked at the account managers and the sales and marketing team and those are the folks that we're keeping. So, what you'll actually see in terms of sales and marketing is a bit of an increase in sales and marketing going forward, and concurrent with that, you'll find for the first time in a long while, we're actually starting to sign up a reasonable number of new clients, which will be producing organic revenue growth, something that we had not been able to do in the past because, candidly, we were spending almost no money on sales and marketing.

Keay Nakae
So, if we add all that up, how much more expense is there to wring out, because, again, we're talking about a sequential increase of over $5 million in the quarter? Yes, you've got the $750,000 that you mentioned, but what about the balance of that increase in expense? What percentage of that can you realistically expect to reduce?

Bill Korn
Maybe one way to look at that is if you look at the gross profit line. Gross profits have been 60% in the past. They were 31% in Q4 of 2016. There's no reason why they won't get back to 60% by the end of the year, so while it would be hard for me to draw the exact straight line, you'll see those operating costs going down and, therefore, you'll see the gross margin going up.

On sort of the flipside, G&A in fourth quarter was 50% of revenue and, again, a lot of that was driven by expenses we picked up from MediGain, so, A) you'll see some of those expenses going away; and, B) you'll start to see revenue growing. So, I expect to see G&A decreasing over time. Again, I don't have a crystal ball, but a target of getting it to the 30% is certainly not unreasonable.

Keay Nakae
Okay. Then, on the top line, historically you've had—we've seen an attrition rate of acquired revenue. So, what does that look like for both MediGain after six months and for some of the other acquisitions you did in 2016, like Gulf Coast and some of the other smaller ones?

Mahmud Haq
Keay, let me—this is Mahmud—let me answer that question. If you go back and look at our IPO in 2014, it took us about six quarters to bring it back to a cash flow positive, and the amount of acquisition revenue was about the same, about $15 million or so at that time. This time around, the reason we are very excited about the prospect is that it took us less than two quarters to wring out, as Bill mentioned, a majority of the expenses and if you look at the revenue, our revenue is stabilized. If you look at the full-year forecast, full-year guidance that we are giving of $31 million, $32 million, roughly it's $8 million a quarter. We are very comfortable with that number.

So what I'm saying is attrition is significantly less than what we experienced at the time of our IPO. Our expenses will wring out very quickly. We learned from our mistakes after the IPO, and at this point it's stable. The revenue, let's say, four quarters of $8 million, kind of gives you $32 million. So, we believe that the revenue is stable. We already have the first quarter closing today, so we are comfortable with that number.

To your other question about expenses, we think that — I would say about 60% to 70% expenses have been reduced so far and about 30% or so has yet to be reduced.

Keay Nakae
Okay. That's helpful. Just factoring in the typical Q1 seasonality due to the new thresholds for deductibles, what sequentially should we be thinking about for that Q1 revenue versus Q4? Traditionally it is lower. Is that the case as well?

Mahmud Haq
I think if you just take the $32 million, divided that by four, $8 million—I think that gives you a good threshold for quarterly revenue. Today being the last day of Q1, we are comfortable with that number.

Keay Nakae
Okay. Very good. That's helpful. Thanks. That's all I have.

Mahmud Haq
I think that's the exciting part. We believe that at this point, at the end of first quarter, we are where we wanted to be in terms of reduction of expenses and revenue control of attrition. As Bill mentioned, with the sales team that we have in place today, we feel that there will be, not only that we will replace the natural attrition, but there'll be a net increase in our revenue going forward from organic sources.

And, which I'm sure you've figured out — we are not focused right now on acquisition; we are just focused on getting this profitable this 2017 and organic growth.

Keay Nakae
Okay. Thanks.

Mahmud Haq
Thanks.

Operator
Once again, if you have a question, please press star, then one.

This concludes our question-and-answer session. I would like to turn the conference back over to Shruti Patel for any closing remarks.

CONCLUSION

Shruti Patel
Thank you, Andrew, and thank you everybody for joining us. That will conclude our 2016 fourth quarter call.

Mahmud Haq
Thank you.

Shruti Patel
Thank you.

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