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Zacks Small-Cap Research

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Brian Marckx, CFA
bmarckx@zacks.com
Ph (312) 265-9474

scr.zacks.com
10 S. Riverside Plaza, Chicago, IL 60606

Medical Transcription Billing (MTBC-NASDAQ)

Orion Synergies Could Double Adj EBITDA in 2019

Based on the average of implied EV/EBITDA and P/S multiples from analysts' estimates of publicly traded EHR / RCM companies and providers of related technology and services, we calculate fair value of MTBC at approximately $11.0/share

Current Price (03/25/19)	$4.57
Valuation	**$11.00**

OUTLOOK

Orion is credited with revenue ($50.5M) beating management's FY2018 guidance of $49M - $50M and adjusted EBITDA ($4.8M) coming in at the high end of their $4.0M - $5.0M estimate. Meanwhile, their initial 2019 guidance for revenue growth of at least 20%, which was announced in a January 2019 shareholder letter, has already been adjusted – to growth between 25% and 29%. Adjusted EBITDA is expected to come in between $8M and $10M – implying growth of 67% - 108%.

The 2019 guidance assumes organic growth from existing and new clients as well as potential 'tuck-in' deals (i.e. small transactions, which we refer to as 'one-and-dones'). Driving much of the anticipated growth in adjusted EBITDA (and operating leverage) is significant expense reduction of Orion's operating costs. MTBC indicated that they have already made substantial progress in this regard, noting that they rapidly shed costs of Orion's RCM business by replacing (relatively expensive) third-party subcontractors with their own (Pakinstan and Sri Lanka-based) employees, shuttering some of Orion's offices and improved efficiencies by moving clients to their own platform. To-date, MTBC has reduced Orion's RCM-related operating expenses by 52%.

Our PT has moved to $11.0/share, largely related to anticipated greater synergies from Orion.

SUMMARY DATA

52-Week High	**$5.65**
52-Week Low	**$3.13**
One-Year Return (%)	**33.53**
Beta	**2.06**
Average Daily Volume (sh)	**55,658**
Shares Outstanding (mil)	**12**
Market Capitalization ($mil)	**$54**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**6**
Insider Ownership (%)	**50**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**20.8**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2019 Estimate	**N/A**
P/E using 2020 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Avg.,**
Type of Stock	**Small-Blend**
Industry	**Healthcare IT**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	8.2 A	7.8 A	7.5 A	8.3 A	31.8 A
2018	8.3 A	8.7 A	17.0 A	16.5 A	50.6 A
2019	15.3 E	16.0 E	16.3 E	16.5 E	64.1 E
2020					70.2 E

EPS (GAAP)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	-$0.29 A	-$0.20 A	-$0.14 A	-$0.08 A	-$0.69 A
2018	-$0.06 A	-$0.09 A	-$0.25 A	-$0.20 A	-$0.59 A
2019	-$0.22 E	-$0.13 E	-$0.08 E	-$0.04 E	-$0.47 E
2020					-$0.10 E

Zacks Projected GAAP EPS Growth Rate - Next 5 Years % **N/A**

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WHAT'S NEW…

Q4 2018 Results:
MTBC reported financial results for their fourth quarter 2018 and provided a business update. This was the second quarter with inclusion of Orion, the acquisition of which closed on July 1st. Financial performance immediately benefitted from the transaction, which included revenue setting record highs in Q3 and two of the three acquired business segments, namely Practice Management and the GPO, adding to profitability in that period.

Importantly, not only did the benefits of the acquisition continue through the final period of 2018 but management's updated revenue and adjusted EBITDA guidance implies Orion's contribution to profitability, and potentially to the topline as well, will grow. Orion is credited with revenue ($50.5M) beating management's FY2018 guidance of $49M - $50M and adjusted EBITDA ($4.8M) coming in at the high end of their $4.0M - $5.0M estimate. Meanwhile, their initial 2019 guidance for revenue growth of at least 20%, which was announced in a January 2019 shareholder letter, has already been adjusted – to growth between 25% and 29%. Adjusted EBITDA is expected to come in between $8M and $10M – implying growth of 67% - 108%.

The 2019 guidance assumes organic growth from existing and new clients as well as potential 'tuck-in' deals (i.e. small transactions, which we refer to as 'one-and-dones'). Driving much of the anticipated growth in adjusted EBITDA (and operating leverage) is significant expense reduction of Orion's operating costs. MTBC indicated that they have already made substantial progress in this regard, noting that they rapidly shed costs of Orion's RCM business by replacing (relatively expensive) third-party subcontractors with their own (Pakistan and Sri Lanka-based) employees, shuttering some of Orion's offices and improved efficiencies by moving clients to their own platform. To-date, MTBC has reduced Orion's RCM-related operating expenses by 52%.

Additional benefits of these cost-cutting measures are expected to be realized (on the income statement) in the coming quarters. MTBC's 2019 guidance implies ~27% (midpoint of guidance) revenue growth but ~88% adjusted EBITDA growth – with the difference between the two growth rates largely reflective of synergies and efficiencies. This is an important point especially when considering MTBC generated adjusted EBITDA of $1.4M in Q4'18, revenue is expected to remain at approximately that same annualized run-rate through 2019 and operating expenses should fall considerably (from the Q4'18 run-rate).

While the 2019 guidance does not assume any meaningful acquisitions, it is clear that management remains on the look-out for another Orion or MediGain-type transaction. They exited 2018 with $14.5M in cash and $10M available under their untapped credit facility. Coupled with the fact that MTBC is now generating consistent positive cash flow, they have the resources to do another sizeable deal. And, as we have noted in the past, given their ability identify undervalued assets and to quickly integrate (and cut costs) without significant disruption to their ongoing operations or to those of the acquired company, a near-term transaction could result in upside to their current guidance.

Q4 Financials
Revenue, at $16.5M was up 99% yoy and down 3% from Q3. Orion-related assets contributed approximately $8.4M, representing 51% of total revenue including $5.0M from the RCM (38% of total), $3.2M (19% of total) from practice management and $178k (% of total) from their GPO.

Total revenue was about 3% better than our $16.1M estimate with almost all of the difference related to better than anticipated RCM sales ($13.2M A vs $12.7M E). Further disaggregating the RCM segment, our miss on the low side relates to MTBCs legacy RCM ($8.1M A vs $7.6M E), which was partially offset by estimating slightly high on Orion's RCM ($5.0M A vs $5.1M E). MTBC noted that renewal rates of the RCM customers remains high with 89% renewing in 2018, largely unchanged from 2017 (90%). Renewal rates among RCM customers that also use the company's HER were even better, with 91% renewing in 2018 (compared to 98% in 2017.

Meanwhile, we were relatively close in both the practice management ($3.2M A vs $3.2M E) and GPO ($178k A vs $201K E) segments. As a reminder, the practice management segment consists of managing three pediatric practices in five locations in Ohio and Illinois, whereby MTBC employs the medical personnel and administration and owns the assets used in the business in return for a management fee. Financial performance of the PM segment should remain fairly consistent. The low variability of revenue and earnings of that business is due to the long contract terms (i.e. 40-year contracts, with ~20 years remaining).

Both the GPO and PM business are already profitable and were accretive to MTBC's results in 2H'18. The regular and predictable earnings of both segments are also attractive from a valuation standpoint, in our opinion. Cross-selling opportunities between the GPO and RCM customers could provide a very efficient complementary incremental revenue stream. Management has indicated that they have already had success with leveraging that opportunity, noting on the Q4'18 call that ~100 existing RCM clients are now customers of the GPO. And, as their comfort level grows in the physician practice management space, we would expect MTBC may be looking to opportunistically add additional practices.

Adjusted EBITDA…

Adjusted EBITDA was $1.4M and $4.8M in the three and twelve months ending 12/31/18, which compares to $1.5M and $2.3M in the prior-year periods. As noted, given that much of the benefits of Orion-related cost-cutting, efficiencies and synergies have yet to be realized, we think operating expenses fall from Q4'18 to Q1'19 and, again, from Q1 to Q2'19. Coupled with expectations of double-digit revenue growth, we now model adjusted EBITDA of $8.0M in 2019 (i.e. the low end of MTBC's $8M - $10M guidance), upwardly adjusted from our previous estimate of $7.5M.

Valuation

We have made adjustments to our model following reporting of Q4'18 results. We now look for FY'19 revenue and adjusted EBITDA of $64.1M and $8.0M, updated from $66.9M and $7.5M. Our FY'20 revenue and adjusted EBITDA are $70.2M and $11.0M.

See our valuation methodology at the end of this report. Updates to our model have moved our calculated fair-value from $9.5/share to $11.0/share.

Investment Thesis

MTBC's EHR / Billing Solution Targets Needs of Small Practices

MTBC's flagship product, PracticePro, is a fully-integrated software-as-a-service (SaaS) web-based platform with a comprehensive suite of functionality designed to streamline the day-to-day operations of medical practices and improve their financial performance. MTBC's proprietary technology and related services include EHR, practice management software and revenue cycle management (RCM) aimed at improving workflow, easing administrative burdens (such as those related to billing, insurance and patient scheduling), reducing insurance claim denials and meeting federal mandates related to adoption and use of healthcare information technology.

PracticePro is a certified EHR as defined by ONC and provides all of the functionality required for establishing 'meaningful use'. Integrated with clinical partners across a wide range of specialties, such as LabCorp (for lab testing and results), SureScripts (for e-prescriptions), HealthCare Compliance Network (for healthcare regulatory compliance), NCO Group (for collections) and Dr. First (for patient data and communication), MTBC's platform provides users with a complete EHR solution.

Per the description of PracticePro on MTBC's website, the system includes the following functionality;

- E-prescribing: prescribe drugs electronically via their SureScripts certified solution
- Patient health records: patients can access their records online, receive statements, make payments and schedule appointments
- Insurance eligibility: instantly verify patient insurance eligibility – reduces risk of claim denials
- Messaging: direct and secure messaging between physicians and patients
- Balance reminder calls (BRC): BRC automatic reminder calls to patients for unpaid invoices reduces cost of collections and improves cash flow and profitability
- Real-time claims adjudication (RTA): flags claims and reimbursement processing errors in real-time to reduce insurance denials and improve collections and cash flow. MTBC's RTA is partnered with national and regional payers
- Patient scheduling: schedule patients appointments and send reminders. Functionality includes the ability to set up automated appointment reminders which can reduce no-shows
- Lab integration: order lab services directly with major labs including LabCorp and Quest
- Business Intelligence: key financial information and metrics which practices can use to make informed operational decisions

- WebEHR dashboard: summary of daily action-items including appointments, messages, pending medication refill requests and patient lab results in a graphical dashboard
- Mobile connectivity: functionality via mobile apps (for iOS and Android) includes 'Patient Health Records App', 'iCheckIn' (for patient check-in, personal information, insurance and payments), 'iRx' (prescription approvals and refills), 'Dictate' (dictate patient notes), 'iEHR' (complete EHR) and 'ICD 9-10 converter' (converts reimbursement coding from legacy to current)
- WebPro: create and maintain professional website

MTBC's EHR Solution



SOURCE: mtbc.com

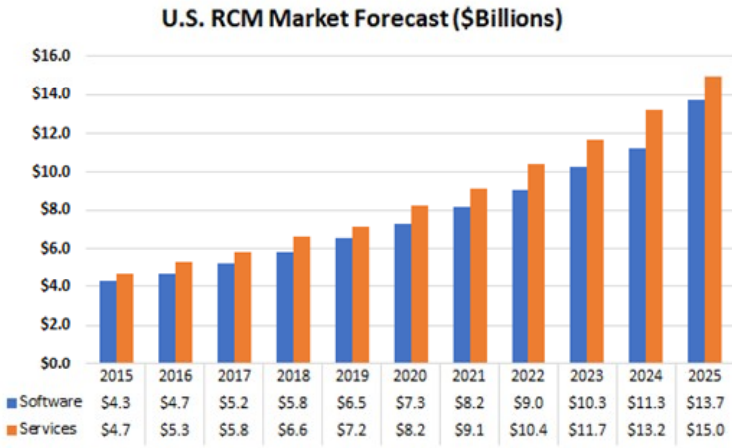
MTBC Provides Bundled EHR / Practice Management, Generates Revenue From Medical Billing Service…
As evidence from the above referenced clinical studies and surveys show, the cost, complexity and (over-) functionality of certified EHR systems means that they (and the meaningful use mandate) often don't fit with the budgets, capabilities and needs of small physician practices. Recognizing this disconnect, MTBC aligned their business and revenue models in such a way so its customers (i.e. mostly small practices) can meet the meaningful use mandates (and receive associated incentives) by adopting their EHR technology and do so with little-to-no cost. They have also been highly cognizant of the disconnect between the meaningful use mandates and the needs of physician practices, as well as MIPS-related performance measures, and have used that knowledge in developing more intuitive, user-friendly and functional EHR technology aimed primarily at the small-to-medium sized physician segment.

In August 2017 MTBC introduced 'talkEHR', their new ONC-certified proprietary EHR solution, which will be rolled out through 2018. talkEHR incorporates artificial intelligence built on Google Voice framework to provide voice assistant functionality. This enables simple, hands-free operation which is expected to further improve upon user-friendliness and reduce time and effort of data input. MTBC offers talkEHR free of charge, including full data migration to their platform, to healthcare practices which are then offered the opportunity to upgrade to their (revenue generating) services.

Instead of charging for EHR, MTBC generates revenue from revenue cycle management (i.e. medical billing) and related services that it provides to medical practices. Many small physician practices may not have the utility for a full-suite of EHR functionality, but do find a need for more efficient, productive and less costly medical billing. Any customer that contracts with MTBC for their medical billing services receives their EHR and practice management software for free.

Physicians Turning to RCM Outsourcing To Address Billing, Reimbursement Challenges…
More and more physicians are expected to turn to RCM services as a way to address the time and costs necessary to keep up with increasing complexity of medical billing, changes in reimbursement and related coding, and requisite technology upgrades. According to a recent survey by healthcare IT research firm, Black Book, traditional medical billing solutions are increasingly crimping practitioners' margins, prompting a majority of the 2k physicians surveyed to seek more efficient billing methods. But, Black Book noted that (as of 2016), 90% of small, independent practices remain unprepared for the new billing challenges presented by value-based care mandates.

According to Grand View Research[1], in 2015 the U.S. RCM market was worth approximately $9B, which included $4.2BM for software and $4.8B for services. They forecast the market to grow to about $28.7B (12% CAGR) by the year 2025, with software accounting for $13.7B (13% CAGR) of the market and $15.0B (12% CAGR) related to RCM services. Grand View cites increasing complexity of managing revenue cycle processes as a result of regulatory reforms, as well as greater financial challenges [faced by providers], as catalysts driving growth of the U.S. RCM services market. In addition, greater focus on reducing claim denials and improving overall work efficiencies through better medical billing management are also mentioned as expected contributors to RCM market growth.



SOURCE: Grand View Research and analyst estimates

Revenue Model Aligns MTBC's Interests With Those of Their Customers…

MTBC's revenue model also aligns their interests with those of their customers. MTBC charges 5% of a practice's net collections (in addition to a small one-time set-up fee), incentivizing MTBC to minimize insurance claim denials, remain current on insurance coding and billing practices, verify patient insurance eligibility and co-pay responsibility, shorten accounts receivable aging and everything else that relates to maximizing collections and cash flow for their customers. In addition to aligned interests, MTBC believes that their fees (i.e. 5% of collections plus small set-up fee) are among the lowest in the industry. Medical billing services account for approximately 89% of MTBC's total revenue.

MTBC has demonstrated significant success with their RCM services, as evidenced by high scores on certain industry metrics. MTBC reported that during 2017 (and 2016) they scored;

- First pass acceptance rate of ~96% (96%): this compares to ~95% of the top 12 payers
    - First pass acceptance is the % of claims submitted electronically to insurers that are not denied
- First pass resolution rate of 94% (94%)
    - First pass resolution is the % of primary claims that are favorably adjudicated after one submission
- Median days in A/R: 37 (33) days for primary care and 41 days (40) for specialist practices. This compares to a 2016 national average of 36 days and 40 days
    - Median days in A/R is directly influenced by first pass acceptance and first pass resolution performance

MTBC also offers clearinghouse and electronic data interchange (EDI) services, services which optimize insurance companies' enrollment processes and track claims and which were obtained through their acquisition of SoftCare in July 2015. Clearinghouse and EDI services currently account for approximately 3% of MTBC's total revenue and are expected to grow from the recent launch of 'EnrollmentPlus, a software-as-a-service EDI service. Another ~8% comes from other (non-billing) ancillary services which includes printing and mailing services (capabilities which came with MTBC's July 2016 acquisition of WFS Services), transcription services, platform usage fees (related to customers' use of non-MTBC EHRs) and coding services. Unlike billing services, fees for ancillary services are generally based on a per unit of work basis.

[1] Revenue Cycle Management Market Analysis By Product, By Type, By Delivery Mode, By End-use, & Segment Forecasts, 2018 - 2025

As of the close of 2017, MTBC serviced 980 customers, including 750 to which they provided medical billing services and 230 which used their clearinghouse and electronic data interchange services. In addition, 950 providers had signed up for talkEHR, 40 of which were actively using it in their practice.

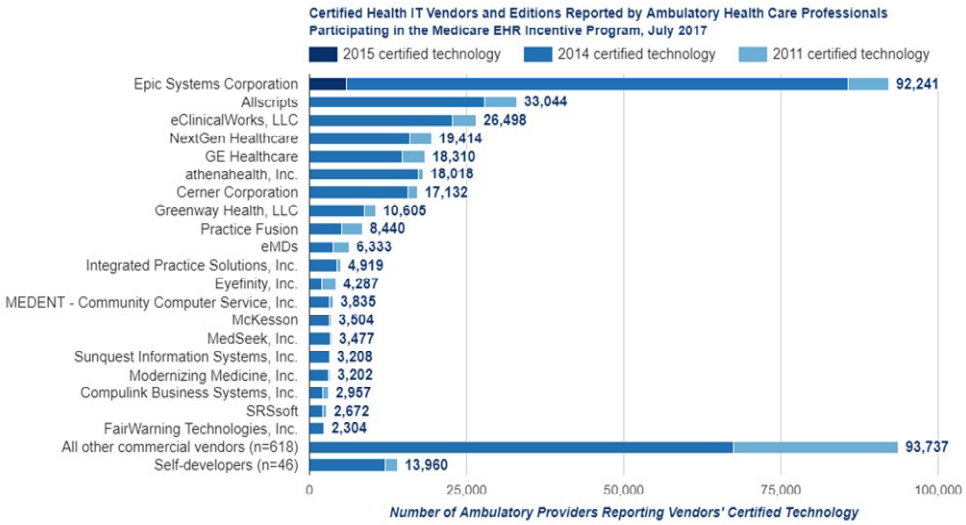
EHR Market and Vendors

The HITECH Act and meaningful use mandates not only spurred adoption of EHRs among medical institutions and professionals, it also had the effect of dramatically increasing the overall size of the EHR market and the number of healthcare IT vendors. The global EHR market, approximately 50% of which is represented by the U.S., grew from approximately $10B in 2010 to $22B today. The ambulatory segment increased from about $1.5B to $4B over the same period.

In 2009 less than 96 EHR vendors operated in the U.S., today that number is estimated at just north of 1,000. This rapid growth (~30% 9-year CAGR) resulted in a fragmented vendor base – ranging from relative behemoths such as Cerner and Epic, which combined are estimated to command nearly 50% market share of the hospital EHR market, to many hundreds of much smaller players vying for single-digit percentage share of the ambulatory space.

There are two distinct segments of the EHR market; hospitals and ambulatory. Hospitals, particularly larger facilities, may employ both an in-house as well as an ambulatory EHR system. The ambulatory segment is also quite diverse and includes outpatient hospitals and medical facilities as well as large and small physician practices. The ambulatory physician practice market is further segmented by size (i.e. number of physicians). KLAS, a healthcare IT research company which publishes data and rankings on EHR vendors, categorizes the ambulatory physician practice segment into large (>75 physicians), medium (11-75 physicians) and small (<10 physicians). While more than 95% of MTBC's customers fall into the ambulatory 'small' category, in November 2017 the company brought on a 950-clinician practice – which is their largest to-date in terms of both size and monthly revenue.

MTBC services the ambulatory segment of the EHR market. The chart below is ONC's data of ambulatory EHR vendors (that were participating in the EHR incentive program as of July 2017) and illustrates the large size (in terms of number of participants), diversity and fragmented nature of the market. MTBC is included in this chart as one of the 618 'other commercial vendors' providing health IT to, in aggregate, almost 94k ambulatory professionals attesting to meaningful use as of 2016. MTBC, per ONC's accompanying data, served 154 'certified' providers as of 2016 (note that we only illustrate this for context as this number relates only to 'certified technology' customers, which is significantly less than the number of customers that MTBC provides medical billing services to).

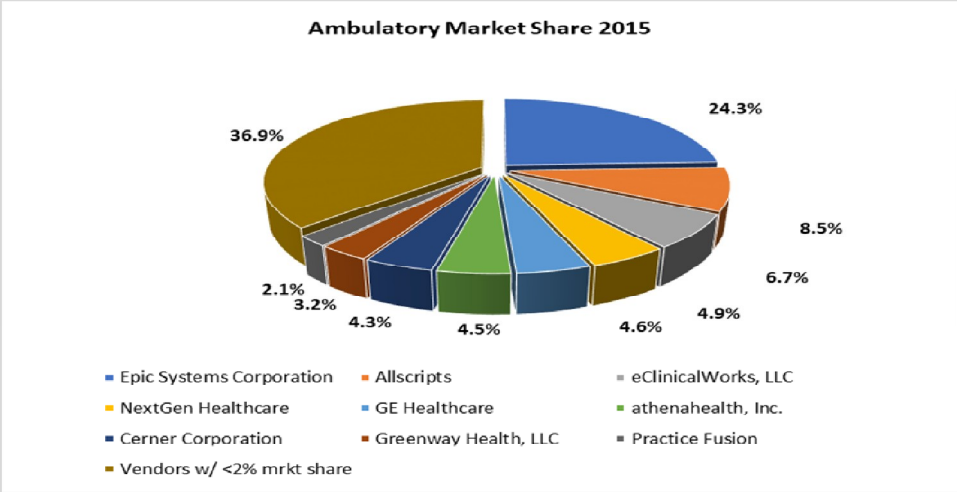


SOURCE: ONC, Health IT Dashboard

With adoption-related meaningful use incentives now largely a thing of the past and MACRA-mandates focused on value-based care, small providers' EHR-related priorities have shifted. Competitiveness in MTBC's target market segment is largely measured by an EHR vendor being able to sufficiently satisfy the needs and desires of small physician practices (at an acceptable cost), requirements which are often much different than those of hospital customers. For example, hospitals look to their EHR for relatively advanced functionality such as interoperability, networking, bundled reimbursement, custom reporting and population health analytics (in addition to more basic

functionality) while small ambulatory practices are likely to be satisfied with a (a more basic) EHR system that addresses different concerns such as; affordability, customer support/service, ease-of-use, regulatory compliance, reimbursement and billing.

Ambulatory Vendors: Goliaths vs. 'Others'
Of the almost 700 vendors that provide certified EHR technology to the ambulatory segment, just six account for over 50% share of the market (based on number of physicians). While some of the larger EHR vendors serve across the ambulatory size spectrum (from small to large physician practices), in general, the larger EHR vendors (most of which also serve the hospital segment) focus mostly on larger ambulatory practices and the ambulatory needs of hospitals (many of which will also have an inhouse system) while much of the small physician practices are served by vendors in the "other commercial" category. The reasons are intuitive – larger practices have larger budgets and may desire more functionality than their smaller counterparts.



While Epic Systems holds nearly 25% share of the ambulatory EHR market (based on 2015 EHR certification), aggregate market share of the more than 600 vendors with less than 2% market share of the ambulatory is almost 37%. This illustrates the top-heavy nature of the ambulatory EHR vendor market. The fragmented nature of the market, inability of many of the smaller vendors to evolve their technology with MACRA/MIPS requirements and growing demands from providers has resulted a weeding-out of some of the smaller EHR players. This has resulted in recent vendor consolidation, with (mostly) larger vendors scooping up less-viable smaller players. While the market remains fragmented, consolidation has (slightly) trimmed the ambulatory EHR vendor base from almost 800 in 2014 to less than 700 as of July 2017.

Big Vendors Acquiring Small Vendors…
A recent report[2] revealed that when it comes to attributes of EHR systems, small ambulatory physician practices are mostly concerned with customer support, user-friendliness and functionality that meets current and evolving regulatory mandates, that provides accurate billing and allows them to effectively care for their patients – all at a cost-effective price.

According to recent reports by Frost & Sullivan and P&S Market Research, EHR solutions for small-to-medium sized physician practices are expected to experience the fastest growth in the ambulatory segment as these providers look to EHRs as a way to improve profitability, address EHR optimization agendas and tackle reimbursement-related changes and complexity. This has fueled a greater shift towards cloud-based systems, which are generally more affordable than installed EHRs, and prompted greater attention from EHR Goliaths. An example of this was Allscripts' January 2018 acquisition of Practice Fusion, a free cloud-based EHR that is popular with small physician practices. With an estimated 30k ambulatory sites (and ~100k physicians) which serve ~5M patients per month, the acquisition afforded Allscripts solid entry into this relatively high-growth segment.

According to a recent report by healthcare IT consulting firm H.I.S. Professionals[3], larger vendors' acquisition-related strategy has been to buy smaller vendors, purge their most expensive (and experienced) personnel and then sell the acquired client base their (i.e. the acquirers') products via a strong sales and marketing approach.

[2] HIT Consultant.net: KLAS Report: Cerner & athenahealth Stumbling in Small Practice Ambulatory EMR/PM Market
[3] Vince Cottie, Elise Ames. H.I.T. Professionals LLC. *Physician Practice Vendor Review*. 2017

While this strategy may be paying initial dividends to the acquirers in the form of quick bolt-on revenue and (at least some level of) cost synergies, providers - particularly smaller practices that place high value on customer service and affordability – may be on the losing end of this trend.

Widespread Physician Dissatisfaction of EHR…

The theme that there may be somewhat of a disconnect between small practices' desires and larger vendors' offerings appears to be supported by the results of a recent KLAS[4] survey of more than 600 small physician practices. The report cited athenahealth, Cerner and Allscripts (all top 7 vendors) as having one or more problems related to customer service, technical support, usability and pricing. Fueled by providers' dissatisfaction, a separate KLAS report indicated that EHR vendor churn could increase – noting that 27% of medical practices were planning to replace their current EHR system and another 12% would, if it were not for financial constraints.

The KLAS survey may actually understate the extent of physicians' dissatisfaction, however. Healthcare IT research firm Reaction Data, recently conducted a survey of users of the top ten EHR vendors, asking them to rate their satisfaction with their EHR system. On a scale of 1-10, Reaction Data categorized scores of 7-10 as users being 'advocates' of their EHR vendor and scores of 5-6 as users being 'fence sitters'. By default, scores under 5 can de considered dissatisfied. Results, in the table below, further confirm high rates of dissatisfaction of ambulatory EHR users including that, on average, over 60% (i.e. 'fence-sitters' and 'dissatisfied' users, combined) would likely not recommend their EHR vendor.

	Percentage of Ambulatory Users That Are:		
	Advocates (score 7-10)	Fence-sitters (score 5-6)	Dissatisifed (score < 5)
Allscripts	18%	13%	69%
athenahealth	50%	18%	32%
Cerner	19%	12%	69%
eClinicalWorks	53%	29%	18%
Epic	41%	21%	38%
GE Healthcare	47%	27%	26%
Greenway	16%	42%	42%
Meditech	40%	20%	40%
NextGen	25%	30%	45%
Practice Fusion	70%	5%	25%
Average	**38%**	**22%**	**40%**

Data source: Reaction Data

While there is no shortage of evidence of physicians' displeasure with EHR, results of a recent large survey by the Mayo Foundation may provide the clearest insight into some of the potential consequences. The survey[5], of almost 7k physicians across all specialties, found that physicians' dissatisfaction with EHRs is so extreme that it is an independent predictor in driving doctors to leave the profession. The authors note that this has the potential to worsen the expected shortage of U.S. physicians.

Lack of ROI Fuels Widespread Dissatisfaction of RCM Providers…

Healthcare practices' dissatisfaction is not just contained to EHR. According to recent surveys by Black Book, medical providers have not only been highly discontented with the services and results provided by RCM vendors, but this displeasure has become increasingly widespread. Black Book reported that, as of Q4 2015, 79% of surveyed healthcare practice CFOs expected to discontinue relationships (within a few months) with RCM vendors that had not generated a positive return on investment. But, by Q3 2016, that figure had risen to 93% of CFOs which had expected to do the same.

Providers' concerns, as explained by Black Book's Doug Brown, are that "[a]s reimbursements come under pressure and costs keep rising, provider CFOs will face unparalleled pressure over the next year to preserve financial solvency, increase productivities in care delivery, implement regulatory mandates and reduce RCM expenses associated with getting paid."

The surveys further indicate that while 94% of CFOs believe that better designed RCM processes could improve efficiencies and result in positive return on investment, almost one-half of the CFOs fear that budget constraints will prevent them from obtaining the RCM solutions necessary to make that happen.

[4] HIT Consultant.net: KLAS Report: *Cerner & athenahealth Stumbling in Small Practice Ambulatory EMR/PM Market*

[5] Sinsky CA, et al. *Professional Satisfaction and the Career Plans of US Physicians*. Mayo Clin Proc. 2017 Nov;92(11):1625-1635. doi: 10.1016/j.mayocp.2017.08.017. Epub 2017 Nov 1.

MTBC Leveraging Competitive Strengths To Capitalize On State of Ambulatory Market
MTBC's revenue model and growth strategy are aimed at capitalizing on the recent changes in, and current dynamics of, the ambulatory EHR market. MTBC's business and revenue model address small physician practices' EHR-related concerns surrounding cost, user-friendliness, reimbursement/coding and regulatory compliance. Unlike most EHR vendors, MTBC offers their EHR technology for free and then offers users the opportunity to upgrade to their revenue cycle management services. MTBC believes that their fees (typically 5% of collections plus small set-up fee, or 2.95% for users of talkEHR) are among the lowest in the industry.

MTBC's growth strategy, which is similarly focused on the desires of small physician practices, includes growth through;

- **Organic means**: MTBC has historically committed few resources towards internal growth strategies. This is evidenced by their almost insignificant sales and marketing expenses. But, with physician dissatisfaction and related EHR vendor churn showing no signs of dissipating, the company has begun implementing an organic growth plan aimed at opportunistically poaching competitor's clients by offering them a better customer experience. The main focus is to provide the products and services that physician practices desire at an affordable cost. Some of the key components include;
    - talkEHR: "make it much easier to use" was cited as the number one reason in a survey[6] by Reaction Data which asked ambulatory EHR users what their EHR vendor could do to retain them as customers. That's exactly what MTBC aims to do with talkEHR, their free ONC-certified proprietary ambulatory EHR solution which includes voice enabled-functionality to further improve upon user-friendliness and reduce time and effort of data input. MTBC offers talkEHR free of charge, including full data migration to their platform, to healthcare practices which are then offered the opportunity to upgrade to their (revenue generating RCM) services.
    - Mobile apps: mobile access is a functionality that is resonating with physicians and will likely soon be a 'must-have'. A survey[7] by the ONC (which queried individuals about their use of technology, including smartphones, for healthcare over the past 12 months) found that more than one-third of individuals used mobile apps (and/or other electronic means) to track healthcare charges, nearly 30% used texting for healthcare purposes and 40% or more scheduled doctor's appointments and filled out paperwork with the use of a mobile device and/or computer. MTBC has developed and continues to develop functionality via mobile apps (for iOS and Android) including 'Patient Health Records App', 'iCheckIn' (for patient check-in, personal information, insurance and payments), 'iRx' (prescription approvals and refills), 'Dictate' (dictate patient notes), 'iEHR' (complete EHR) and 'ICD 9-10 converter' (converts reimbursement coding from legacy to current).
    - RCM: while small physician practices may mostly view EHRs as a necessary evil (to avoid penalties), changes to and complexity of reimbursement and related coding means that billing and collections is time consuming and often costly if not done properly. The issue can be particularly problematic for primary care practices, which typically have a high volume of patients but relatively low per-patient billings. MTBC provides expertise in this at a relatively low cost (~5% of collections) and with better than industry average performance. Key to MTBC's ability to keep expenses (and thereby their fees) low is their use Pakistani labor, which MTBC estimates costs approximately 50% of that of comparable labor in India and approximately 10% of comparably experienced and educated labor in the U.S. Importantly, their Pakistani workforce (which includes all operational and IT-related functions) is highly educated and trained and customer-facing personnel speak fluent English.
    - Customization: MTBC's relatively inexpensive and capable Pakistan-based development team means that they have the ability to customize their EHR and RCM platforms to 'fit' the needs of different practices and do so cost-effectively. We think this has the potential to be a significant competitive advantage against RCM / EHR vendors with higher operating expenses. Given differing needs of different practices, customization capability can be potentially critical for winning business.
    - Practice Fusion: an estimated 100k clinicians across ~30k ambulatory practices which serve about 5M patients per month use technology from Practice Fusion, which, similar to MTBC, offered certified EHR for free (Practice Fusion sold ad-space as a way to fund the free version). The fact that it was free helped Practice Fusion achieve relatively high customer satisfaction scores (see table), although that could soon change. Just weeks after being acquired by Allscripts in early 2018, it was announced

[6] reactiondata.com. *Trends and Insights in Ambulatory EHR*. 2015
[7] ONC. Health IT Dashboard. *Individuals Use of Technology to Track Health Care Charges and Costs*. 2017

that Practice Fusion was doing away with free EHR and will instead charge users $100 per month. While not exorbitant, if recent history (of hospital EHR vendors' acquisitions of ambulatory EHR vendors) is a guide, customer experience may suffer in the event that Allscripts looks to further monetize their acquired customer base. Regardless, customer defections are a certainty and we expect MTBC will be waiting at the gate. Clearly MTBC views this as a major opportunity and they have made preparations to capitalize on it including bringing on Practice Fusion's founder and former CEO, Ryan Howard, as a special advisor to the company.

  - EnrollmentPlus: MTBC also offers clearinghouse and electronic data interchange (EDI) services, capabilities which optimize insurance companies' enrollment processes and track claims – capabilities which were obtained through their acquisition of SoftCare in July 2015. Clearinghouse and EDI services currently account for approximately 3% of MTBC's total revenue and are expected to grow from the recent launch of 'EnrollmentPlus, a software-as-a-service EDI service.
  - Sales/marketing: MTBC has indicated that they expect to build a more dedicated sales and marketing outreach effort including hiring additional personnel. Expect there to be more activity related to this throughout 2018

- **Partnerships**: MTBC's partnership-related strategy is really also part of the organic plan, although it is more reliant on third-party relationships and collaborations. Part of this focus will be leveraging existing relationship with other EHR vendors – for example, MTBC would provide RCM for clients of other EHRs.

- **Acquisitions**: MTBC's revenue has grown from $10.5M in 2013 to $31.8M in 2017. Most of this growth was the result of acquisitions (MTBC completed 16 acquisitions in the last five years). Following a game-plan of buying cheap and quickly moving the cost base to their Pakistani operations, their acquisition strategy has largely proven successful. Several of their acquisitions have been structured (so as to be almost fully de-risked) with little-to-no upfront payment and only back-end sales contingencies (i.e. % of sales of the acquired company through a specified future period). While others have required significant upfront cash, these were also priced at highly attractive (i.e. inexpensive) valuations. MediGain has been the most successful acquisition to-date, but could be soon eclipsed by Orion – which MTBC bought for $12.6M (just ~40% estimated revenue) in July 2018. MTBC has indicated that they expect to continue to be an opportunistic acquirer. Recent acquisitions include;

  - 2014 acquisitions (Omni Medical Billing, Practicare and CastleRock): three revenue cycle management companies' assets were acquired for $17.4M in July 2014. Within five months MTBC had migrated 72% of customers and retained 92% of acquired customers. Incremental revenue from these companies was $8.2M in 2014 (~5 months) and $12.4M in 2015. Adjusted EBITDA improved from ($1.7)M in 2014 to ($675)k in 2015
  - 2016 acquisitions: acquired assets of four companies, including MediGain, MTBC's largest acquisition to-date. Terms of two of the three acquisitions included no significant upfront payment (and modest back-end contingencies). MediGain, a medical billing company, was in financial distress when acquired by MTBC in September 2016 for $7M. While operating expenses increased immediately after the acquisition, the assets were quickly integrated, costs were cut and MediGain generated incremental revenue to MTBC of $13.6M in 2017. Contribution from MediGain was also a major component of MTBC's significantly improved financial results: revenue grew 30% ($24.5M in 2016 to $31.8M in 2017), operating loss fell by $3.4M ($7.9M to $4.5M) adjusted EBITDA improved by $2.9M and ended the year in the black at $2.3M and MTBC even generated $282k of cash from operations (compared to $889k used by operations in 2016). MTBC bought MediGain for (what would prove to be) just of 50% of forward revenue. Much of the success of this acquisition was credited to the quick integration and ability to minimize customer and revenue attrition through providing a better customer experience (i.e. MTBC was able to quickly improve billing processes and collections which helped stem defections)
  - 2017: Washington Medical Billing acquired with just $205k upfront plus contingencies on Washington's revenue for the first three years.
  - 2018 Orion HealthCorp: In July 2018 MTBC paid $12.6M for the core operating assets of Orion HealthCorp – which, based on management's revenue guidance, implies a purchase price of just ~40% of annualized revenue. Orion is expected to approximately double MTBC's annualized revenue and more than double adjusted EBITDA. Along with 300 U.S.-based employees with offices in 10 states, Orion brings RCM-related accounts and expands MTBC's capabilities to include long-term practice management services and a vaccine group purchasing organization. These bolt-on capabilities not only bring immediate incremental revenue and operating margin (as both the PM and

GPO businesses are already profitable) but also opportunity to add-value via cross-selling to MTBC's current customer base. In addition, Orion accelerates MTBC's penetration into the hospital segment. We also think that (what appears to be much) greater revenue generating efficiency of Orion's RCM business (as compared to MTBC's legacy), could prove to be a substantial catalyst towards accelerating growth in profitability and adjusted EBITDA – particularly as MTBC realizes greater synergistic cost savings.

Valuation

MTBC was able to immediately shed costs of legacy-Orion as they were not required to assume certain commitments, such facility and equipment leases. MTBC has also been quick to integrate operations, noting on recent calls that they have already transitioned offshore back-office RCM-related work from Orion's vendors to their own employees – and in the process shed ~70% of the related costs. In addition, all customers that had been using Orion's software have been transferred to MTBCs. Additional integration and related cost savings are anticipated over the coming quarters – and expected to further improve upon profitability and EBITDA.

We now assume proportional segment-level contribution to total revenue is RCM ~79%, PM 19% and GPO 2%. We also think that we may have been underestimating the extent and benefits of cost-cutting, efficiencies and synergies of combining Orion's RCM with that of legacy MTBC's. The most recent updates to our model (i.e. following reporting of Q4'18 results), include our updated assumptions in that regard.

While the 2019 guidance does not assume any meaningful acquisitions, it is clear that management remains on the look-out for another Orion or MediGain-type transaction. They exited 2018 with $14.5M in cash and $10M available under their untapped credit facility. Couple with the fact that MTBC is now generating consistent positive cash flow, they have the resources to do another sizeable deal. And, as we have noted in the past, given their ability identify undervalued assets and to quickly integrate (and cut costs) without significant disruption to their ongoing operations or to those of the acquired company, a near-term transaction could result in upside to their current guidance.

As always, our model should be considered fluid, particularly given the potential for near-term acquisitions and Orion-related integration tweaks. We base our valuation on the average of implied EV/EBITDA and P/S multiples from analysts' estimates of publicly traded EHR / RCM companies and providers of related technology and services. Based on a fully diluted share count of approximately 14M, **our calculated fair value has moved from $9.5/share to $11.0/share (currently).**

	P/S		EV/EBITDA	EV/EBITDA	
	2019	2020	2019	2020	
Comparable Multiples	2.3x	2.1x	26.1x	20.4x	**Average**
MTBC Per Share Value	$10.5	$10.5	$10.8	$11.7	**$10.9**

Financial Model

MTBC	Q1A	Q2A	Q3A	Q4A	2018 A	Q1E	Q2E	Q3E	Q4E	2019 E
RCM Total	$8,307.3	$8,682.9	$13,252.9	$13,146.7	$43,389.9	$12,241.0	$12,768.1	$12,565.6	$13,223.1	$50,797.82
% of total revenue	100.0%	100.0%	77.8%	79.6%	85.8%	80.0%	79.9%	77.1%	80.0%	79.2%
yoy growth	1.1%	11.5%	76.4%	58.5%	36.4%	47.4%	47.0%	-5.2%	0.6%	17.1%
Practice mgmt Total	$0.0	$0.0	$3,314.4	$3,186.7	$6,501.1	$2,896.0	$3,022.0	$3,247.5	$3,123.4	$12,288.9
% of total revenue	0.0%	0.0%	19.4%	19.3%	12.9%	18.9%	18.9%	19.9%	18.9%	19.2%
yoy growth	-	-	-	-	-	-	-	-2.0%	-2.0%	89.0%
GPO Total	$0.0	$0.0	$477.2	$177.6	$654.8	$162.5	$181.6	$488.9	$184.2	$1,017.2
% of total revenue	0.0%	0.0%	2.8%	1.1%	1.3%	1.1%	1.1%	3.0%	1.1%	1.6%
yoy growth	-	-	-	-	-	-	-	2.5%	3.7%	55.3%
MTBC Total Revenue	$8,307.3	$8,682.9	$7,646.2	$8,111.0	$32,747.4	-	-	-	-	-
% of total revenue	100.0%	100.0%	44.9%	49.1%	64.8%	-	-	-	-	-
yoy growth	1.1%	11.5%	1.8%	-2.2%	2.9%	-	-	-	-	-
Orion Total Revenue	$0.0	$0.0	$9,398.4	$8,400.0	$17,798.4	-	-	-	-	-
% of total revenue	-	-	-	-	-	-	-	-	-	-
yoy growth	-	-	-	-	-	-	-	-	-	-
Total Revenue	**$8,307.3**	**$8,682.9**	**$17,044.5**	**$16,511.0**	**$50,545.8**	**$15,299.5**	**$15,971.7**	**$16,302.0**	**$16,530.7**	**$64,103.9**
YOY Growth	1.1%	11.5%	126.8%	99.1%	58.9%	84.2%	83.9%	-4.4%	0.1%	26.8%
Direct operating costs	$4,484.1	$4,333.6	$12,123.9	$10,311.0	$31,252.6	$9,960.0	$9,519.1	$9,324.7	$8,926.6	$37,730.4
% direct op costs	54.0%	49.9%	71.1%	62.4%	95.4%	65.1%	59.6%	57.2%	54.0%	58.9%
Selling & mktg	$305.0	$403.1	$461.5	$442.4	$1,612.0	$443.7	$431.2	$456.5	$462.9	$1,794.2
% S&M	3.7%	4.6%	2.7%	2.7%	4.9%	2.9%	2.7%	2.8%	2.8%	2.8%
General & admin	$2,600.7	$3,054.2	$5,131.3	$5,478.3	$16,264.5	$4,872.9	$5,126.9	$5,151.4	$5,355.9	$20,507.2
% G&A	31.3%	35.2%	30.1%	33.2%	49.7%	31.9%	32.1%	31.6%	32.4%	32.0%
R&D	$255.9	$248.9	$263.7	$261.0	$1,029.5	$275.4	$271.5	$260.8	$264.5	$1,072.2
%R&D	3.1%	2.9%	1.5%	1.6%	3.1%	1.8%	1.7%	1.6%	1.6%	1.7%
Change in contingent consideration	$31.7	$11.0	$25.5	$5.0	$73.2	$0.0	$0.0	$0.0	$0.0	$0.0
Depreciation & amort	$590.8	$559.7	$822.1	$881.2	$2,853.8	$775.0	$716.6	$597.2	$519.7	$2,608.5
Restructuring charges	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
TOTAL OpEx	$8,268.2	$8,610.5	$18,828.0	$17,378.9	$53,085.6	$16,326.9	$16,065.4	$15,790.7	$15,529.6	$63,712.6
% Total OpEx	99.5%	99.2%	110.5%	105.3%	105.0%	106.7%	100.6%	96.9%	93.9%	99.4%
Operating Income	**$39.1**	**$72.5**	**($1,783.5)**	**($867.9)**	**($2,539.8)**	**($1,027.4)**	**($93.7)**	**$511.3**	**$1,001.1**	**$391.3**
Operating Margin	0.5%	0.8%	-10.5%	-5.3%	-5.0%	-6.7%	-0.6%	3.1%	6.1%	0.6%
Total Other Income (Expense)	$82.6	$174.4	($299.0)	$286.2	$244.0	($70.0)	($2.0)	($48.0)	($44.0)	($164.0)
Pre-Tax Income	**$121.7**	**$246.8**	**($2,082.5)**	**($581.8)**	**($2,295.8)**	**($1,097.4)**	**($95.7)**	**$463.3**	**$957.1**	**$227.3**
Tax expense (benefit)	$46.7	$51.5	($250.1)	($5.5)	($157.4)	$0.0	$0.0	$0.0	$0.0	$0.0
Tax Rate	38.3%	20.9%	12.0%	0.9%	6.9%	-	-	-	-	10.8%
Preferred dividends	$775.3	$1,248.7	$1,056.2	$1,743.7	$4,824.0	$1,486.0	$1,486.0	$1,486.0	$1,486.0	$5,944.0
Net Income (to common SH)	**($700.3)**	**($1,053.4)**	**($2,888.7)**	**($2,320.0)**	**($6,962.4)**	**($2,583.4)**	**($1,581.7)**	**($1,022.7)**	**($528.9)**	**($5,716.7**
YOY Growth	-75.9%	-50.4%	76.9%	149.6%	-8.3%	268.9%	50.1%	-64.6%	-77.2%	-17.9%
Net Margin	-8.4%	-261.4%	-16.9%	-14.1%	-13.8%	-16.9%	-9.9%	-6.3%	-3.2%	-8.9%
EPS (GAAP)	**($0.06)**	**($0.09)**	**($0.25)**	**($0.20)**	**($0.59)**	**($0.22)**	**($0.13)**	**($0.08)**	**($0.04)**	**($0.47)**
YOY Growth	-78.9%	-53.9%	72.6%	143.6%	-13.9%	256.9%	44.8%	-65.7%	-77.9%	-20.5%

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Shares O/S	11,617	11,665	11,770	11,833	11,721	12,008	12,100	12,140	12,200	12,112

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