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Zacks Small-Cap Research

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MTBC, Inc. (MTBC-NASDAQ)

Q3 Results: ETM Upside, Integration Synergies Drive Record Profitability. Revenue, EBITDA Guidance Are Achievable

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 $11.25/share

Current Price (11/20/19)	$3.94
Valuation	**$11.25**

OUTLOOK

Adjusted EBITDA was $2.6M in Q3, a new quarterly high, up 200% from $865k in Q3'18, up 128% from $1.1M in Q2'19 and about 20% higher than our $2.2M estimate. The outsized increase in adjusted EBITDA is the product of near-record revenue (second only to Q3'18) coupled with the continuance of synergistic expense reduction from the rapid integration of MTBC's recent acquisitions (including Etransmedia which closed on April 1st), which is reflected in the $2.5M yoy decrease in operating expenses and resulted in record operating income of $669k.

Management reiterated their previously issued FY2019 revenue and adjusted EBITDA guidance of $63M-$65M and $8M-$10M, respectively. Through the first nine months, revenue and adjusted EBITDA were $48.7M and $5.3M - or approximately 77% and 66% of the low-ends of the respective forecasts. This guidance assumes organic growth from existing and new clients. While (per our Q2 update) we had been less certain that MTBC would achieve the low-end of their adjusted EBITDA guidance, the greater-than-expected decrease in OpEx and $424k beat on adjusted EBITDA in Q3 now has us much more confident that this is achievable.

SUMMARY DATA

52-Week High	**$5.49**
52-Week Low	**$3.25**
One-Year Return (%)	**-18.41**
Beta	**1.71**
Average Daily Volume (sh)	**330,264**
Shares Outstanding (mil)	**12**
Market Capitalization ($mil)	**$48**
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 (%)	**25.6**
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-Value**
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	15.1 A	16.8 A	16.9 A	15.9 E	64.5 E
2020					68.5 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	-$0.15 A	-$0.19 A	-$0.14 A	-$0.08 E	-$0.56 E
2020					-$0.12 E

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

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Q3 2019 Results:
MTBC reported financial results for their third quarter 2019 and provided a business update. **Revenue was down 1% yoy, up 1% qoq and about 6% better than our estimate.** While our revenue estimates for both (what we refer to as) MTBC's legacy business and that related to Orion appear to be almost dead-on with the respective actuals (calculation of 'actuals' require some interpolation), our Etransmedia estimate missed by about $850k (or ~50% of the $1.7M actual).

Revenue fell significantly less (yoy) than we had anticipated as better than expected client retention from Etransmedia helped offset what we estimate was a ~$2.0M (or 21%) dip in Orion related revenue. The drop in Orion sales was largely expected as catch-up collections that benefitted and resulted in record revenue in Q3'18 (i.e. period the acquisition closed) did not repeat in the most recent quarter. We note, however that while we had expected Orion RCM-related revenue to fall yoy, the actual decrease was about $500k, or 20%, greater than what we were anticipating (although this was completely offset by higher than estimated Orion-related practice management revenue). Meanwhile, (per our calculations) MTBC legacy revenue ticked up by about 1% from the prior year.

Adjusted EBITDA was $2.6M in Q3, a new quarterly high, up 200% from $865k in Q3'18, up 128% from $1.1M in Q2'19 and about 20% higher than our $2.2M estimate. The outsized increase in adjusted EBITDA is the product of near-record revenue (second only to Q3'18) coupled with the continuance of synergistic expense reduction from the rapid integration of MTBC's recent acquisitions (including Etransmedia which closed on April 1st), which is reflected in the $2.5M yoy decrease in operating expenses and resulted in record operating income of $669k.

Management reiterated their previously issued FY2019 revenue and adjusted EBITDA guidance of $63M-$65M and $8M-$10M, respectively. Through the first nine months, revenue and adjusted EBITDA were $48.7M and $5.3M - or approximately 77% and 66% of the low-ends of the respective forecasts. This guidance assumes organic growth from existing and new clients. While (per our Q2 update) we had been less certain that MTBC would achieve the low-end of their adjusted EBITDA guidance, the greater-than-expected decrease in OpEx and $424k beat on adjusted EBITDA in Q3 now has us much more confident that this is achievable.

MTBC also remains very much on the hunt for **additional acquisitions** and indicated on the call that a recent acceleration in the number of leads has the potential to increase the likelihood that a deal is consummated. But while additional bolt-on and tuck-in acquisitions likely continues to represent the most opportune way to significantly steepen the near-term growth curves (on both the top and bottom lines), the company has recently begun to **layer on additional organic growth initiatives**. As we have repeated in the past, MTBC has shown an adeptness at finding, quickly integrating and profitably leveraging synergies of attractive acquisition targets – this strategy has been responsible for virtually all of their recent growth and improved financial performance (and financial position).

Unfortunately, the Street does not necessarily appreciate (and value) growth by acquisition as it might growth by organic means. Organic growth is also generally more predictable and typically not exposed to the same level of binary risk that a pure acquisition growth strategy might have. As such, we are encouraged to see that MTBC appears to have **re-energized and broadened the size and scope of their organic growth strategy** which, if successful, could provide the dual benefits of a lower equity risk premium and incremental profitability.

As part of this organic growth initiative, the company recently added marketing personnel, began rolling out new offerings and, to further incentivize sales productivity, tweaked customer-facing personnel compensation (i.e. bonus) structures. MTBC's new partnership offering is one of their most significant recent strategic initiatives aimed at growth via leverage of their existing capabilities.

Q4 may also see some incremental initial contribution from **MTBC's new partnership offering**, which launched earlier this quarter and provides an additional revenue opportunity via (what amounts to) outsourcing the company's technology and / or human capital to smaller (i.e. too small to be attractive acquisition candidates) RCM companies. Management noted that they signed their first 'partnership' (RCM) customer in October and that they are in discussions with others. We will be eager to hear updates regarding customer interest in this offering as well as the relative financial contribution from these arrangements.

Telemedicine functionality is the most recent major enhancement to MTBC's technology platform. Management noted on the call that their telemedicine solution has already undergone beta testing and is expected to begin a formal roll-out to existing accounts in Q4. Of 500 current clients that the company put out feelers to, approximately

one-third indicated that they had interest in the telemedicine functionality. We expect we will here status updates as the launch gets underway.

Q3 Financials
Revenue, at $16.9M was down 1% yoy, up 1% from Q2'18 and $946k higher than our estimate. We estimate that Orion-related assets contributed approximately $7.4M (44% of total) of revenue including $3.2M (19% of total) from RCM, $3.9M (23% of total) from practice management and $296k (2% of total) from the GPO. Etransmedia-related assets contributed approximately $1.7M (10% of total), almost all of which relates to RCM (ETM contributed minimally to PM as well). MTBC legacy assets contributed the remaining $7.8M (46%), all of which we have rolling up to RCM.

Breaking out the $946k beat to our total revenue estimate into each of the three major operating segments in our model (RCM, PM and GPO) shows we underestimated RCM revenue by $431k (3%) – which relates to a combination of better-than-anticipated ETM client retention and slight overperformance (+1.0% vs our respective estimate) of legacy MTBC RCM, underestimated practice management revenue by $665K (17%) and overestimated group purchasing organization revenue by $149k (50%).

As it relates to our miss on PM revenue – that appears to be an unforced error as on our part and not consistent with our excel sheet notes. As a reminder, PM is typically seasonally stronger in Q3 benefitting from pre-back to school visits. As such, we expect to see a PM revenue decline sequentially into Q4 (which can experience seasonal softness as a result of the holiday season).

Q3 was the fifth full quarter with inclusion of Orion, the acquisition of which closed on July 1, 2018. Orion-related assets contributed approximately 44% and 46% of MTBC's total revenue in the three and nine months ending 9/30/19 (i.e. through Q3). MTBC legacy accounted for 46% and 47% of total revenue in the three and nine months through Q3'19 compared to 45% and 72% in the comparable prior year periods (note that Orion closed at the start of Q3'18).

Q3 was also the second full quarter with inclusion of Etransmedia Technology, MTBC's latest acquisition for which the company paid $1.6M and which closed on April 1st of this year. Etransmedia is a relatively small ("tuck in") deal for MTBC which is now largely integrated. More than 30% of ETM clients have been moved to MTBC's platform. While MTBC had initially anticipated that ETM would generate about $3.5M in revenue per year, a higher rate of client retention from that acquisition looks to potentially provide meaningful further upside (this is consistent with comments in our Q2 update where we noted that we thought ETM could outperform MTBC's $3.5M run-rate forecast). ETM contributed $2.0M and $1.7M in Q2 and Q3, respectively – while catch-up collections are included the Q2 number, Q3 revenue was nearly double what we had anticipated. So while the acquisition appears to have already proven its worth, barring significant client churn, we think ETM could end up being one of the company's biggest (small acquisition) wins.

Operating expenses continue to benefit from quick integration of the Orion and ETM acquisitions. Moving these clients to MTBC's own platform, eliminating operational redundancies and moving support functions to their overseas facilities (which, in many cases, had previously been performed by relatively very costly third parties) has resulted in significant decrease in operating expense and helped push **operating income to a record $669k** in Q3. Operating income improved by $2.5M and $1.9M in the year and quarter-earlier periods, respectively.

Direct operating expenses, which typically accounted for 60% - 65% of total OpEx, were $10.5M in Q3, or just 62.5% of total revenue – this is down 13% from Q3'18 ($12.1M, or 71.1% of total revenue) and 8% lower than Q2'19 ($11.4M, or 68.0% of total revenue). G&A, which is the second most significant operating expense (accounting for ~25% - 30% of total OpEx) also showed significant improvement, falling 13% on both yoy and qoq bases to $4.5M in Q3. As a percentage of revenue, G&A expense looks to have achieved a record low of 26.4%. For context of the relative improvement in G&A expense, this averaged 51%, 37% and 32% of total revenue in fiscal years 2016, 2017 and 2018, respectively.

Operating expenses are anticipated to decrease again going into Q4, albeit likely more modestly than the improvement from Q2 to Q3. While we think revenue falls about 6% sequentially to ~$15.9M in Q4, this should be more than offset by incremental cost savings associated with operating synergies and productivity gains.

Record Adjusted EBITDA
Adjusted EBITDA was $2.6M, a record high, up 200% from $865 in Q3'18 and up 128% from $865k in Q2'19. YTD adjusted EBITDA was $5.3M through Q3, up 56% from $3.4M in the prior year period. On a margin basis, adjusted EBITDA was 15.4% of total revenue in Q3'19 and 11.4% through the first nine months of the year.

Valuation
We note that while (per our Q2 update) we had been less certain that MTBC would achieve the low-end of their $8M - $10M full-year adjusted EBITDA guidance, the greater-than-expected decrease in OpEx and $424k beat on adjusted EBITDA in Q3 has re-boosted our confidence.

We now think both the revenue and adjusted EBITDA guidance are likely to be achieved. We now model full-year revenue of $64.5M (revised from $63.7M) and adjusted EBITDA of $8.2M (revised from $8.0M, with less confident outlook). Our current estimates imply adjusted EBITDA margin of 18.1% for Q4'19 and 12.7% for the full year 2019.

Our FY'20 revenue and adjusted EBITDA are now $68.5M and $11.3M, updated from $69.1M and $11.3M (i.e. unchanged). Our calculated fair value has moved up slightly, from $11.0/share to $11.25/share.

	P/S		EV/EBITDA	EV/EBITDA		
	2019	2020	2019	2020		
Comparable Multiples	2.0x	1.8x	17.7x	14.0x	**Average**	
MTBC Per Share Value	$10.4	$9.8	$12.4	$12.4	**$11.3**	

Financial Model

MTBC	Q1A	Q2A	Q3A	Q4A	2018 A	Q1A	Q2A	Q3A	Q4E	2019 E	2020 E
RCM Total	**$8,307.3**	**$8,682.9**	**$13,252.9**	**$13,146.7**	**$43,389.9**	**$11,919.7**	**$13,255.5**	**$12,642.2**	**$12,214.0**	**$50,031.42**	**$53,334.8**
% of total revenue	*100.0%*	*100.0%*	*77.8%*	*79.6%*	*85.8%*	*79.0%*	*79.1%*	*75.0%*	*77.1%*	*77.5%*	*77.9%*
yoy growth	*1.1%*	*11.5%*	*76.4%*	*58.5%*	*36.4%*	*43.5%*	*52.7%*	*-4.6%*	*-7.1%*	*15.3%*	*6.6%*
Practice mgmt Total	**$0.0**	**$0.0**	**$3,314.4**	**$3,186.7**	**$6,501.1**	**$2,960.5**	**$3,288.9**	**$3,913.3**	**$3,452.2**	**$13,614.9**	**$13,926.4**
% of total revenue	*0.0%*	*0.0%*	*19.4%*	*19.3%*	*12.9%*	*19.6%*	*19.6%*	*23.2%*	*21.8%*	*21.1%*	*20.3%*
yoy growth	-	-	-	-	-	-	-	*18.1%*	*8.3%*	*109.4%*	*2.3%*
GPO Total	**$0.0**	**$0.0**	**$477.2**	**$177.6**	**$654.8**	**$200.0**	**$205.1**	**$295.9**	**$182.7**	**$883.7**	**$1,207.4**
% of total revenue	*0.0%*	*0.0%*	*2.8%*	*1.1%*	*1.3%*	*1.3%*	*1.2%*	*1.8%*	*1.2%*	*1.4%*	*1.8%*
yoy growth	-	-	-	-	-	-	-	*-38.0%*	*2.9%*	*35.0%*	*36.6%*
MTBC Total Revenue	**$8,307.3**	**$8,682.9**	**$7,646.2**	**$8,111.0**	**$32,747.4**	**$7,419.7**	**$7,605.5**	**$7,751.2**	**$7,841.7**	**$30,618.1**	**$33,067.6**
% of total revenue	*100.0%*	*100.0%*	*44.9%*	*49.1%*	*64.8%*	*49.2%*	*45.4%*	*46.0%*	*49.5%*	*47.4%*	*48.3%*
yoy growth	*1.1%*	*11.5%*	*1.8%*	*-2.2%*	*2.9%*	*-10.7%*	*-12.4%*	*1.4%*	-	-	-
Etransmedia Total Revenue	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	$2,067.3	**$1,999.4**	**$1,700.0**	**$860.0**	**$4,559.4**	**$3,933.4**
% of total revenue	-	-	-	-	-	-	*11.9%*	*10.1%*	*5.4%*	*7.1%*	*5.7%*
yoy growth	-	-	-	-	-	-	-	-	-	-	-
Orion Total Revenue	**$0.0**	**$0.0**	**$9,398.4**	**$8,400.0**	**$17,798.4**	**$7,660.5**	**$7,144.6**	**$7,400.1**	**$7,147.2**	**$29,352.5**	**$31,467.6**
% of total revenue	-	-	*55.1%*	*50.9%*	-	*50.8%*	*42.7%*	*43.9%*	*45.1%*	*45.5%*	*46.0%*
yoy growth	-	-	-	-	-	-	-	*-21.3%*	-	-	-
Total Revenue	$8,307.3	$8,682.9	$17,044.5	$16,511.0	$50,545.8	$15,080.2	$16,749.5	$16,851.3	$15,848.9	$64,530.0	$68,468.6
YOY Growth	*1.1%*	*11.5%*	*126.8%*	*99.1%*	*58.9%*	*81.5%*	*92.9%*	*-1.1%*	*-4.0%*	*27.7%*	*6.1%*
Direct operating costs	$4,484.1	$4,333.6	$12,123.9	$10,311.0	$31,252.6	$9,847.5	$11,396.4	$10,535.6	$9,620.3	$41,399.9	$38,000.1
% direct op costs	*54.0%*	*49.9%*	*71.1%*	*62.4%*	*95.4%*	*65.3%*	*68.0%*	*62.5%*	*60.7%*	*64.2%*	*55.5%*
Selling & mktg	$305.0	$403.1	$461.5	$442.4	$1,612.0	$361.4	$382.6	$347.6	$348.7	$1,440.2	$1,711.7
% S&M	*3.7%*	*4.6%*	*2.7%*	*2.7%*	*4.9%*	*2.4%*	*2.3%*	*2.1%*	*2.2%*	*2.2%*	*2.5%*
General & admin	$2,600.7	$3,054.2	$5,131.3	$5,478.3	$16,264.5	$4,162.1	$5,143.8	$4,452.0	$4,202.3	$17,960.1	$21,088.3
% G&A	*31.3%*	*35.2%*	*30.1%*	*33.2%*	*32.2%*	*27.6%*	*30.7%*	*26.4%*	*26.5%*	*27.8%*	*30.8%*
R&D	$255.9	$248.9	$263.7	$261.0	$1,029.5	$254.6	$218.4	$175.8	$221.9	$870.7	$1,300.9
%R&D	*3.1%*	*2.9%*	*1.5%*	*1.6%*	*3.1%*	*1.7%*	*1.3%*	*1.0%*	*1.4%*	*1.3%*	*1.9%*
Change in contingent consideration	$31.7	$11.0	$25.5	$5.0	$73.2	($64.2)	$0.0	($279.6)	$0.0	($343.8)	$0.0
Depreciation & amort	$590.8	$559.7	$822.1	$881.2	$2,853.8	$756.7	$836.2	$814.2	$745.7	$3,152.8	$1,600.0
Restructuring charges	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$136.3	$0.0	$136.3	$0.0
TOTAL OpEx	**$8,268.2**	**$8,610.5**	**$18,828.0**	**$17,378.9**	**$53,085.6**	**$15,318.2**	**$17,977.3**	**$16,181.9**	**$15,138.9**	**$64,616.2**	**$63,701.0**
% Total OpEx	*99.5%*	*99.2%*	*110.5%*	*105.3%*	*105.0%*	*101.6%*	*107.3%*	*96.0%*	*95.5%*	*100.1%*	*93.0%*
Operating Income	$39.1	$72.5	($1,783.5)	($867.9)	($2,539.8)	($238.0)	($1,227.8)	$669.4	$710.1	($86.3)	$4,767.6
Operating Margin	*0.5%*	*0.8%*	*-10.5%*	*-5.3%*	*-5.0%*	*-1.6%*	*-7.3%*	*4.0%*	*4.5%*	*-0.1%*	*7.0%*
Total Other Income (Expense)	$82.6	$174.4	($299.0)	$286.2	$244.0	($98.2)	$512.2	($720.0)	($30.0)	($336.1)	$25.0
Pre-Tax Income	$121.7	$246.8	($2,082.5)	($581.8)	($2,295.8)	($336.2)	($715.6)	($50.6)	$680.1	($422.3)	$4,792.6
Tax expense (benefit)	$46.7	$51.5	($250.1)	($5.5)	($157.4)	($40.5)	$55.4	$87.0	$82.3	$184.1	$771.6
Tax Rate	*38.3%*	*20.9%*	*12.0%*	*0.9%*	*6.9%*	*12.1%*	*-7.7%*	*-172.0%*	*12.1%*	*10.8%*	*16.1%*
Preferred dividends	$775.3	$1,248.7	$1,056.2	$1,743.7	$4,824.0	$1,492.7	$1,486.7	$1,602.8	$1,611.1	$6,193.4	$5,912.5
Net Income (to common SH)	($700.3)	($1,053.4)	($2,888.7)	($2,320.0)	($6,962.4)	($1,788.4)	($2,257.7)	($1,740.4)	($1,013.4)	($6,799.8)	($1,891.5)
YOY Growth	*-75.9%*	*-50.4%*	*76.9%*	*149.6%*	*-8.3%*	*155.4%*	*114.3%*	*-39.8%*	*-56.3%*	*-2.3%*	*-72.2%*
Net Margin	*-8.4%*	*-261.4%*	*-16.9%*	*-14.1%*	*-13.8%*	*-11.9%*	*-13.5%*	*-10.3%*	*-6.4%*	*-10.5%*	*-2.8%*
EPS (GAAP)	($0.06)	($0.09)	($0.25)	($0.20)	($0.59)	($0.15)	($0.19)	($0.14)	($0.08)	($0.56)	($0.12)
YOY Growth	*-78.9%*	*-53.9%*	*72.6%*	*143.6%*	*-13.9%*	*148.3%*	*108.0%*	*-41.6%*	*-57.6%*	*-5.2%*	*-78.0%*
Shares O/S	11,617	11,665	11,770	11,833	11,721	11,946	12,022	12,146	12,200	12,079	15,300

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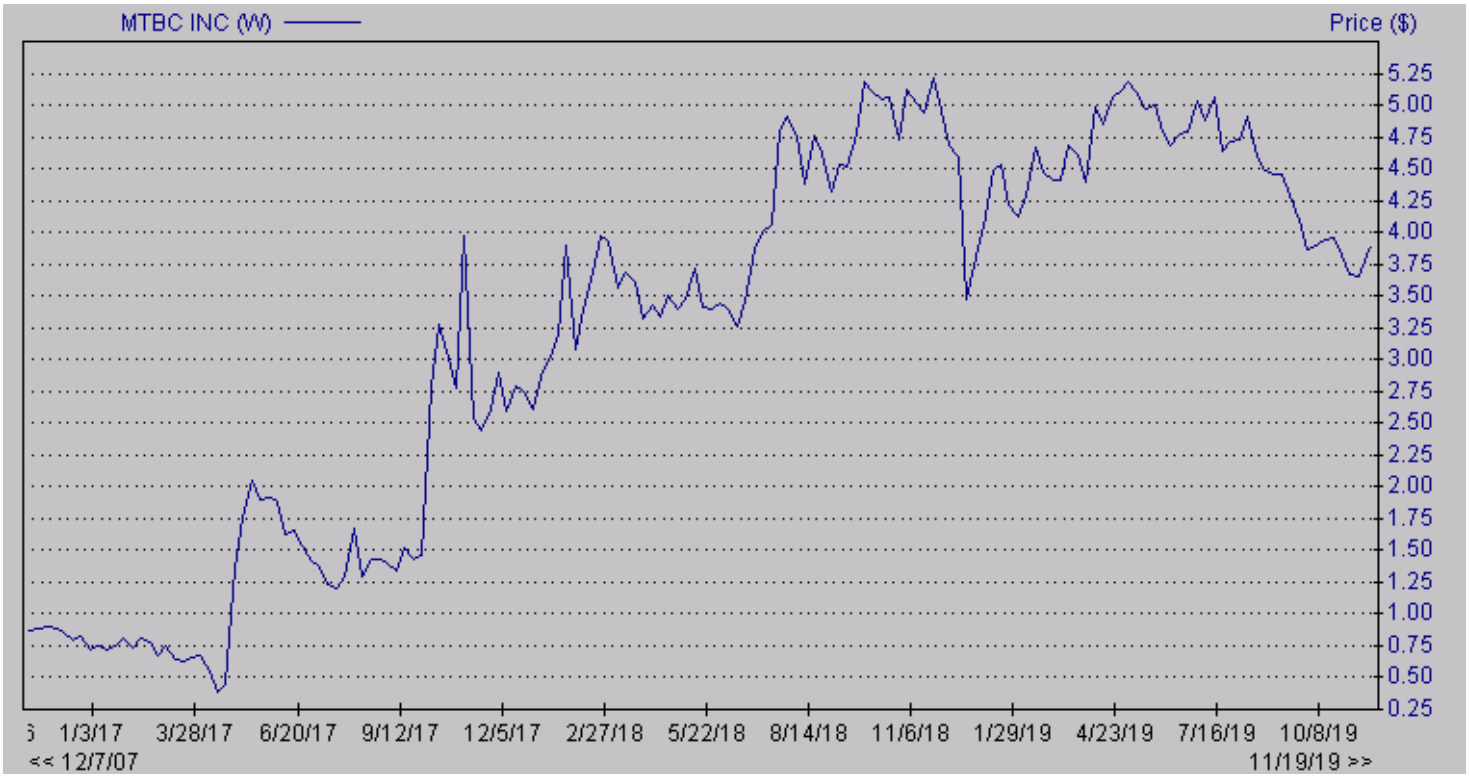

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