



OTC Markets Group Inc.

Fourth Quarter and Year-End 2015 Earnings Call

March 3, 2016

CORPORATE PARTICIPANTS

Dan Zinn, *General Counsel*

R. Cromwell Coulson, *Chief Executive Officer, President*

Bea Ordonez, *Chief Financial Officer*

PRESENTATION

Operator:

Greetings, and welcome to the OTC Markets Group Fourth Quarter and Year-End 2015 Earnings Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require Operator assistance during the conference, please press star, zero on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to Mr. Dan Zinn, General Counsel for OTC Markets. Thank you, Mr. Zinn; you may now begin.

Dan Zinn:

Thank you, Operator. Good morning and welcome to the OTC Markets Group Fourth Quarter and Year-End 2015 Conference Call. With me today are Cromwell Coulson, our President and Chief Executive Officer; and Bea Ordonez, our Chief Financial Officer.

Before we begin today's call, I would like to review the Safe Harbor statement. This conference call may contain forward-looking statements about the Company's future plans, expectations and objectives concerning, but not limited to, the Company's expected financial results for 2016. Words such as may, will, expect, intend, anticipate, plan, believe, could, and estimate, and variations of these words and similar expressions, are intended to identify forward-looking statements. These forward-looking statements are not historical facts and are subject to risks and uncertainties that could cause the actual results to differ materially from those predicted in these forward-looking statements.

These risks and uncertainties could include, but are not limited to, the risk factors described in the Risk Factor section of the Company's Annual Report for the year ended December 31, 2015. The Company does not intend and undertakes no obligation to update its forward-looking statements to reflect future events or circumstances.

With that, I'd like to turn the call over to Cromwell Coulson.

R. Cromwell Coulson:

Thank you, Dan. Good morning and thank you everyone for joining the call. I want to start with business and operational developments from the fourth quarter and full year of 2015, as well as opportunities and

challenges that lie ahead in 2016. Our CFO, Bea Ordonez, will then discuss the details of our financial results.

During 2015, we continued to concentrate on our mission: creating better-informed and more efficient financial markets. We fulfilled that mission by executing our strategy: to operate world leading securities markets; we share information widely through open networks that foster greater transparency; we connect broker-dealers; organize markets; and inform investors. We deliver elegant, reliable and cost-effective subscription-based solutions for a future that is online, data-driven, and social.

We focused on four main initiatives during 2015: reliability of our core systems, processes, and data with a focus on regulation FDI compliance; enhancing the corporate client experience on our OTCQX Best and OTCQB Venture Market; increasing the breadth and depth of securities traded on OTC Link ATS and of our market data; and finally, continuing to build out the strength of our Team to support future organic growth and opportunities, as well as create value for our clients.

So we're incredibly pleased to have achieved 100% uptime of our core OTC Link ATS systems during the trading hours throughout all of 2015 and into 2016. This was our top goal. You know, we needed to build trust with our clients and regulators. We had not achieved that in either 2014 or 2013, and it was a great achievement that was the result of hard work and collaboration across all of our Technology and Business Teams. This was a full Company push and we had a successful year. But uptime is only as good as your last month, so we are still focusing very highly on this going forward. You know, the larger our business becomes, the more we become part of our nation's financial infrastructure, the more critical it is that we deliver reliability and trust to the markets.

We also spent much of 2015 preparing for the SEC's regulation FDI—systems, compliance, and integrity. The new people, processes and procedures we have added will help strengthen our systems and foster trust with our regulators and our broker-dealer subscribers and investors.

Our challenge in 2016 will be adding elegant, reliable and cost-effective new features and functionality for our broker-dealer subscribers to our OTC Link ATS, while still building on our record of reliability. Last year was a lot of putting in process and strengthening our Team. Now, we want to move forward and keep innovating on our unique network-based broker-dealer market model.

We achieved great success with the first full year of our improved OTCQB Venture Market and saw our OTCQX Best Market grow as well. You know, we are building America's venture market, as well as a leadership position in global ADR and foreign ordinary share trading by giving innovative and entrepreneurial companies the public market they need today so they can grow for tomorrow.

Rapid growth in OTCQB corporate clients in the first half of 2015 gave way to more stable fluctuations in the second half of this year, as we assessed how to best support, improve, and grow this exciting market going forward. You know, it's really an early version of OTCQB. We know the target companies. We know what we're trying to build. We know a fair amount of the problems; we're trying to solve them. Some will take work with regulators, a lot will take work of how we can make the process more transparent, how we can provide better data for an online and data-driven world, how we can build the communities around it is—but OTCQB is an exciting new development and it's—and a real venture market has not existed in the US in an organized manner like this, targeted for these types of companies and really using transparency to risk and be priced efficiently.

During 2015, we also amended the OTCQX rules to strengthen financial standards, add a continuing penny stock prohibition, and introduced commonsense corporate governance standards already followed by the majority of OTCQX US companies. The new rules are in effect for new companies joining OTCQX in 2016 and will apply to all OTCQX companies beginning next year. These changes help further to

solidify OTCQX to the best market, for established companies with investable securities that can meet well-established regulatory financial standards and corporate governance practices.

We had 60 companies graduate for our markets to a New York Stock Exchange or a NASDAQ listing last year, maintaining our position as the global leader in exchange graduates with over 200 graduates in the last three years. This is important because the TFX Venture last year only had nine graduates; the AIM only had four. You know, last year was a very slow market for IPOs and—but we are a market that for companies that want to grow and want to eventually become exchange listed, we are a great place for Management to build out the infrastructure and build out the size of operations to support being on an exchange. But we're also, because our markets are tailored for smaller companies, not the S&P 500 with all the complexity and costs, there's lots of small companies and global companies that use our infrastructure to get the market they need today and they don't plan on going to exchanges. They just want a cost-effective public market that provides trading transparency and trust without too much complexity and pay.

As Congress and the SEC continue to discuss the role of venture markets in the US, we are actively participating in the discussion, educating lawmakers about the kind of changes that would benefit the companies on our markets, in areas like access to Reg A-plus and Reg Crowdfunding for SEC reporting companies. The JOBS Act had a lot of innovative rules, but SEC reporting companies kind of got left out of the new financings that work online. They were only allowed to do Title II online raisings of—to accredited investors. Title III and Title IV, they were left out of, which is completely ludicrous because these are the companies that have better disclosure that are required for that, and if we want to see the online financial portal industry, these companies already have the disclosure.

This is a big change is—you know Reg A is completely innovative because it allows companies to raise capital online. You know, if you think about, Amazon started a business model in the early 90s about wanting to use the Internet to sell things and we have not allowed companies to use the Internet to sell new securities until now. There is no—up until now there was no E-Trade or TD Ameritrade or Scottrade or Schwab online for selling new securities, and that needs to change.

Blue Sky preemption, you know, we need to work with—federally for federally regulated companies and also with the states for state regulated companies. You know, we need to come together and build out standards so there really is a uniform Securities Act. The world has changed a lot today. Broker-dealers have lots of compliance pieces. Blue Sky is too complicated, too costly for America's small companies. It needs to be streamlined with participation by all participants.

Finally, for the more established companies, the Fed needs to bring back the OTC margin lists. We have community banks on OTCQX which have left NASDAQ. They have the same market makers, they have the same share price, they have the same or more volume, is—but they've lost their margin eligibility because the Fed's not doing their OTC margin lists. They've got lazy when NASDAQ became an exchange. We need to change that because one way you make securities worth more is you make the ability to be lent against.

So, I mean, as I said about the future of financial markets is online, data-driven, and social, and we've just had a momentous event on our markets, which is on February 16 of this year, Elio Motors closed on a nearly \$17 million Regulation A-plus IPO with a participation of 6,000 investors through an online crowdfunding portal StartEngine, and on February 19, Elio Motors' shares began trading on our OTCQX market sponsored by the investment bank Hambrecht.

We, of course, are thrilled that Elio Motors chose to have its securities traded on our OTCQX market and that OTCQX is now a venue for the new generation of IPOs raising capital online. We're thankful that the pioneer, Paul Elio, chose our market for their public trading. We're excited to see what Paul Elio is doing, as well as the Team at StartEngine, Hambrecht, and everyone else around the community coalescing

around this brave new frontier of being able to raise capital online that is completely disruptive. We believe our markets, and particularly our top two markets, OTCQX and OTCQB, are tailor-made to become the venues of choice for the new generation of innovative and entrepreneurial crowdfunded offerings for three reasons: we offer better regulated markets with flexible listing standards to meet the needs of innovative companies and their investors; two, we offer an elegant, reliable, and cost-effective alternative. OTCQX is less than half the cost of NASDAQ's lowest tier, and OTCQB is less than a quarter. Our markets provide transparent and trusted public trading through online brokers and institutional brokers and they allow small companies with limited budgets and management resources to allocate their time and capital towards growing the company, rather than meeting complex and costly stock exchange listing requirements designed for S&P 500 companies.

Unlike a stock exchange—and finally, this point is really important—we operate a dealer market that electronically connects a diverse community of competing broker-dealers providing liquidity and execution services. Our network-based model helps foster liquidity in small-company shares by allowing our broker-dealer subscribers to provide more liquidity than what is displayed. We believe one of the problems with small-company markets was when NASDAQ, at the turn-of-the-century, decided, because they were losing their largest companies in New York Stock Exchange, to become a stock exchange. Two things happened: they made their listing standards for smaller companies more stringent and costly and complex, and they got rid of their dealer market model. They became a centralized exchange.

That's really good for companies that have a big natural resource of liquidity. It doesn't work for companies that need liquidity. You need dealers, supplying liquidity as a service. We're very lucky that we have built a market that has lots of competing broker-dealers and fits the ecosystem of investors coming through online brokers who want a high-quality, low-cost execution, and WYSIWYG pricing, which means What You See Is What You Get. That comes from the dealers and we have the leading electronic dealers and we have specialists across industries. It's very important.

We've discussed with Congress—it isn't possible in a stock exchange centralized matching engine that can only match anonymously, orders that are entered. You know, matching engines are fast and dumb. You get what you get and you don't get upset. Dealers can create liquidity as a service and we think part of it is a whole discussion—and we lost it when we had competition between organized OTC broker-dealer markets and the stock exchanges—is the need to facilitate dealer markets, and that's something that we are going to be out there for a long time. In companies that don't have liquidity, you need liquidity providers and you need competition, and you can't have an exchange deciding which liquidity provider you go to because the best part—if an online broker gets a bad execution from a liquidity provider, they can either get the price fixed for the customer's clients, is that their client is happy, or they stop sending order flow to that liquidity provider. That let's up—that's a market-driven solution and is very important.

Throughout 2015, we upgraded our OTC Link ATS messaging platform to handle higher volumes with lower latencies and it worked to upgrade subscribers to our new FIX (phon) Gateways. We are almost done with the FIX Gateway changeover and that is going to be very important because we're going to be able to move forward rapidly on new features and new functionalities. Again, this has been a big Team effort of everyone at OTC Markets and our clients, and we're very thankful as we move this forward while delivering the uptime that our subscribers and our regulators and investors are expecting. These changes position us well as we prepare to allow subscribers to quote Tier-2 NMS securities on OTC Link ATS in the coming months. Again, our broker-dealer network-based market is the ideal model to allow subscribers to offer robust liquidity and consistent execution quality for companies ranging from smaller US companies to second-tier ETFs and the largest cross-border traded ADRs.

You know, we want to build the market for proprietary liquidity providers, a transparent market where the consumer can choose the best execution provider based on their liquidity displayed and their track record, and this is a very different platform and it's targeting not the securities that trade a million times a

day. We want to target the securities that trade less than a million times a year, thus, less than 4,000 trades a day, which is—you know, there's 10s of seconds or minutes between trades in these securities.

Now, the recent overall market environment has been slower with lower trading velocity. We did not accomplish our goals in our Market Data business line in 2015. You know, part of that was because other priorities took precedence and our focus waivered. We need to be better marketers of our market data in 2016. Exciting companies, continued investor education, and the introduction of new securities onto our markets will broaden the appeal of our market data. New data products that help the future of online data-driven worlds is very important, and better distributor relations. All of these are things that we need to build on because we still only have penetration to approximately 8% of the professional market data users that NASDAQ UTP has. But, it is a challenge.

It is something we are going to be putting focus into figuring out how to better grow this year is the—and so Bea will go over the details of our financial performance, but I want to also recognize the outstanding efforts of the entire OTCM Team, particularly our Corporate Services Group in generating record revenues with an 18% increase in revenue during 2015. Our operating expenses also rose as a function of building a stronger Team and enhancements to our systems, and an operating margin was strong at 35%. These results are a testament to the hard work and dedication of our entire Team and they provide a platform for continued value creation going forward.

We're in this space for the long gain. We want to build an enduring competitive franchise that helps brokers connect, helps companies raise capital and value their shares, and finally, has the information so investors can make good decisions directly and build the ecosystem around it because you can't do anything; you need a community, and building our community, being a strong market focused on smaller companies, global companies, and companies that are not in the S&P 500, and the broker-dealers and broker-dealers of all sorts to help them be more efficient, and providing great data is a great position to be in and a way to continue to build a strong franchise.

I want to turn to some important Corporate developments. On February 24, our Board of Directors declared a quarterly dividend of \$0.14 per share payable in March. This is our 29th consecutive quarterly dividend and our third consecutive \$0.14 quarterly dividend. As we enter 2016, we are pleased with our strong operating results and cash position and we are optimistic about our ability to add new value to all of our subscriber bases this year.

You know, this quarter we became a market for IPOs and that's an incredible spot to be in because for companies, IPOs and being a public company on a national stock exchange is too complex, too costly, it's too painful. Over the next few years we want to fix that, and the ability for companies to go directly to investors, use today's online marketing instead of human-driven push to use technology-driven pull and targeting to raise capital is going to be completely disruptive. It's going to create a new wave of capital raising and new connections of communities, and we offer—we have built a cost-effective market for these companies that are good at interacting with their investors online with their data and having the social network supporting it.

Finally, I'm pleased to introduce our new CFO, Bea. We conducted a thorough search for the role and we are thrilled to have her on the Team. But before I turn the call over to Bea, I just want to thank the whole Team at OTC Markets for everything they accomplished this year. This has been the strongest Team we've had and we—and our platform, they've made our platform the strongest and they've made our product offering the strongest and—but what we've built is just an opportunity to become—completely change the ability of companies, whether it's the community bank around the corner, the global champion across the ocean, or an exciting and entrepreneurial three-wheel car company who wants to create low-cost, high-mileage cars so people can get to work.

Thank you. With that, I will turn the call over to Bea.

Bea Ordonez:

Thank you, Cromwell. So I'm excited to be here for this, my first earnings call, and I wanted to extend my thanks, first of all, to everyone at OTC Markets for extending such a warm welcome, and especially to the Finance Team for all their hard work over the last several weeks.

With that, onto the numbers. On a quarter-over-quarter basis, OTC Markets Group saw a 16% increase in gross revenues to \$13.1 million. Year-over-year, we've realized an 18% increase in gross revenues, closing out the full year with \$49.9 million in gross revenues. This compared to \$42.2 million in 2014. The increase, both on a quarter-over-quarter basis and on a year-over-year basis, was driven by significant growth in our Corporate Services business. That business line saw a \$7.6 million or 77% increase in revenues year-over-year on a quarter that translated to a \$2.1 million or 74% increase quarter-over-quarter.

These increases were largely a result of the growth in companies verified to trade on the OTCQB Venture Market. We ended 2015 with 942 companies on our Venture Market as compared to 311 companies at the end of 2014. We also continued to see growth in revenues from our OTCQX Best Market, both from a year-over-year basis, as well as on a quarter-over-quarter basis. We ended 2015 with 424 companies on our OTCQX Best Market. This compared to 377 companies at the end of 2014. That year-end count of 424 companies included 145 US companies, including 81 banks and 279 international companies. Over the course of 2015, we added 48 community and regional banks to the Best Market. The 424 companies trading on our OTCQX Best Market is the highest year in total since the inception of that market back in 2007.

This growth was partially offset for the quarter by a 10% decrease in OTC Link ATS revenue from \$3.2 million for the fourth quarter of 2014 to \$2.9 million for the fourth quarter of 2015. For the full year, our ATS revenue saw a 2% decrease from \$12 million in 2014 to \$11.8 million in 2015.

Effective on July 1, 2015, we made certain pricing changes affecting our Link ATS subscribers. We eliminated quote fees to subscribers quoting securities traded on our premium markets, and we increased fees for messaging. Both on a quarter-over-quarter and a year-over-year basis, this had the effect of reducing quote fee revenues while increasing message fee revenues.

For the full year, an updated fixed connection pricing schedule, new OTC dealer Internet connection charge, and increases in certain dealer license fees introduced in July 2014 further offset the loss of revenues related to quote fees. Within our OTC Link ATS business, the updated pricing structure discussed for quoting, messaging, and other services has caused a shift in revenues from quoting fees to messaging fees, but as can be seen, has not resulted in a material impact to total revenues on a year-over-year basis.

Market data revenues remain flat quarter-over-quarter at \$5.1 million. In the fourth quarter of 2015, a small increase in revenue from professional users was mostly offset by a similar decrease in the reported number of nonprofessional uses. On a full year basis, market data revenues showed a 1% increase over 2014 with \$20.6 million in revenues for 2015 versus \$20.3 million for the prior year. Revenues from professional user licenses saw a 2% increase in 2015.

Also in 2015, for the full year, we saw increased revenues from sales of our compliance data files to broker-dealer subscribers. These increases were partially offset by declines in advertising revenues, as well as by lower reported nonprofessional user licenses.

During the fourth quarter, operating expenses increased 13% to \$7.4 million. As in previous quarters this year, the increase was primarily due to an increase in compensation and benefit costs, which rose 17%

over the prior year quarter to \$4.3 million. This was largely a result of annual salary increases and increase in our headcount, as well as a higher bonus pool accrual in 2015 which reflected our improved results and performance over the course of the year.

In terms of expenses, a similar story when reviewing the year-over-year results, with operating expenses of \$30.7 million, up 14% over 2014. Again, the primary driver was the 20% increase in compensation costs when compared to the prior year. In addition to this—and this speaks to Cromwell's discussion around investment in our people and technology—our information technology and infrastructure costs increased by 13% to \$4.9 million on a year-over-year basis.

Falling (phon) from all of the above, our income from operations for the fourth quarter was \$5 million, an increase of 26% over the prior year quarter. For the full year, our operating income was \$16.9 million, up 31% from the prior year. Our operating margin for the full year was 35%, again, up from the 32% we realized in 2014.

Net income for the quarter increased 10% to \$2.9 million, primarily, of course, due to the increase in operating income, but partially offset by an increase in the expected tax rate. The drivers for that expected tax rate increase for the quarter was the timing of recognition of certain research and development tax credits which we took back in the fourth quarter of 2014.

On a full year basis, net income increased 30% from \$7.9 million in 2014 to \$10.3 million in 2015. The Company's effective tax rate for the full year was 39%, which was in line with the 2014 rate.

In addition to certain GAAP and other measures, Management utilizes the non-GAAP measure, Adjusted EBITDA, which excludes non-cash stock-based compensation expenses. Adjusted EBITDA increased 23% during the fourth quarter to \$5.8 million, or \$0.50 per adjusted diluted share. This was up from \$4.7 million and \$0.41 per share for the same period in 2014. For the full year, our Adjusted EBITDA was \$20.1 million, up 28% from \$15.7 million in 2014. You can find a reconciliation of our GAAP to non-GAAP results in our press release which is made available on our website.

Finally, we continue to produce solid growth in cash flows. Cash flows from operations for the full year amounted to \$17.1 million, up 37% versus 2014. We ended the year with \$23.9 million in cash on-hand, up 18% from the prior year balance. We continue and plan to continue to utilize our cash flows to grow our business organically through strategic investment in our people and technology, and to provide value to our shareholders through dividends and a share buyback. During 2015, we paid four quarterly dividends and one special dividend for a total of \$1.08, a 32% increase over the \$0.82 paid in the fiscal year 2014. Over the course of 2015, we also repurchased a total of 58,000 shares.

With that, I would like to thank everyone for their time and pass it back to the Operator to open up the line for questions.

Operator:

Thank you. We will now be conducting a question-and-answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two, if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment while we poll for questions.

Once again, ladies and gentlemen, please press star, one now if you would like to ask a question.

Okay. At this time, we have no questions. I would like to turn the conference back over to Mr. Coulson for any closing comments.

R. Cromwell Coulson:

Thank you. In wrapping up, this year has been a lot of work. I want to thank again our Team and OTC Markets; all of the companies that have become engaged to OTCQX and OTCQB to provide a better information experience to investors, and to build a better market going forward is—and a disruptive market; our broker-dealers who every day are competing for order flow to execute best trades, risking capital, serving clients and investors; and across the community, not just the market makers on our systems but all the online brokers who totally transformed trading and that—and then the future, all these exciting crowdfunding portals that are going to become the ibankers, you know, put an I in ibanking in the future so companies have access through the Internet to raise capital and sell new securities. All of these pieces of the community and our spot in the community to help make the public markets work better for smaller companies, entrepreneurial companies, innovative companies, and global companies, that's—you know, we're very thankful because we're a community-driven platform. So thank—and thank you everyone for calling in.

Operator:

Thank you. Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time and thank you for your participation.