

NewMarket Technology Inc. (NMKT)



PHILIP VERGES, Chairman and Chief Executive Officer of NewMarket Technology Inc., previously managed VTI from its inception. Mr. Verges is an experienced executive manager, with a track record in both telecommunications and high technology. Mr. Verges is a 1988 graduate of the United States Military Academy. His studies at West Point centered on national security. Accelerated for early promotion, Mr. Verges served with distinction as a U.S. Army Captain in a wide variety of important engagements, including research and development of counterterrorism communication technologies and practices. Mr. Verges' early career after the Army included time in the Computer Sciences Research and Development Department of General Motors as well as experience teaching

systems engineering methodology and programming to Electronic Data Systems (EDS) employees from 1991 to 1995. Mr. Verges' first business startup experience was at EDS in a new division concentrating on call center technology in financial institutions. Later in 1995, he added to his startup experience at a \$30 million technology services business with the responsibility to open a new geographic region with a greenfield operation. Mr. Verges founded VTI in 1997.

SECTOR: BUSINESS SERVICES

(ADT605) TWST: Would you begin with a brief historical sketch of NewMarket Technology Inc. and then bring us up to date on the company?

Mr. Verges: NewMarket is a company concentrated on evolving corporate high-tech research and development — research and development coming out of some of the incumbent technology providers such as Microsoft, Cisco and Sun. All of those companies depend on continuous research and development that provides new features and functions in their product lines from year to year. Certainly, if we were all using Windows 95 today, Microsoft might be having some corporate issues with ongoing revenue and continuous growth, so research and development is critical.

Research and development budgets traditionally come from earnings. Yet, earnings at incumbent technology companies are under pressure from the globalization of information technology, so there is less money available for research and development and there is less venture capital available for research and development that might otherwise occur outside of the corporate walls of the incumbent technology providers.

NewMarket has set out to try and develop a new process and a new approach for finding capital to invest in research and development and to monetize the investment return from successful research and development. We do this by taking three fairly traditional business functions and combining them in a way they haven't been put together before. One is simply systems integration, very similar to the business that IBM, Electronic Data Systems or Affiliated Computer Systems is in today. NewMarket provides traditional systems integration services. We are a reseller for Cisco, Microsoft and Sun, just to name a few incumbent technologies. We integrate and maintain and resell those products.

We also are a technology incubator. We acquire emerging technologies that are being developed in garages and on kitchen ta-

bles around the world. We put those two business functions together so that we can get some good old-fashioned operational efficiencies from a core business (systems integration) and a developing business, as well as getting the marketing synergies of combining brand name incumbent technologies with no-name emerging technologies.

The third function, which is just starting to come into play in our business development to date, is where we monetize the value of the incubated companies by publicly listing them independent of NewMarket Technology. That gives us the ability to, one, issue a dividend in the form of a new stock to the shareholders of NewMarket Technology and, two, be able to sell fractional ownership. While NewMarket still stays in control of that company, we can create equity income that will improve our profit margins beyond typical systems integrators. The third, of course, is so that the spin-off company can be capitalized using its own stock to grow even beyond where it has been incubated inside of NewMarket Technology.

TWST: How long have you been an incubator?

Mr. Verges: We have been an incubator since a company that I founded with my family in 1997 merged into a public company, NewMarket Technology, originally named IPVoice. My family's company, VergeTech, was started to bring new technologies to market, and we really did that first function of being a traditional systems integrator and then reselling the products of many of the dot-com technologies that were out there. But, of course, they ran out of funding, so we decided to see if we could build a process that not only brought those technologies to market, but provided that necessary early funding through those early stage emerging technology companies.

TWST: Would you give us a couple examples of that?

Mr. Verges: I think one of our founding technologies has been a voice over Internet (VoIP) protocol. There is a lot of excitement in the market about VoIP, and there are a few companies out there that have made big names for themselves and have a number

of customers signed up. But as far as the global telephone market is concerned, VoIP is still a relatively small overall portion of that entire market. The primary reason is overcoming perceptions, the technologies' capability at the moment, and then also overcoming some of the collateral hurdles. Your potential customer already has sunk investment in a traditional telephone switch or has a long-term contract with a traditional service provider, so our approach has been to go in and provide traditional services to the telecommunications department, establish a long-term relationship, and as those long-term contracts with traditional service providers end, replacing it with a VoIP contract. And as those traditional switches are fully depreciated, we replace them with soft switches. Our VoIP business, which was one of the earliest technologies we started with, just posted its first profit in the third quarter of 2005 and has grown to just shy of \$10 million in annualized revenue.

TWST: You are saying that voice over IP can temporarily coexist with embedded technologies?

Mr. Verges: That is correct. We have more of an evolutionary approach from a marketing perspective. It is packaged with some of the traditional solutions today, and we move it in over time.

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TWST: Where do you go from here? What are the key elements in your strategy for the next couple of years?

Mr. Verges: I think we are really in an exciting stage of our business. NewMarket has grown to \$50 million in annualized sales with good profitability. We have done that really with just the first two components of our business model, the systems integration and the incubation. We have not yet started to realize the most exciting benefits of the company that come from the monetization of our emerging technologies. In 2006 and beyond, shareholders will begin to see the first public listings of some of our incubated technology and see the opportunity to have equity dividends issued in the form of stock in the spinoff company and the increase in our profitability from adding the equity income line to our traditional systems integration and incubated technology product and service sales.

TWST: What challenges or problems might lie ahead for you?

Mr. Verges: In the traditional systems integration business, there are certainly a lot of competitors. We're being successful. We are growing rapidly and being noted for that growth. We were recognized this year by Deloitte in their Fast 500 program as the second fastest growing high-tech company in Texas and the 13th fastest growing company in the nation. Great recognition, great ac-

colades, but we still don't have household name recognition or an appreciation in the investment world for our success.

Our challenge is continuing to compete and be recognized as a viable provider of traditional system integration services. The most exciting part of our business model is the challenge, because it is a new business model. We actually have made our first attempt at listing our first subsidiary in an independent public listing and issuing our first dividend, and we stubbed our toe, but only temporarily. We are months behind on actually getting that dividend out the door to our shareholders, and in fact, it may not end up being our first dividend. Our second publicly listed company may be our first dividend received by our shareholders.

Understandably, the delay has frustrated some shareholders, but I think we have to look at it in a similar fashion to breaking the sound barrier. Certainly, Chuck Yeager didn't break the sound barrier in his first attempt, not even in his first aircraft that he took off the ground. In building the new business model, we will perhaps have other toe stubbing issues along the way, but I am confident we will succeed and establish the full cycle of this new business model, the systems integration, the incubation and the equity monetization of those incubated companies.

TWST: What would you reasonably expect the company to look like in about three years?

Mr. Verges: In three years, our goal is to develop NewMarket into a company approaching \$500 million in revenue, primarily from the traditional systems integration business and the growing portfolio of incubated technologies. It is a goal that we feel is attainable, but not quite a forecast yet. I think that you'll see a lot of that growth from our success at building a reputation for managing larger and larger contracts in the traditional systems integration business. Our approach to establishing that reputation and growing organically by winning larger contracts today is largely by expanding our Board of Directors with some industry names and reputations.

For instance, we just added General Hugh Robinson, a retired Major General who graduated at the United States Military Academy at West Point. After his retirement from the military, he served for seven years on the Board of Directors of the Federal Reserve of Dallas and was the Chairman for two of those seven years. He sits on the Board of Directors of CarMax today and ROS. With that type of reputation and the relationships that he brings to our company, I believe we'll be able to bring in more impressive customers than we have today with larger and longer-term contracts.

I think that in a couple of years, you will see our profitability improve dramatically and impressively as we kick this equity monetization program into high gear and are able to sell fractional ownership in a number of publicly listed subsidiaries, where we are able to acquire the company at a par rate per share of pennies and sell it for a significant profit on that pennies-per-share acquisition. I think that shareholders in years to come can look forward to a reputation of NewMarket issuing dividends in the form of equity in publicly listed subsidiaries.

TWST: Would you tell us about the career path that you followed that led you to be the CEO of NewMarket Technology, as well as some sense of how you developed your own ideas over the years?

Mr. Verges: There is a great deal of continuity in my career path and what NewMarket is today. I would say some of that may be accidental as much as it is logical in hindsight. I am not sure it was well thought out or planned. I'm a graduate of the United States Military Academy and chose a life dedicated to public service until I started having a family and my wife informed me that public service was not going to support the size family that we were planning on. I have five children today, and I had to look for a new job.

I ended up moving back to my hometown when I exited the Army and going to work for a notable hometown company that was started by Ross Perot. I went to work for Electronic Data Systems and cut my teeth in technology. I was actually a programmer building the mechanical engineering software application for Electronic Data Systems' client, General Motors.

I grew from there and eventually went into account management, managing customers outside the mechanical engineering area. I ended up working in the non-depository credit industry, working for credit card companies and mortgage banks. With a background in low-level programming of Unix applications and working in financial institutions, at that time I discovered that many financial institutions were investing in the early computer telephony integration. These platforms were largely low-level C/Unix software applications. Ironically, I had a technology background and fell into a space where the industry I was working in was buying applications in the area that I had a technology background in.

What I discovered there is that digital technology for decades has been sold to create efficiencies and savings. When you're selling the technology that has been used to manage customer relationships into an environment, you're using technology to create differentiation from your other financial institution competitors at that time or create new lines of revenue.

That's what the vision is for NewMarket today. How can emerging technology be used to create differentiation for the customers of that emerging technology? How can it be used to create new revenues that are complementary to existing revenues for the customers of that emerging technology? And we have simply gone and built a business model by turning to existing business models and combining them in order to achieve that vision.

TWST: Would you also tell us about the backgrounds of a couple of your key colleagues?

Mr. Verges: Until the last 12 months, NewMarket has been largely a key man operation. But in order for us to grow beyond \$50 million, clearly we'll have to have a full management team. I think one of the most exciting additions to the team has been Phil Rauch, our current Chief Financial Officer. Phil Rauch has come to the company through one of our acquisitions. Phil Rauch is a graduate of Wharton Business School, brings a great deal of experience with supporting the financial infrastructure of the company and has a lot of experience in large corporations as well as startup and fast growth companies.

We are also adding a great deal of oversight to the company by expanding our Board of Directors. One example is General Hugh Robinson, which I've already shared with you. An additional example is a gentleman named Mike Tinsley, who has worked for one of the largest notable turnaround consultant companies in the world. And sitting on our Board of Directors, while we are not necessarily

doing turnarounds, often when you acquire a young, emerging technology company, some of the disciplines that need to be implemented are similar to corporate turnarounds, so he is an example of the oversight that we are adding to the company. In addition to adding that function of oversight, he is also chairing the subcommittee on our Board of Directors to continue to add to our management team.

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TWST: How many employees do you have now?

Mr. Verges: NewMarket has well over 300 employees. Domestically, we are just shy of 100 employees. Most of our other employees work for us in Asia and Latin America.

TWST: Being a small company, do you anticipate having some difficulties in satisfying the requirements of Sarbanes-Oxley, since it is often very burdensome for the small company?

Mr. Verges: The challenges of Sarbanes-Oxley for small companies is something I am extremely vocal about to as many as possible sources that I think may be able to create change. I'm talking to legislators, to Chairmen of various exchanges and now trying to bring General Robinson and some of his contacts to the table.

Some of the challenges may actually be outside of what people might expect. There are fewer accounting, auditing and legal vendors available to small businesses as a result of Sarbanes-Oxley. Having fewer of them available to you by law of supply and demand is increasing the price small businesses have to pay. There is more volume of work that has to be done, and I think that interested shareholders would expect those prices to increase just by the volume.

I think one of the unanticipated impacts has been the reduction in the number of available resources to small businesses, and the resulting increase in just the hourly rate of service. That certainly will be an impact. I think that the key for small business to manage that impact is by building a strong Board of Directors that brings with them a great deal of experience, knowledge and capability, as well as the attitude to roll up their sleeves and get involved, so that we take on as much of the burden of Sarbanes-Oxley internally and leave as little of the burden of Sarbanes-Oxley as possible to outside vendors.

TWST: Do you see any need to improve the company's capital structure?

Mr. Verges: We are doing a number of things to address the capital structure inside the company. We've been a company traded on the Over the Counter Bulletin Board, which is a tremendous environment for concepts and early development stage companies, because concepts and early development stage companies do not have fundamental financials to submit to potential investors in order to gain the necessary capital to build their companies. But

with a publicly listed stock, that company without fundamental financials has a tool they can use for capital formation. Inevitably, the issued and outstanding and the float of those early development stage companies grows. Ours has grown from less than \$50 million shares outstanding in the last three years to over \$100 million in recent months, so we had a substantial increase in the number of issued and outstanding shares.

Certainly, there are many companies on the OTCBB that are in the billions of shares outstanding. In fact, the top 100 most actively traded companies on the OTCBB are 1 billion shares on average issued and outstanding. So, while ours has been significant, we still feel as though we have got a respectable issued and outstanding. Nevertheless, now that we have fundamental financials with three years of profits and \$50 million in revenue, we have a balance sheet that can stand on its own for potential financing without simply turning to our stock for capital formation and mergers and acquisitions.

Recently, as a watershed event for the company, we just made our first acquisition of a company for all cash, so we have been able to demonstrate the soundness of our fundamental financials in order to continue to execute on our business plan. We are looking at this all cash acquisition of a company that has \$14 million in sales as a watershed event and a turning point to demonstrate that we can not only grow without a continued significant increase in the issued and outstanding, but also reduce that issued and outstanding. We have used preferred stock for many, if not all of our other acquisitions.

We are currently in the process of restructuring much of the preferred stock into subsidiary companies, so that we can actually reduce the fully diluted issued and outstanding of NewMarket. We anticipate disclosing a dramatic reduction in the fully diluted issued and outstanding of NewMarket Technology concurrent with the release of our 2005 annual report on Form 10-K. We also anticipate upgrading our listing. We have announced an application to the American Stock Exchange and do anticipate the listing on an upgraded exchange in the course of 2006.

TWST: What would be the two or three best reasons for the long-term investor to look very closely at NewMarket technology?

Mr. Verges: I think our growth would be one. There's the recognition, for example, that we have received from Deloitte in their Fast 500 program, being one of the 13th fastest growing companies in North America, the three-year of profitability, the 18,000% growth and our continued growth into 2006. I think investors should keep a close eye on the third aspect of our business model, the equity monetization, and the public listing of our subsidiary companies, the dividends that will be issued, the continued growth of those subsidiaries gaining access to financing with an independent listed stock, and the ability to increase our profits well beyond the profit opportunity of comparable technology service companies when we add equity income to our traditional technology service income.

TWST: Is there anything that you would like to add, especially regarding challenges, opportunities, strategies and long-term objectives?

Mr. Verges: I think that challenges in general are associated with the pros and the cons, which are the same topic of conversation in regard to the Over the Counter Bulletin Board exchange, as I mentioned earlier in our conversation. In a concept or very early development stage of the company, when you don't have fundamental financials, the Over the Counter Bulletin Board exchange is a tremendous environment for managers and Founders of companies. As you establish fundamental financials, there is very little correlation to the fundamental financials and what the share price is. Share prices on the OTCBB lean toward a simple formula of supply and demand, rather than any true representation to the fundamentals and market valuations of the company.

Those are challenges that we have to overcome, and one of several approaches to overcome that challenge is growing off of the OTCBB. I think a related challenge is in managing the patience of shareholders. Shareholders in early development stage companies invest for the dramatic return opportunities of an early development stage company that successfully grows to sustainability.

What a shareholder in an early development stage company has to understand is that they are investing in the fundamental strategy and the fundamental financials that are produced from the strategy of that company and that, fundamentally, a reasonable valuation is not always reflected in the share price of the company. The company has to mature past the OTCBB listing for the share price to be aligned with the fundamental investment in the company. That is a difficult stage for shareholders to be in, but, inevitably, every early development stage company that leverages the OTCBB environment will go through this stage. And, if they are successful in building this sustainable company, they will grow through that stage.

But that transitional period can be a challenging period, testing the patience of shareholders, and I believe that is the period that we're in with some of our long-term shareholders today. That's offset by people who are meeting NewMarket for the first time and haven't previously invested in the company and they've discovered a company that has an undervalued share price. That brings new excitement into the company and bolsters that patience that the long-term shareholders have to have during the transition.

TWST: Thank you. (MC)

PHILIP VERGES

Chairman & CEO

NewMarket Technology Inc.

14860 Monfort Drive

Suite 210

Dallas, TX 75254

(972) 386-3372

newmarkettechnology.com

e-mail: ir@newmarkettechnology.com