

**BELZBERG TECHNOLOGIES INC.**

*Management's Discussion and Analysis*

*March 31, 2004*

BELZBERG TECHNOLOGIES INC  
**Management's Discussion and Analysis**  
*for the three months ended March 31, 2004*

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*The following discussion and analysis provides a review of Belzberg's results for the first quarter of 2004 compared to the first quarter of 2003. This discussion should be read in conjunction with the unaudited consolidated interim financial statements and related notes in the quarterly report and the MD&A, consolidated financial statements and related notes in Belzberg's annual report for the year ended December 31, 2003. All monetary amounts are reported in Canadian dollars.*

*This report contains forward-looking statements that involve risk and uncertainties. These statements can be identified by the use of forward-looking terminology such as (but not limited to) "may," "will," "expect," "anticipate," "estimate," "plans," "continue," "believe," or the negative thereof or other variations thereon or comparable terminology referring to future events or results. The Corporation's results could differ materially from those anticipated in these forward-looking statements as a result of numerous factors. The corporation wishes to caution readers not to place undue reliance on such forward-looking statements that speak only as of the date made.*

## **General**

Belzberg Technologies Inc. is a leading provider of exchange connectivity, trade execution, order management, and routing software for the financial industry. In addition to its technology, through one of its wholly owned subsidiaries, an agency-only broker-dealer, Belzberg offers low cost trade execution. The Company's customers include broker-dealers and their customers, who use Belzberg's trading software to buy and sell equities and stock options on a variety of stock exchanges, Electronic Communications Networks (ECNs), or Nasdaq market maker trade management systems. Belzberg products enable traders to execute and manage large volumes of transactions at high speed, and with great reliability and security.

## **Financial Summary and Results of Operations**

<b>Belzberg Technologies Inc.</b>		
<b>Consolidated Statements of Operations</b>		
(\$000's except per share information)	Three months ended March 31,	
	<b>2004</b>	<b>2003</b>
Revenue	\$ 6,710	\$ 6,038
Cost of revenue	3,448	3,587
Gross margin	3,262	2,451
Expenses	2,552	3,305
Earnings (loss) before undernoted items	710	(854)
Amortization	579	734
Interest expense, net	-	50
Restructuring charges	-	273
Net earnings (loss)	\$ 131	\$ (1,911)
Earnings (loss) per share:		
Diluted	\$ 0.01	\$ (0.14)
Basic	\$ 0.01	\$ (0.14)

## Revenues

For the three months ended March 31,

(\$000's)	2004			2003		
	Canada	USA	Total	Canada	USA	Total
Transaction fees - core	524	3,042	<b>3,566</b>	462	1,816	<b>2,278</b>
Subscription fees	\$ 1,553	\$ 304	<b>\$ 1,857</b>	\$ 1,535	\$ 837	<b>\$ 2,372</b>
Transaction fees - brokerage	-	860	<b>860</b>	-	1,145	<b>1,145</b>
Other revenue	260	167	<b>427</b>	215	28	<b>243</b>
<b>Total revenue</b>	<b>\$ 2,337</b>	<b>\$ 4,373</b>	<b>\$ 6,710</b>	<b>\$ 2,212</b>	<b>\$ 3,826</b>	<b>\$ 6,038</b>

Total revenue increased from \$6.0 million in the first quarter of 2003 to \$6.7 million in the first quarter of 2004, an increase of 11%. This increase was attributable primarily to transaction fees in the core business. This has been caused by an increase in equity order flow from new clients signed in 2003 and Q1 2004 as well as an increase in trading volumes from our existing clients as market conditions improved. We also saw increased option order flow caused by increased users of the CBOE Hyts trading platform that utilizes Belzberg's technology. Lastly, the Company recorded significantly higher revenues associated with exchange fees, specialist fees, etc. that were passed back to clients. Transaction fee revenue from the core business, which includes customers paying a fee per transaction routed through the Belzberg Gateway, increased by 57% in the first quarter of 2004 to \$3.6 million as compared to \$2.3 million in the first quarter of 2003 and accounted for 53% of total revenues in the first quarter of 2004 as compared to 37% of total revenues in the first quarter of 2003.

Subscription fee revenue, which is based on customers paying a fixed monthly fee for each terminal connected to the Belzberg Gateway, decreased by 22% in the first quarter of 2004 to \$1.9 million as compared to \$2.4 million the first quarter of 2003 and accounted for 28% of total revenues in the first quarter of 2004 as compared to 39% of total revenues in the first quarter of 2003. This was caused primarily by certain clients in the earlier part of 2003 moving toward in house solutions rather than continue with the Belzberg solution as they attempted to save money in the uncertain market conditions that prevailed in Q1 2003.

Transaction fee revenue from the brokerage operation, that executes on an agency basis exchange traded equity and index options on the Chicago Board Options Exchange, decreased by 25% in the first quarter of 2004 to \$0.9 million as compared to \$1.1 million in the first quarter of 2003 and accounted for 13% of total revenues in the first quarter of 2004 as compared to 19% of total revenues in the first quarter of 2003. This decrease was caused by continued downward pricing pressure in the market place to execute options on the floor of the CBOE.

Other revenue that includes software development fees, installation fees, information distribution fees and revenue from connectivity to the Belzberg Gateway, increased to \$0.4 million in the first quarter of 2004

as compared to \$0.2 million in the first quarter of 2003 and accounted for 6% of total revenues in the first quarter of 2004 as compared to 4% of total revenues in the first quarter of 2003. This increase was caused by increased project work the company was able to bill on a time and materials basis to certain clients.

### **Gross Profit and Gross Margin**

For the three months ended March 31,

(\$000's)	2004	2003
Revenue	\$ 6,710	\$ 6,038
Cost of Revenue	3,448	3,587
Gross Profit	\$ 3,262	\$ 2,451
Gross Margin %	49%	41%

Gross margin as a percentage of sales increased to 49% in the first quarter of 2004, from 41% in the first quarter of 2003. The increase in margin is attributable to increased revenues, reduced headcount and the Company realizing the full effects of self-clearing that were not fully realized in the first quarter of 2003.

### **Operating Expenses**

For the three months ended March 31,

(\$000's)	2004	2003
Sales and marketing	\$ 805	\$ 922
Research and development	579	1,056
Administration	1,174	1,272
Foreign exchange loss (gain)	(6)	55
Total operating expenses	\$ 2,552	\$ 3,305

#### **Sales and Marketing Expenses**

Sales and marketing expenses decreased by \$0.1 million or 13% to \$0.8 million in the first quarter of 2004 as compared to \$0.9 million in the first quarter of 2003. The decrease is primarily due to reduced headcount, reduced travel and certain consulting costs incurred in the first quarter of 2003 that did not occur in the first quarter of 2004.

#### **Research and Development Expenses**

Research and development expenses decreased by \$0.5 million or 45% to \$0.6 million in the first quarter of 2004 as compared to \$1.1 million in the first quarter of 2003. The decreased expense is primarily due to headcount reductions.

### **Administration Expenses**

Administration expenses decreased by \$0.1 million or 8% to \$1.2 million in the first quarter of 2004 as compared to \$1.3 million in the first quarter of 2003. The primary factors that contributed to the decreased expenses were headcount reductions, reduced professional fees and the cancellation of an insurance policy.

### **Foreign Exchange Loss (Gain)**

The Company incurred an unhedged foreign exchange gain of \$6,000 in the three months ended March 31, 2004 compared to an unhedged foreign exchange loss of \$55,000 in the three months ended March 31, 2003. The Company uses forward exchange contracts to manage a portion of its exposure to fluctuations in foreign exchange rates. As at March 31, 2004, the Company had outstanding forward exchange contracts for the purchase of Cdn\$4.5 million at US\$.725 maturing in December 2004. The cumulative unrealised gain on these contracts at March 31, 2004 was \$196,000 (March 31, 2003 unrealized loss of \$7,000).

### **Other Expenses**

For the three months ended March 31,

(\$000's)	<b>2004</b>	2003
Amortization of capital assets	\$ 579	\$ 734
Interest expense, net	-	50
Restructuring charges	-	273
Other expenses, net	\$ 579	\$ 1,057

### **Amortization of Capital Assets**

Amortization of capital assets decreased by \$0.2 million or 21% to \$0.6 million in the first quarter of 2004 as compared to \$0.7 million in the first quarter of 2003. The decrease resulted from certain capital assets coming to the end of their useful lives and no longer incurring amortization expense.

### **Net Interest Expense**

Net Interest expense decreased by \$50,000 to nil in the first quarter of 2004 as compared to \$50,000 in the first quarter of 2003. The decrease resulted from interest income of \$26,000 on a research and development tax refund being received in the first quarter of 2004 as well as a reduction in interest expense from the buy out of certain capital leases that matured in the latter part of 2003 as well as in 2004.

### **Restructuring Charges**

During the quarter ended March 31, 2003, the Corporation completed the restructuring of certain of its finance, sales and research and development operations announced in the quarter ended December 31, 2002 and recorded an additional restructuring charge of \$273,284 for employee severances and benefits.

### **Net Earnings (Loss)**

Net earnings of \$0.1 million were generated for the quarter ended March 31, 2004 as compared to a net loss of \$1.9 million in the comparable quarter of 2003. Basic and diluted earnings per share for the quarter ended March 31, 2004 was \$0.01 as compared to a loss of \$0.14 per share for the first quarter of 2003.

## **Recent Accounting Pronouncements**

### **i) Revenue Recognition**

Effective January 1, 2004, the Company adopted the CICA Emerging Issues Committee Abstract 142 issued in December 2003, regarding the timing of revenue recognition and the classification of certain items as revenue or expense. Adoption did not have an impact on the consolidated financial statements.

### **ii) Hedging Relationships**

In November 2001, the CICA issued Accounting Guidelines 13, "Hedging Relationships"(AcG-13), and in November 2002, the CICA amended the effective date of the guideline. AcG-13 established new criteria for hedge accounting and applies to all hedging relationships in effect on or after January 1, 2004. Effective January 1, 2004, the Company determined that it would not treat its derivative instruments as hedges for accounting purposes. Accordingly, the Company is continuing its previous policy of recognizing changes in the fair value of the derivative instruments into income each period.

## **Liquidity and Capital Resources**

Cash flow generated by operations was \$1.0 million in the first quarter of 2004 compared to cash flow used for operations of \$0.5 million in the first quarter of 2003. This was attributable to profitable operations and improved collections in accounts receivable.

The Company utilized \$1.9 million of cash for investing activities in the first quarter of 2004 compared to \$0.3 million for the first quarter of 2003. Investing activities in the first quarter of 2004 consisted of the acquisition of capital assets of \$0.3 million and short-term investments in T-bills of \$1.6 million while investing activities in the first quarter of 2003 consisted of \$0.3 million for the acquisition of capital assets.

The Company utilized \$0.3 million of cash for financing activities in the first quarter of 2004 compared to utilizing \$0.6 million for the first quarter of 2003. Financing activities in the first quarter of 2004 consisted of repayment of bank debt and capital lease obligations of \$0.4 million and proceeds from the exer-

cise of stock options of \$0.1 million. Financing activities in the first quarter of 2003 consisted of repayment of bank debt and capital lease obligations of \$0.5 million and the repurchase of 25,000 common shares under a normal course issuer bid for \$0.1 million. As at March 31, 2004, the Company had cash and cash equivalents amounting to \$3.2 million, and had working capital of \$5.4 million. The Company believes that its current cash resources and cash flow from operations will be sufficient to meet its normal working capital requirements capital expenditure requirements for the current year.