Zacks Small-Cap Research

November 23, 2012
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DecisionPoint Systems (DPSI-OTC)

DPSI: Transformation of the Business Model- OUTPERFORM

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	02/23/2012
Current Price (11/20/12)	$0.85
Target Price	**$3.00**

OUTLOOK

DecisionPoint designs, sells, installs and services voice and data communications products and systems for private networks and wireless broadband systems to a wide range of enterprise markets, including retail, transportation and logistics, manufacturing, wholesale and distribution. The combination of its blue chip portfolio of customers as well as the Transformation of the business model has the firm projecting the top-line to nearly double to $100 million and for margins to surge. We see value in the shares of DecisionPoint.

SUMMARY DATA

52-Week High	**$1.63**
52-Week Low	**$0.52**
One-Year Return (%)	**-7.61**
Beta	**1.00**
Average Daily Volume (sh)	**2,861**
Shares Outstanding (mil)	**9**
Market Capitalization ($mil)	**$8**
Short Interest Ratio (days)	**18.02**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**N/A**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**47.5**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2013 Estimate	**6.3x**
Zacks Rank	**3**

Risk Level	**High,**
Type of Stock	**Small-Value**
Industry	**Comp-Software**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2010	$11.1 A	$13.3 A	$16.4 A	$15.5 A	$56.3 A
2011	$12.8 A	$13.2 A	$16.4 A	$15.9 A	$58.4 A
2012	$17.8 A	$17.8 A	$18.6 A	$20.0 E	$74.1 E
2013					$85.0 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2010	-$0.05 A	-$0.04 A	$0.00 A	$0.00 A	-$0.09 A
2011	-$0.05 A	-$0.25 E	$0.01 A	-$0.02 A	-$0.31 A
2012	-$0.06 A	-$0.20 A	-$0.11 A	-$0.01 E	-$0.38 E
2013					$0.19 E

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KEY POINTS

- The mobile computing industry has matured and this has opened the firm up to new vertical markets.
- DecisionPoint has been repositioning itself to focus more on providing higher margin, customer-driven, mobile wireless and RFID solutions.
- The transformation of the business model from Hardware to Services will likely grow the top-line to $100 million annually and increase margins significantly.
- Within the commercial enterprise market, there continues to be long-term opportunity for growth as the global workforce continues to become more mobile.

INVESTMENT THESIS

DecisionPoint delivers to its customers the ability to make better, faster, and more accurate business decisions by implementing industry-specific, enterprise wireless and mobile computing systems for their front-line employees. It is these systems which provide the information to improve the hundreds of individual business decisions made each day. The "productivity paradox" is that the information remains locked away in their organization's enterprise computing system, accessible only when employees are at their desk. DecisionPoint solves this productivity issue. The result for its customers is they are able to move their business decision points closer to their own customers whom in turn, drive their own improved productivity and operational efficiencies.

DecisionPoint does this by providing customers with everything they need through the process of achieving their enterprise mobility goals starting with the planning of their systems, to the design and build stage, to the deployment and support stage, and finally to achieving their projected Return On Investment ("ROI"). DecisionPoint's business designs, sells, installs and services voice and data communications products and systems for private networks and wireless broadband systems to a wide range of enterprise markets, including retail, transportation and logistics, manufacturing, wholesale and distribution, as well as other commercial customers (which are referred to as the "commercial enterprise market").

Target Markets

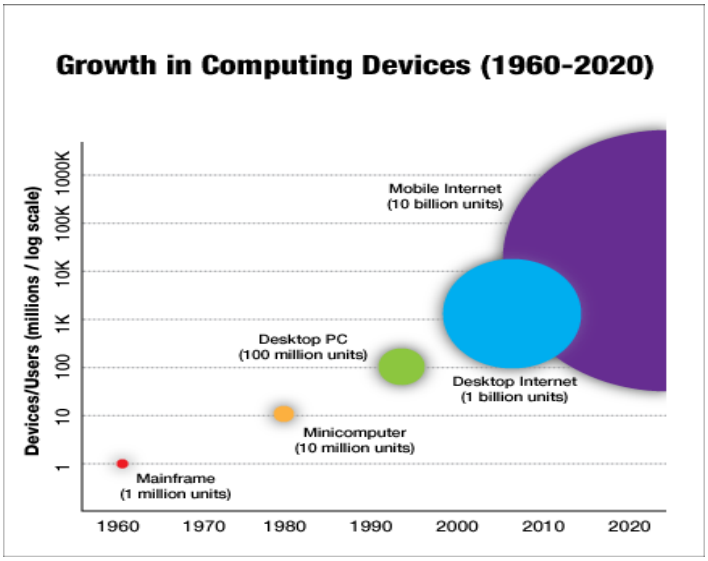
The markets for enterprise wireless and mobile computing are very fragmented while also being extremely complex in nature. But generally they can be characterized by the following attributes:

- Vertical market industries which require specific domain expertise. (Traditionally retail, warehousing, and manufacturing)
- Industries which track goods or deliver a service in the field (or both).
- Industries which have a significant group of mobile workers, whether they operate primarily in one place or in the field.

Backdrop of Growth

Over the past several years several of the key technologies in the mobile computing industry have matured and improved. Several key technologies have been standardized such as Windows mobile operating

systems, Wifi wireless local area networks, and the building out of nationwide wireless data networks such as HSDPA technology and EVDO technology. DecisionPoint designs applications that tailor to that firm's specific industry. An example would be proof-of-Delivery (POD) system for couriers.



Source: Minneapolis news

Rather than simply providing hardware and customized software the firm has been shifting its focus to providing higher margin consulting services along with customer driven mobile wireless and RFID solutions. This has the effect of increasing profitability and margins

Transformation of the Business Model
DecisionPoint has two primary business lines; Hardware and Software and Professional Services.

The firm has completed three acquisitions over the last 19 months (CMAC, Apex and Illume Mobile) which allow the Company to offer the full range of mobile solutions to meet the requirements of any enterprise mobility strategy as well as generate higher margins than other divisions in the Company, which in turn should lead to improved corporate gross margins.

	% Current Revenue	Current Pipeline	Gross Margin Range
Hardware	64%	55%	11-25%
Software Services	36%	45%	30-65%

CMAC
CMAC is a logistics consulting and systems integration provider headquartered in Alpharetta, Georgia. The purchase price of $3.15 million was paid 70% in cash and 30% in stock. Management feels CMAC offers complementary services to similar end markets and is a good fit with DecisionPoint. Combining with CMAC will shift DecisionPoint's revenue mix more in favor of services and software, resulting in expected incremental gross margin expansion of 100 to 200 basis points. Further CMAC's strong presence in the Southeast complements geographic service presence in the U.S. to that important and fast growing region.

APEX
On June 5, 2012 DecisionPoint announced a deal with APEX Systems Integrators. The purchase price was

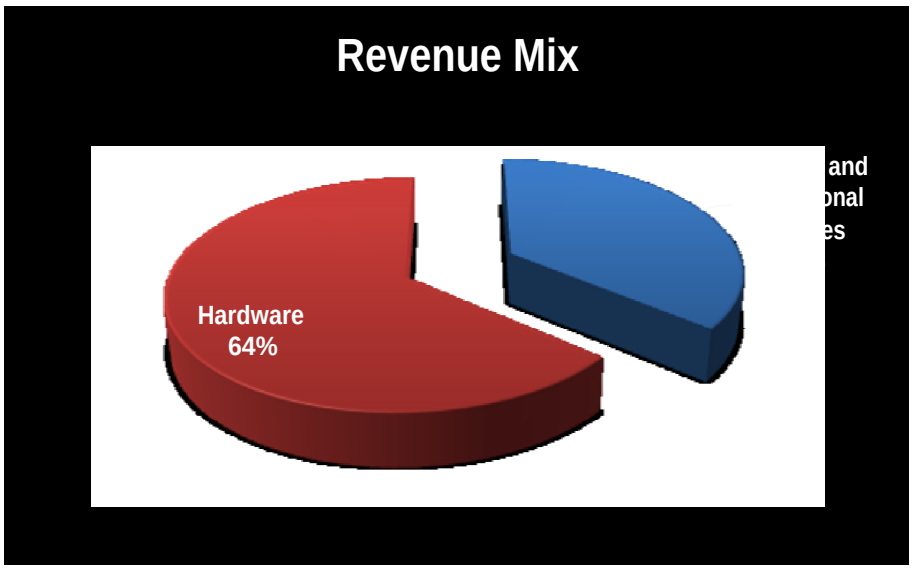
$5.0 million in cash at closing. In addition, there is an earnout and bonus capped at an additional $8.5 million, which is dependent upon future performance through July 31, 2015. The transaction is expected to be accretive to DecisionPoint's fiscal year 2012 earnings by $0.15 per share on an annualized basis. Servicing clients in the consumer packaged goods, retail, B2B and service sector, Apex has enjoyed an approximately 55 percent per annum growth over the past five years, growing normalized EBITDA from roughly CAD $0.5 million in 2007 to approximately CAD $1.8 million during the full year ended July 31, 2010. The Company's APEXWare™ suite of products provides mobile productivity solutions in the areas of merchandizing, sales and delivery, field service, logistics and transportation, and warehouse management. Furthermore, Apex's software product set is anticipated to fit directly with DecisionPoint's own retail, field force mobility, warehousing, logistics and transportation markets and to provide opportunities for cross selling by both companies' teams.

Illume
On July 31, 2012, DecisionPoint acquired Illume Mobile Software, a division of MacroSolve, Inc., based in Tulsa, OK for approximately $1.0 million in cash and stock. Illume Mobile has patent protected domain expertise in developing Enterprise mobile software for Android and Apple (iOS) mobile devices.

After acquiring and building the business lines, the firm receives revenue four different ways,

- Hardware.
- Services.
- Software Licenses.
- Custom Software.

The Transformation of the business model from the majority of sales coming from Hardware to Software and Professional Services should transform the company's margin and growth characteristics to that of a high margin/ high growth profile. Management has targeted a 60-40 mix with 60% coming from Services. Services enjoys significantly higher margins, stickier revenues, and longer contracts.



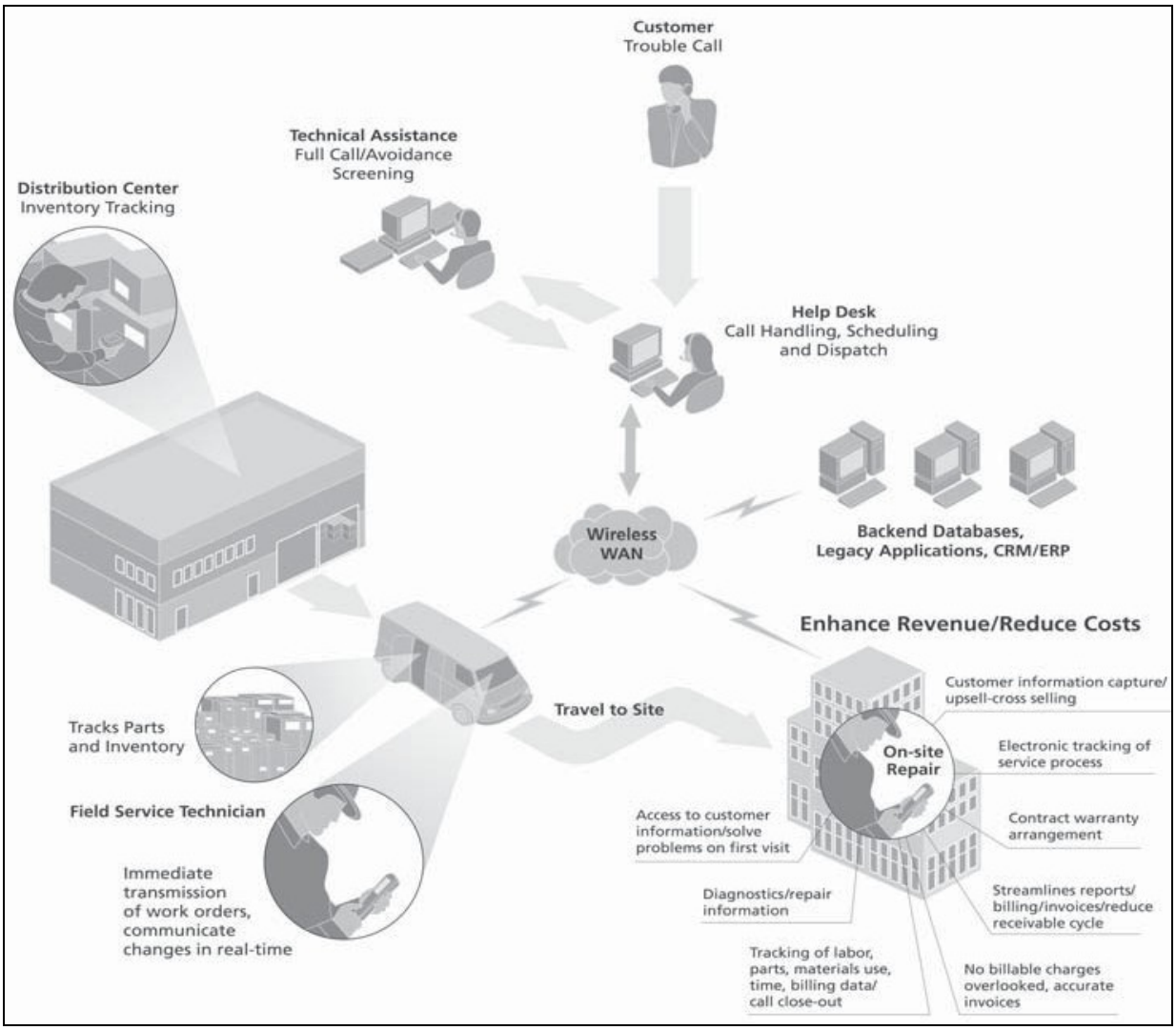
Vertical Markets Shifting

Historically the firm's largest vertical markets were retail, warehousing, and manufacturing. This is intuitive since each had a large amount of goods in motion which needed to be tracked. While these markets are still

attractive to DNPI, new markets have emerged such as Transportation and logistics, and field services such as repair and maintenance, and delivery and inspections. This new group of markets, which cuts across multiple industries and business applications, is referred to as “Field Mobility.” Meaning goods or services are being tracked by field based workforces rather than workers at a single location.

Example of Field Service Management (*Source Symbol Technologies White Paper)

In a day and age when service offerings have become a key competitive differentiator, mobile computing solutions deliver the power to change field service operations from a typical ‘cost of doing business’ to a strategic business unit that contributes heavily to the overall profitability of the company and a dramatic improvement in its competitive position.



Through a combination of technology such as bar code scanning, image capture devices, mobile handhelds and wireless networking, mobile computing solutions reveal a wealth of strategic information that can be used at all levels in a company—from the analysis of an individual services call to planning for a more effective field service operation and identification of repair patterns that can lead to uncovering unknown product weaknesses and better manufacturing. How much impact can a mobile computing solution have on a field service organization? One company shaved one hour of labor off of the workday for each of its 800 field service workers. The total 800 hours in labor savings daily translated into 200,000 hours per year (or

250 workdays). With an average fully loaded cost per hour of $100 per field worker, the company realized a savings of approximately $20 million per year, easily justifying the investment in mobile computing technology.

Fleet Control Set to Grow

The Fleet Control Bundle is DecisionPoint's comprehensive solution for the Transportation & Distribution market delivering Department of Transportation Compliance, real time fleet visibility, automated Federal tax reporting, push-to-talk communication between drivers and dispatchers, complete chain of custody visibility and package condition image capture.

The bundle's three primary components include the Airclic Proof of Delivery, Xata Turnpike Hours of Service and Inspection application and the Push-to-Talk user menu.

Together, the applications allow dispatchers unparallel communications and oversight capabilities, including the ability to examine individual driver performance and vehicle data. All this, while providing automation that driver's need.

The Airclic Proof of Delivery software offers a complete chain of custody visibility.

The application allows all packages to be scanned onto and off of the truck, signatures to be collected and damaged packages to be photographed, ensuring accurate and complete delivery through the use of a Motorola smartphone.

Through, time, date and GPS stamps, the application ensures delivery documentation and other paperwork is properly completed and filed. What's more, if a package is damaged, the damage can be recorded through the smartphone camera.

The Xata Turnpike Hours of Service and Inspection application collects information automatically and electronically making fraud impossible by automating driver reporting tasks.

Through an on board recorder, engine diagnostics and GPS data is collected and blue toothed to the Motorola Smartphone. All of this information is stored on the device and easily viewable by the driver and roadside inspectors.

Additionally, the application eases monthly IFTA tax reporting burdens by automating IFTA reporting through complete detailed reports showing where fuel was burned so that IFTA can distribute the taxes appropriately.

What's more, the software tracks hours of service and supports FMCSA log compliance.

The Grapevine Push-to-Talk solution offers a number of key features including a private and secure network with voice encryption; scalability that allows communication with thousands of individuals and group participants at once; voice history where the user can replay previous conversations; interoperability anywhere in the world across all WWAN, and Wi-Fi networks at the same time (including over different carriers); and is an SaaS managed service requiring no hardware or overhead.

It is important to note that recent market trends show retailers making strategic investments in wireless and tablet based solutions.

DecisionPoint has been attempting to leverage this latest trend of customized solutions and support by deepening its relationship with major wireless carriers through the launching of co-branded products that would combine DecisionPoint's new products and technology (such as Grapevine, Proof of Delivery and Mobile Device Management) with some of the major mobile provider's other products and services.

This recent business strategy by DecisionPoint, is expected to increase ROI by generating high margin products with recurring revenue while lowering costs and risk.

DecisionPoint's working with Verizon's Transportation & Distribution Vertical Market team to design and deliver the Fleet Control bundle is proof that this business strategy may be starting to bear fruit.

Still, it is important to note that while Verizon owns the trade marked Fleet Control name, DecisionPoint is the exclusive solution provider.

RECENT NEWS

On November 14, 2012, DecisionPoint Systems, reported financial results for its fiscal 2012 third quarter and nine months, ended September 30, 2012.

The solid third quarter performance resulted in record revenue, with sales jumping $2.120 million or nearly 13 percent year over year to $18.567 million from $16.446 million for the three months ended September 30, 2011.

Sequentially, third quarter revenues improved by 4.5 percent over the $17.767 million from the second quarter fiscal 2011. The upturn in revenues for the three months ended March 31, 2012 was driven by increased field mobility solution sales and increased professional services revenue.

Gross margin surged 250 basis points year over year from 20.9 percent in the third quarter of 2011, up to 23.4 percent for the three months ended September 30, 2012. Sequentially, third quarter gross margin improved 210 basis points from 21.3 percent for the three months ended June 30, 2012.

The increase in gross margins was primarily a result of the higher gross margin from professional services revenue and improved utilization of professional services resources.

It should be noted that the higher margin professional software and services revenue has now grown to over 35% of total revenue. Additionally, the Company has continued to emphasize cost control and improved efficiencies throughout its operations.

Selling, general and administrative expenses in the third quarter increased year over year by $1.676 million and sequentially by $102,000 to $4.951 million. The year over year increase in selling, general and administrative expenses was primarily the result of increased personnel and operating expenses relating to the Illume and Apex acquisitions of $0.6 million as well as Illume and Apex acquisition related costs of $0.5 million.

Adjusted EBITDA for the third quarter of 2012 improved year over year by $300,000 to $1.1 million compared to a $0.8 million for the same quarter of fiscal 2011.

Net loss attributable to common shareholders was $1.262 million for the fiscal 2012 third quarter compared to net income attributable to common shareholders of $54,489 for three months ended September 30, 2011. Based on a weighted average number of diluted shares of 8.182 million, diluted net loss per share resulted in a net loss of $0.15 per share for the third quarter of fiscal 2012. This compared to diluted net income per share of $0.01 based on a weighted average number of diluted shares of 7.417 million during the three months ended September 30, 2011.

The Company ended the quarter with $392,424 in cash and a working capital deficit of $9.220 million. This compares to $498,357 in cash and a working capital deficit of $6.005 million as of June 30, 2011.

Still, cash flow from operating activities for the first nine months of 2012 was $0.7 million compared to $(1.4) million for the same period in 2011.

Recently DecisionPoint made three acquisitions (CMAC, Apex and Illume Mobile) which have broadened the Company's software products and professional services capabilities, opened new markets and deepened relationships with customers.

Furthermore, the Company's record revenue and gross margin expansion in the third quarter reflects the growing success of the strategic shift that DecisionPoint has made over the past two years to develop its field mobility solutions and professional services and software divisions.

Likewise, management stated that it continues to see its field mobility solutions gaining traction with wireless carrier partners and customers as well as the continued expansion of its pipeline of opportunities in its retail and warehouse and distribution segments.

As a result of this positive momentum in its field mobility and retail systems divisions, management believes the Company remains well positioned for continued revenue and adjusted EBITDA growth.

VALUATION

DecisionPoint remains well positioned to achieve solid revenue growth and operating leverage given the trend toward to mobile communications with machines that communicate from the field. We feel the company's competitive advantage is twofold. It connects a growing number of businesses beyond traditional industries as well as incorporating higher margin services beyond being a reseller.

We value the company based our two stage intrinsic model.

The intrinsic value is essentially a sum of the company's future earnings, minus any long-term debt. Dividing the intrinsic value by the number of shares outstanding yields an intrinsic stock price. We used the following inputs:

- A 10-year period with an earnings growth rate of 12.5% (average forecast) and a discount rate of 10.3%.
- A continuing period assumed to go on forever, with earnings growing at 6% and a discount rate of 11.4%.

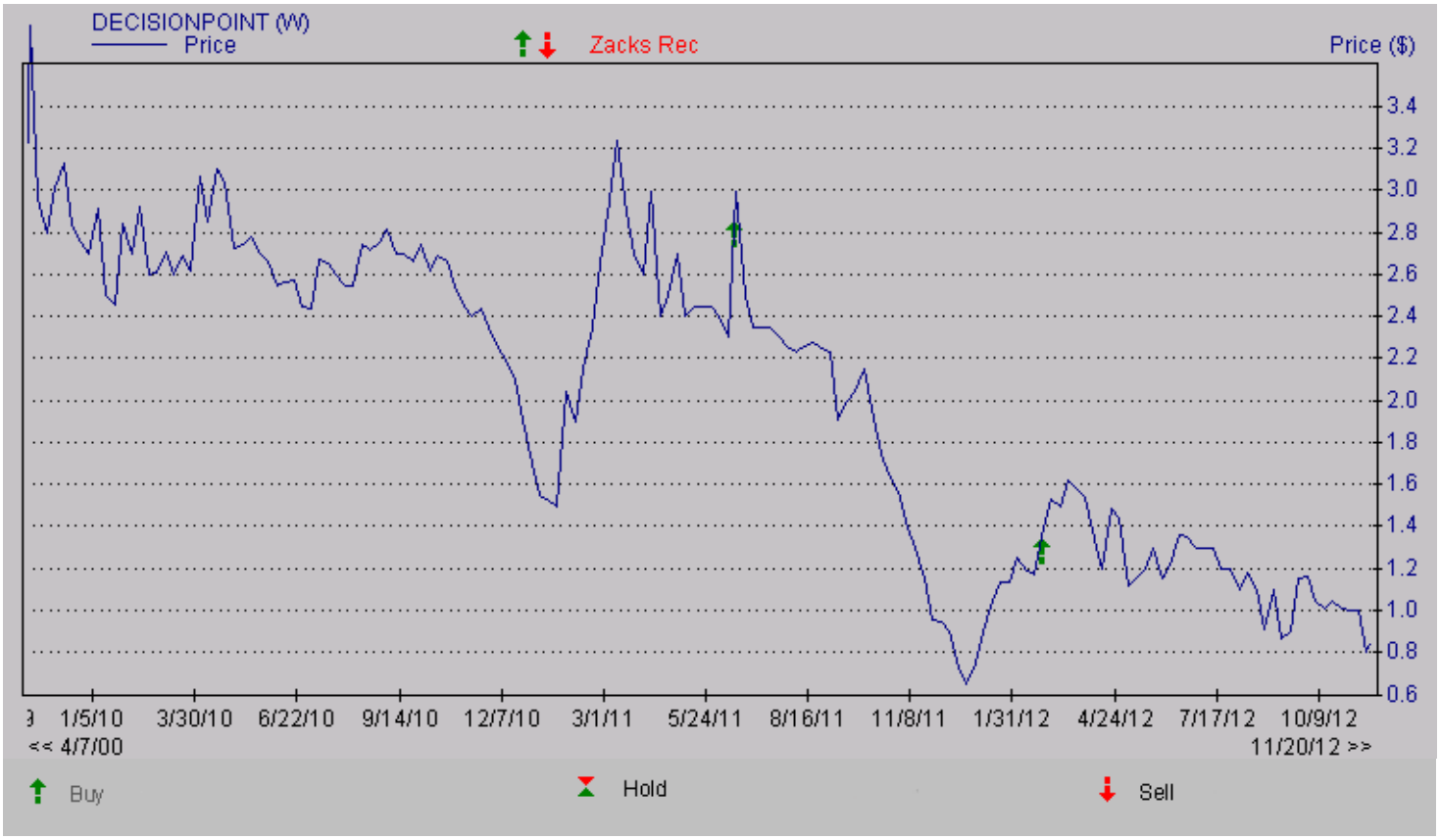
With these inputs we arrive at a target price of $3.00.

PROJECTED INCOME STATEMENT & BALANCE SHEET

INCOME STATEMENT ($ Millions)	Sep-11 Q3 11	Dec-11 Q4 11	Mar-12 Q1 12	Jun-12 Q2 12	Sep-12 Q3 12	Dec-12 Q4 12 E	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012 E	FY 2013 E
REVENUE												
Net Revenue	**16.45**	**15.89**	**17.81**	**17.77**	**18.57**	**20.00**	**53.31**	**48.31**	**56.24**	**58.37**	**74.14**	**85.00**
Sequential Growth		*-3%*	*12%*	*0%*	*5%*	*8%*						
OPERATING EXPENSES												
Cost of Revenues	13.01	12.32	14.06	13.99	14.22	15.75	43.21	38.57	45.39	46.4	58.0	64.0
% of Revenue	*79.1%*	*77.6%*	*78.9%*	*78.7%*	*76.6%*	*78.8%*						
Gross Profit -	**3.4**	**3.6**	**3.8**	**3.8**	**4.3**	**4.3**	**10.10**	**9.74**	**10.9**	**12.0**	**16.1**	**21.0**
Proforma Gross Margin	*20.9%*	*22.4%*	*21.1%*	*21.3%*	*23.4%*	*21.3%*	*18.9%*	*20.2%*	*19.3%*	*20.6%*	*21.7%*	*24.7%*
R&D + Engg	0.00	0.00	0.00	0.00	0.00	0.00	0.0	0.0	0.0	0.0	0.0	0.0
% of Revenue	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*
SG&A	3.27	3.33	3.84	4.85	4.95	4.00	9.15	7.97	9.61	13.49	17.64	17.00
% of Revenue	*19.9%*	*21.0%*	*21.5%*	*27.3%*	*26.7%*	*20.0%*	*17.2%*	*16.5%*	*17.1%*	*23.1%*	*23.8%*	*20.0%*
GW Amort, Restructuring, other	-	-	-	-	-	-	-	-	-	-	-	-
% of Revenue												
Total Operating Expenses	3.27	3.33	3.84	4.85	4.95	4.00	9.15	7.97	9.61	13.49	17.64	17.00
% of Revenue	*19.9%*	*21.0%*	*21.5%*	*27.3%*	*26.7%*	*20.0%*	*17.2%*	*16.5%*	*17%*	*23%*	*24%*	*20%*
Operating Income -	**0.2**	**0.23**	**-0.1**	**-1.1**	**-0.6**	**0.3**	**0.95**	**1.78**	**1**	**-1**	**-2**	**4**
Operating Margin	*1.0%*	*1.5%*	*-0.5%*	*-6.0%*	*-3.3%*	*1.3%*	*2%*	*4%*	*2%*	*-3%*	*-2%*	*5%*
NON-OPERATING ITEMS												
Non operating Income/Expense	0	0	0	0	0	0	(1.88)	-1.4	-3.37	-1	-1	-1
% of Revenue	*0.71%*	*-0.56%*	*-0.63%*	*-1.05%*	*-1.85%*	*-0.40%*	*-3.53%*	*-2.81%*	*-6.00%*	*-1.41%*	*-0.97%*	*-1.18%*
Tax Provision	0.013	0.079	0.042	0.026	0.064	0.050	-0.046	0.071	0.079	0.100	0.182	0.150
Pref Divs	*$ 0.21*	*$ 0.22*	*$ 0.22*	*$ 0.24*	*$ 0.25*	*$ 0.22*			*$*	*0.49*	*$ 0.93*	*$ 0.60*
Net Income -	**0.05**	**-0.15**	**-0.46**	**-1.52**	**-1.26**	**-0.10**	**(0.89)**	**0.35**	**-2.2**	**-2.9**	**-3.3**	**2.3**
Net Income Margin	*0.3%*	*-1.0%*	*-2.6%*	*-8.6%*	*-6.8%*	*-0.5%*	*-1.7%*	*0.7%*	*-4%*	*-5%*	*-5%*	*3%*
EARNINGS PER SHARE												
EPS - Basic	$0.01	-$0.02	-$0.06	-$0.20	-$0.15	-$0.01	-$0.18	$0.02	-$0.09	-$0.31	-$0.43	$0.25
EPS - Diluted	$0.01	-$0.02	-$0.06	-$0.20	-$0.11	-$0.01	-$0.18	$0.02	-$0.09	-$0.31	-$0.38	$0.19

Ken Nagy, CFA Zacks Investment Research 11/18/2012

HISTORICAL ZACKS RECOMMENDATIONS



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