Zacks Small-Cap Research

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Labor Smart Inc (LTNC-OTCBB)

LTNC: *Raising estimates on recent revenue trends.*

Current Recommendation	**Buy**
Prior Recommendation	N/A
Date of Last Change	05/22/2013
Current Price (07/17/13)	$0.27
Target Price	**$0.80**

OUTLOOK

Labor Smart, Inc. is an emerging growth company that serves the on-demand labor market, focusing primarily on filling blue-collar staffing positions on a temporary basis. In just two short years, the company has grown its footprint to 14 branches operating in nine states, up from only two in 2011, and annual revenue to an estimated $16.09 million in 2013, up from only $0.16 million in 2011. With a seasoned industry veteran at the helm, an experienced operating team, an ambitious growth strategy and the tailwind of favorable sector dynamics, we maintain our Outperform rating on Labor Smart shares.

SUMMARY DATA

52-Week High	**$0.82**
52-Week Low	**$0.10**
One-Year Return (%)	**N/A**
Beta	**-10.60**
Average Daily Volume (sh)	**27,716**
Shares Outstanding (mil)	**19**
Market Capitalization ($mil)	**$5.2**
Short Interest Ratio (days)	**0.6**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**78**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2013 Estimate	**N/A**
P/E using 2014 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Staffing**
Zacks Rank in Industry	**N/A**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2011					0.16A
2012	1.184A	1.710A	2.152A	2.129A	7.176A
2013	2.503A	4.037E	4.864E	4.685E	16.090E
2014					30.572E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2011					$0.00 A
2012	$0.00 A	$0.00 A	-$0.01 A	-$0.02 A	-$0.03 A
2013	-$0.04 A	-$0.03 E	-$0.03 E	-$0.02 E	-$0.11 E
2014					-$0.10 E

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

2011 reflects May (inception) to December

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KEY POINTS

- We are revising our forecast to reflect Labor Smart's recent revenue trends. Our 2Q13, 3Q13 and 4Q13 estimates go to $4.04 million, $4.86 million and $4.69 million compared to $3.76 million, $4.78 million and $4.47 million before. This puts our 2013 projection at $16.09 million versus $15.52 million earlier. We are also increasing our gross margin forecasts slightly. We estimate Labor Smart's customer base at well above 500, which we believe improves the company's ability to expand margins.

- Reflecting management's goal to consolidate the existing footprint and drive revenue and margin increases at this stage, we do not anticipate additional office openings in 2013. We expect branch expansion will resume in 2014.

- Recent economic and industry data support continued growth, in our view. A key takeaway from the Bureau of Labor Statistics June 2013 Jobs Report is that the economy continues to shift towards temporary jobs in the current economic climate.

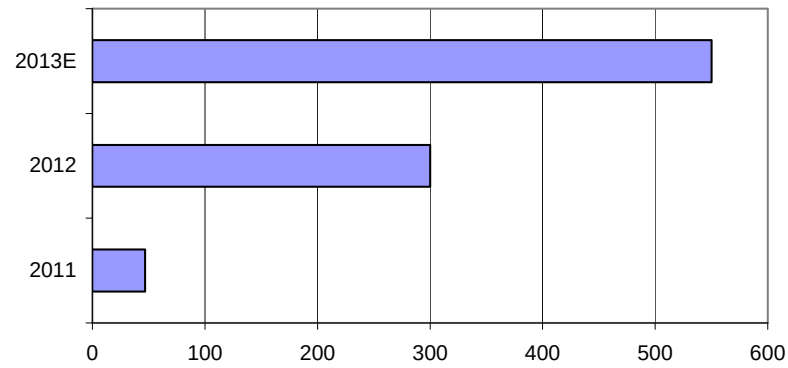
- Labor Smart shares trade at 0.2X on an EV / projected 2014 revenue basis. Our $0.80 price target equates to 0.5X, which is in-line with competitor True Blue.

- Risks include that: the company is highly dependent on founder and CEO Ryan Schadel, is under capitalized, could expand too rapidly, competition could increase, customers could shift towards hiring permanent employees instead of using temporary workers and economic factors could constrain industry growth.

2Q13 PREVIEW: RAISING REVENUE ESTIMATES

Revenue Above Expectations We believe recent announcements from Labor Smart (LTNC-OTC BB) indicate that our original 2013 revenue forecast of $15.52 million may have been too conservative. Last week, the company noted that June 2013 revenue of $1.46 million exceeded June 2012 by 122%. With May and April 2013 revenue at $1.58 million and $1.00 million respectively, 2Q13 revenue came in at an estimated $4.04 million, nearly $275,000 ahead of our $3.76 million projection. We are raising our forecast to reflect the recent run rate. Our 2Q13, 3Q13 and 4Q13 estimates go to $4.04 million, $4.86 million and $4.69 million. This puts our full year 2013 projection at $16.09 million, the low end of management's targeted $16-$18 million. If revenue trends remain as strong as they have been, we believe there could be further upside.

Labor Smart's Growing Customer Base



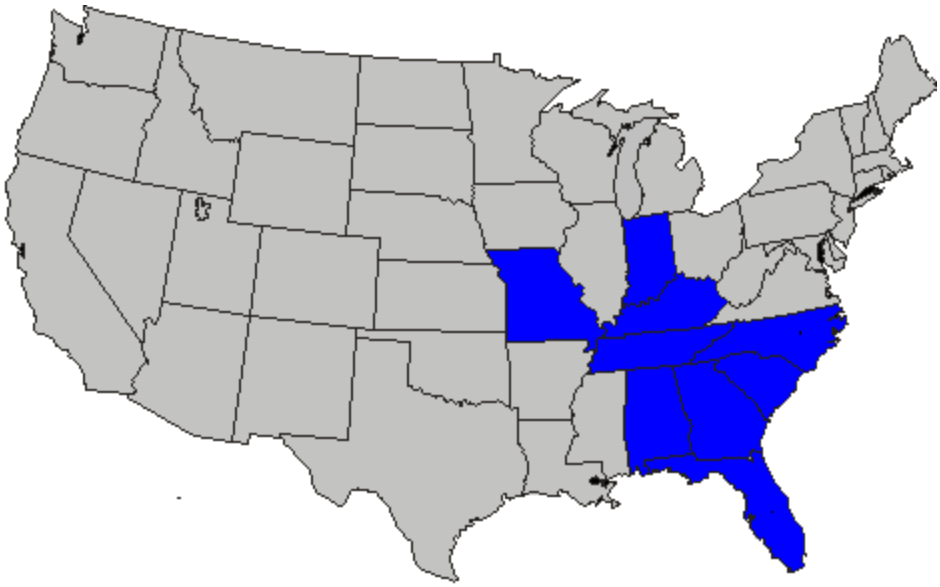
Source: Company reports, Zacks estimates

We are also **raising our gross margin forecast**. At this early stage, the company has not yet reached its targeted 28% branch level gross margin. Nevertheless, management recently indicated that gross margins are improving as Labor Smart's customer base expands and diversifies. Revenue growth is highly correlated to customer base expansion, in our opinion. In 2011, Labor Smart had 47 customers. In November 2012, the company announced that its customer base exceeded 300. We estimate that it is well above 500 now.

Having a large and diversified customer base gives the company **greater flexibility in managing gross margins**, in our view. When a new location opens, the branch manager first looks to the construction and janitorial industries for potential customers. These industries have relatively short sales cycles and their staffing needs fluctuate considerably. As they mature, branches can fill more competitive assignments, often leveraging the customer base that the overall organization has established. Other industries that frequently turn to on demand staffing include: hospitality, warehousing, manufacturing, logistics and events, among others. For example, when hotel occupancy rates spike during peak seasons or holidays, hotels often add workers on a short term basis. The company also tries to generate sales in new verticals with existing customers.

We believe the company will manage for revenue and margin growth over footprint expansion for the remainder of 2013. Therefore, we would not be surprised if no additional branches opened in 2013, which implies that the company might not reach its targeted 18 to 20 offices by year-end. Nevertheless, Labor Smart has pursued an ambitious expansion strategy since launching operations two years ago. The company started with two branch offices in November 2011 and has grown to 14 branch offices currently, operating in nine different states.

States in Which Labor Smart Operates Branches



Source: Company reports

We anticipate that branch expansion will resume in 2014. Labor Smart intends to open another 25 to 30 locations next year. Initially, expansion efforts were concentrated on the Southeast U.S. The first two branch offices were located in Marietta, Georgia and Nashville, Tennessee. Labor Smart has subsequently expanded into Kentucky, Florida, Indiana, Alabama, Missouri, South Carolina and North Carolina and ultimately plans to have a national footprint. This would provide a competitive advantage, we believe, over more regionally focused competitors and enable Labor Smart to leverage its marketing efforts across geographic markets.

Most of the early growth has been through new branch openings, although in 2Q13 the company acquired the operating assets of a small, three branch staffing company based in Florida. Qwik Staffing Solutions had offices in Jacksonville, Orlando and Tampa. Based on their historical performance, management anticipates they will contribute more than $3.2 million in revenue and roughly $350,000 in EBITDA over the next 12 months and be immediately accretive to EBITDA. Half of the purchase price is to be paid out over time as a percentage of the earnings the branches generate. In our view, this protects Labor Smart on the downside if the branches do not perform up to management's expectations.

We believe it is also consistent with management's goal of minimizing net cash use required to fuel its substantial growth. Labor Smart had $125,742 in cash as of March 2013. Although we expect the company to continue to engage in short term financings during this early period of rapid growth, we believe it has sufficient resources and access to funding to meet its 2013-15 expansion goals.

ECONOMIC AND INDUSTRY DATA SUPPORT CONTINUED GROWTH

We also believe recent economic and industry data support continued growth. A key takeaway from the Bureau of Labor Statistics **June 2013 Jobs Report** is that the economy continues to shift towards temporary jobs in the current economic climate. The Bureau of Labor Statistics estimates that 28 million people are employed in part-time positions. Most of Labor Smart's customers are engaged in businesses such as construction, freight handling, landscaping, warehousing, janitorial, disaster response, light manufacturing, hospitality, retail or wholesale operations. They frequently require manual laborers for services such as hauling, cleaning, digging, loading and assembly.

Florida Attractive Market Moreover, the Qwik Staffing Solutions acquisition gave Labor Smart entry into the Florida market, which we believe is one of the most attractive markets for on demand labor. According to the Associated Press (AP), Florida, along with Texas, Arizona, California, and Colorado is experiencing a dramatic shortage of labor for the rebounding construction industry because so many workers exited the industry during the recession. AP notes that "many former skilled construction workers have moved on to other fields."[1] For Labor Smart customers in the hospitality industry, hotel occupancy rates through May 2013 in Orlando, Tampa and Jacksonville were up 1.8%, 1.6% and 3.6% respectively, according to Smith Travel. In metropolitan Orlando where Labor Smart operates a new branch, hotel occupancy of 68.8% was the highest overall rate since 2005. According to consulting firm HVS, "The Amway Center… has served as a catalyst for a number of new downtown development projects" in Orlando, including new hotels and the Orlando Magic's proposed sports and entertainment venue. We believe this bodes well for Labor Smart's continued growth in the region.

Orlando Occupancy Trends by Submarket

Rank	Submarket	2010	2011	2012
1	Lake Buena Vista*	71.7%	77.7%	76.1%
2	International Drive	65.6%	69.4%	70.5%
3	Orlando South	67.7%	70.0%	70.4%
4	Orlando Central	58.7%	61.5%	63.0%
5	Kissimmee East	54.2%	58.9%	62.4%
6	Orlando North	49.7%	53.1%	57.3%
7	Kissimmee West	46.2%	49.0%	55.2%
Total -Metro Orlando		64.5%	67.6%	68.8%

*Excluding Disney properties

Source: Visit Orlando, Smith Travel Research

[1] *US home construction is rebounding, but builders say they can't find enough qualified workers,* AP, May 10, 2013

VALUATION

Labor Smart Peer Analysis

Company	Ticker	7/17/2013 Price	52-Week High	52-Week Low	Revenue ($M) 2012A	Revenue ($M) 2013E	Revenue ($M) 2014E	EPS 2012A	EPS 2013E	EPS 2014E
Command Center, Inc.	CCNI	0.24	0.35	0.18	98	103	109	0.01	0.01	0.02
Insperity, Inc.	NSP	32.59	34.20	23.94	2,160	2,290	2,500	1.67	1.54	1.84
Kelly Services	KELYA	18.42	18.99	11.26	5,450	5,460	5,620	1.34	1.46	1.59
Kforce, Inc.	KFRC	15.50	16.65	10.34	1,080	1,120	1,210	0.85	0.85	1.04
Labor Smart	LTNC	0.27	0.82	0.10	7	16	31	(0.03)	(0.11)	(0.10)
Manpower Group	MAN	60.75	60.91	30.53	20,680	20,130	20,790	2.96	3.39	3.84
On Assignment	ASGN	29.80	30.40	14.50	1,240	1,650	1,800	1.03	1.10	1.36
Resources Connection*	RECN	12.67	13.68	10.58	556	574	590	0.53	0.61	0.74
Robert Half	RHI	35.05	37.75	25.10	4,110	4,250	4,610	1.55	1.80	2.09
TrueBlue, Inc.	TBI	23.36	23.82	11.84	1,390	1,640	1,760	0.84	1.00	1.27

	Mkt Cap ($M)	EV / Revenue			P/E		
Command Center, Inc.	14	0.1x	0.1x	0.1x	24.0x	24.0x	12.0x
Insperity, Inc.	833	0.4x	0.4x	0.3x	19.5x	21.2x	17.7x
Kelly Services	688	0.1x	0.1x	0.1x	13.7x	12.6x	11.6x
Kforce, Inc.	525	0.5x	0.5x	0.4x	18.2x	18.2x	14.9x
Labor Smart	5	0.7x	0.3x	0.2x	nm	nm	nm
Manpower Group	4,690	0.2x	0.2x	0.2x	20.5x	17.9x	15.8x
On Assignment	1,610	1.3x	1.0x	0.9x	28.9x	27.1x	21.9x
Resources Connection*	510	-	0.9x	0.9x	23.9x	20.8x	17.1x
Robert Half	4,820	1.2x	1.1x	1.0x	22.6x	19.5x	16.8x
TrueBlue, Inc.	812	0.6x	0.5x	0.5x	27.8	23.4	18.4

*FY ends May

Source: Company reports, Yahoo Finance, Zacks

In our view, True Blue and Command Center are direct competitors to Labor Smart in the on demand segment. There are also several other publically traded companies that provide the more traditional temporary staffing services. The shares of many of these companies have enjoyed strong price appreciation year-to-date on the back of economic drivers and the potential impact of the Affordable Care Act, despite its recent delay. We expect Labor Smart to benefit from these same exogenous drivers as it executes its expansion goals. Labor Smart is in the early stage of development and has yet to convert rapid revenue growth into net profits. However, we believe the company's revenue expansion and potential uplisting down the road could be catalysts for the shares. Our $0.80 price target equates to EV / projected 2014 revenue of 0.5X, which is in-line with True Blue.

RISKS

- The company is highly dependent on founder and CEO Ryan Schadel.
- Labor Smart is under capitalized and has significant funding needs for working capital and to support its growth. To-date, the company has engaged in short term financings but the cost or supply of capital could make it difficult for Labor Smart to fulfill its planned expansion.
- Given the rapid growth and the infrastructure that Labor Smart has built to fuel this growth, including hiring experienced operating leaders, the company has not yet converted strong revenue expansion into positive EPS at this early stage.
- Competition could increase. The temporary staffing industry is one with few barriers to entry, we believe. Thus, just as Labor Smart has entered as a new player, another company could also launch and complete with Labor Smart.
- Customers could shift towards hiring permanent employees instead of using temporary workers.
- Economic factors could constrain industry growth.
- A worker could get hurt when on assignment, although the company maintains workers' compensation insurance for its on demand workers to mitigate risk.

PROJECTED INCOME STATEMENT & BALANCE SHEET

Labor Smart, Inc.
Income Statement and Projections ($ Millions except per share data)

	1Q12	2Q12	3Q12		4Q12	2012	1Q13A	2Q13E	3Q13E	4Q13E	2013E	2014E
Revenues	**$1,183,716**	**$1,710,324**	**$2,152,243**		**$2,129,563**	**$7,175,846**	**$2,503,872**	**$4,037,439**	**$4,864,069**	**$4,685,039**	**$16,090,418**	**$30,571,795**
Cost of services	986,484	1,431,248	1,776,081		1,761,866	5,955,679	2,152,476	3,429,804	4,083,386	3,886,240	13,551,906	25,374,590
Gross Profit	**197,232**	**279,076**	**376,162**		**367,697**	**1,220,167**	**351,396**	**607,635**	**780,683**	**798,799**	**2,538,513**	**5,197,205**
Professional fees	9,650	4,210	25,000	E	2,271	41,131	62,500	61,875	61,256	60,644	246,275	184,706
Stock based compensation					210,600	210,600	250,616	248,110	245,629	243,172	987,527	1,540,542
Payroll expenses	68,565	93,061	184,081		203,664	549,371	160,076	322,995	437,766	374,803	1,295,640	2,338,742
Bad debt expense			62,104	E	2,214	64,318					-	
General and administrative	71,577	142,408	169,326		144,646	527,957	249,167	403,744	486,407	468,504	1,607,822	2,506,887
Loss on sale of receivables	7,147	40,222	51,751		27,201	126,321	35,522	35,877	36,236	36,598	144,234	145,676
Total operating expenses	156,939	279,901	492,262		590,596	1,519,698	757,881	1,072,601	1,267,294	1,183,721	4,281,498	6,716,554
Operating income/(loss)	40,293	(825)	(116,100)		(222,899)	(299,531)	(406,485)	(464,966)	(486,611)	(384,922)	(1,742,985)	(1,519,349)
Interest expense	(5,525)	(7,427)	(15,963)		(116,258)	(145,173)	(7,630)	(7,638)	(7,645)	(7,653)	(30,566)	(39,736)
Interest income					-		73	75	75	75	298	298
Financing costs			(2,526)		2,526		(233,746)	(23,375)	(23,398)	(23,421)	(303,940)	(304,244)
Realized loss on trading securities					(38)	(38)	(185)				(185)	
Other	-	-	-		(4,723)	(4,723)	(1,170)	(1,000)	(1,000)	(1,000)	(4,170)	(1,000)
Total other income (expenses)	(5,525)	(7,427)	(18,489)		(118,493)	(149,934)	(242,658)	(31,937)	(31,968)	(31,999)	(338,563)	(344,681)
Net income (loss) before taxes	34,768	(8,252)	(134,589)		(341,392)	(449,465)	(649,143)	(496,904)	(518,579)	(416,922)	(2,081,548)	(1,864,030)
Income tax expense	5,172	-	-		-	-	-	-	-	-	-	-
Net income (loss) after taxes	29,596	(8,252)	(134,589)		(341,392)	(449,465)	(649,143)	(496,904)	(518,579)	(416,922)	(2,081,548)	(1,864,030)
Unrealized gain on marketable securities		2,278	2,989		985	6,252	2,381	2,381	2,381	2,381	9,524	9,619
Comprehensive income (loss)	29,596	(5,974)	(131,600)		(340,407)	(443,213)	(646,762)	(494,523)	(516,198)	(414,541)	(2,072,024)	(1,854,411)
EPS or loss per share	**$0.00**	**($0.00)**	**($0.01)**		**($0.02)**	**($0.03)**	**($0.04)**	**($0.03)**	**($0.03)**	**($0.02)**	**($0.11)**	**($0.10)**
Average shares outstanding	16,045,000	16,045,000	16,328,424		16,756,244	16,293,667	18,029,377	18,029,378	18,029,379	18,029,380	18,029,379	18,029,379
Y/Y revenue growth (%)							112%	136%	126%	120%	124%	90%
Gross margin	16.7%	16.3%	17.5%		17.3%	17.0%	14.0%	15.1%	16.1%	17.1%	15.8%	17.0%
Payroll expenses % revenue	5.8%	5.4%	8.6%		9.6%	7.7%	6.4%	8.0%	9.0%	8.0%	8.1%	7.7%
G&A % revenue	6.0%	8.3%	7.9%		6.8%	7.4%	10.0%	10.0%	10.0%	10.0%	10.0%	8.2%

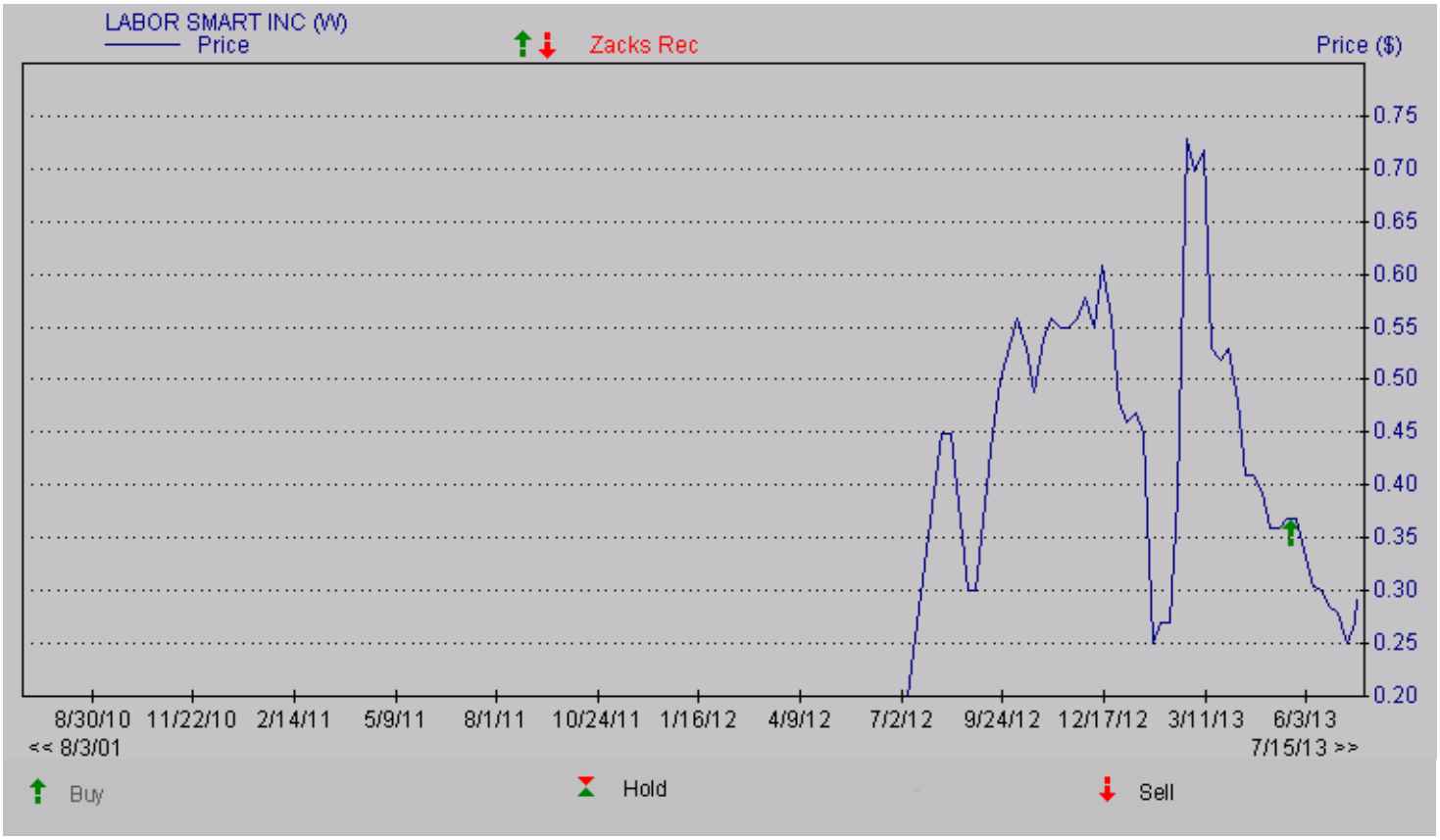
Source: Company reports, Zacks estimates

Labor Smart, Inc.
Balance Sheet and Projections ($)

	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13A	2Q13E	3Q13E	4Q13E
Cash	65,111	91,799	68,258	-	124,888	125,742	100,594	80,475	64,380
Accounts receivable	72,186	471,625	626,276	774,381	711,210	1,086,028	1,151,190	1,220,261	1,293,477
Prepaid expense	13,119	22,209	18,524	79,162	43,336	273,751	290,176	307,587	326,042
Deferred financing costs	-	-	-	138,264	83,634	122,029	97,623	78,099	62,479
Marketable securities	-	-	3,671	6,662	28,424	29,450	23,560	18,848	15,078
Other assets	2,384	25,724	44,336	44,101	34,552	49,270	39,416	31,533	25,226
Total current assets	152,800	611,357	761,065	1,042,570	1,026,044	1,686,270	1,702,559	1,736,802	1,786,682
Total assets	**152,800**	**611,357**	**761,065**	**1,042,570**	**1,026,044**	**1,686,270**	**1,702,559**	**1,736,802**	**1,786,682**
Accounts payable	2,499	9,897	11,706	19,657	844		675	540	432
Accrued liabilities	6,358	26,830	61,368	126,792	125,861	153,708	122,966	98,373	78,698
Notes payable-related party	100,000	310,000	300,000	250,000	219,375	180,247	153,210	130,228	110,694
Notes payable			-	-	15,160	10,106	8,085	6,468	5,174
Convertible notes payable net	-		-	52,160	184,355	332,989	266,391	213,113	170,490
Payroll taxes payable	25,691	213,225	319,711	380,872	579,400	824,125	881,814	943,541	1,009,589
Taxes payable		5,172	-	-	-	-	-	-	-
Other liabilities	7,185	5,570	32,975	33,843	-	-	121,341	226,078	316,835
Total current liabilities	141,733	570,694	725,760	863,324	1,124,995	1,501,175	1,554,483	1,618,341	1,691,913
Total liabilities	141,733	570,694	725,760	863,324	1,124,995	1,501,175	1,554,483	1,618,341	1,691,913
Total stockholder's equity	11,067	40,663	35,305	179,246	(98,951)	185,095	148,076	118,461	94,769
Total liabilities & stockholders' equity	**152,800**	**611,357**	**761,065**	**1,042,570**	**1,026,044**	**1,686,270**	**1,702,559**	**1,736,802**	**1,786,682**

Source: Company reports, Zacks SCR estimates

HISTORICAL ZACKS RECOMMENDATIONS



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