Zacks Small-Cap Research

May 23, 2013

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Labor Smart Inc (LTNC-OTCBB)

LTNC: *We Expect Positive Sector Dynamics to Enhance Labor Smart's Ambitious Growth Strategy. Initiating coverage with a Buy rating and $0.80 price target.*

Current Recommendation	**Buy**
Prior Recommendation	N/A
Date of Last Change	05/22/2013
Current Price (05/22/13)	$0.39
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 $15.5 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 initiate coverage of Labor Smart with an Outperform rating on the shares.

SUMMARY DATA

52-Week High	**$0.82**
52-Week Low	**$0.10**
One-Year Return (%)	**N/A**
Beta	**-10.60**
Average Daily Volume (sh)	**18,499**
Shares Outstanding (mil)	**19**
Market Capitalization ($mil)	**$7.6**
Short Interest Ratio (days)	**N/A**
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	3.763E	4.778E	4.472E	15.518E
2014					29.482E

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

- With a seasoned industry veteran at the helm, a strong operating team, an ambitious growth strategy and the tailwind of favorable sector dynamics, we believe Labor Smart has strong prospects in the on demand staffing industry. We initiate coverage with a Buy rating and $0.80 price target on the shares.
- Labor Smart is an emerging growth company that serves the on demand labor market, focusing primarily on blue-collar staffing positions. Since launching operations in 2011, Labor Smart has pursued an ambitious expansion strategy. 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 $15.5 million in 2013, up from only $0.16 million in 2011.
- Reflecting its dramatic footprint expansion, Labor Smart recently reported revenue of $2.5 million for the first quarter ending in March 2013, up from $1.183 million registered in the prior year first quarter. This equates to an impressive 112% increase
- The company intends to develop a national footprint over the next few years. Its growth strategy is to: 1) expand through new branch openings; 2) boost revenue as branches mature by broadening the range of staffing services they provide, and 3) leverage relationships with large regional or national customers to fill staffing needs across multiple verticals and multiple geographic markets.
- The temporary staffing industry is highly fragmented. A handful of global players such as Manpower and Kelly Services compete with a few national operators and myriads of small mom and pops. Few compete in the on demand niche in which Labor Smart operates and which is more specialized. Management believes its expanding footprint can provide a competitive advantage that can enable Labor Smart to leverage its marketing efforts and work with customers across several markets.
- While the industry has few barriers to entry, we believe that experience and relationships are crucial to the success of an on demand staffing organization. Labor Smart's founder and CEO has about 13 years of industry experience, the five district managers have a combined 65 years of operating experience and the company is assembling a strong, seasoned Board of Directors.
- Historically, the growth of the U.S. staffing industry has outpaced that of the general economy. Over the past 20 years, real GDP has averaged 2.5% per annum growth while the temporary staffing industry has averaged 4.8%. Several factors are likely to fuel continued industry growth, in our view, including the economic recovery and upcoming regulatory changes to the healthcare system. We also believe that economic uncertainty is likely to drive continued use of on demand staffing.
- The Affordable Care Act is generally expected to stimulate demand for temporary and on demand staffing. When the initiatives go into effect in 2014, companies that employ more than 50 full-time workers will need to provide healthcare coverage to them or pay penalties of up to $3,000.
- Given the favorable sector outlook, shares of larger companies in this sector[1] have appreciated by an average of 25% year-to-date versus +11.3% for the NASDAQ. Conversely, LTNC shares have declined 15%. We believe the company's continued revenue growth, as management executes its expansion initiatives, and a potential uplisting down the road could be catalysts for the shares.
- 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.

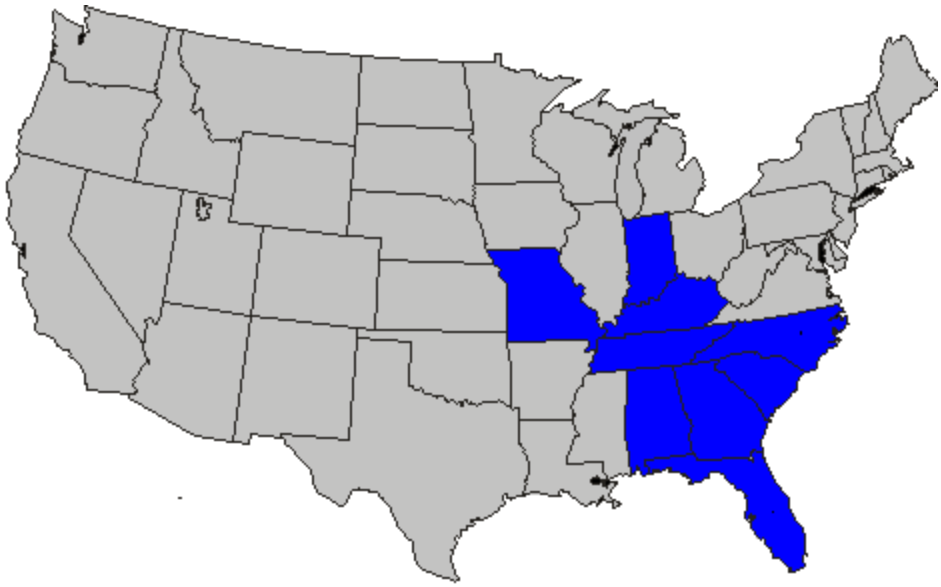
[1] These companies are: Kelly Services, Manpower Group, On Assignment and True Blue, Inc. The latter also made an acquisition during the period discussed.

OVERVIEW

Incorporated in May, 2011, Labor Smart, Inc. (LTNC-OTC BB) is an emerging growth company that serves the on-demand labor market, focusing primarily on companies that need blue-collar staffing positions filled on a temporary basis. The company supplies general laborers to the manufacturing, logistics, hospitality and warehousing industries, among others. Labor Smart also provides skilled workers to the commercial construction industry on an on-demand and temporary basis.

Since launching operations two years ago, Labor Smart has pursued an ambitious expansion strategy. The company started with two branch offices in November 2011 and has grown to 14 branch offices currently. Labor Smart now has branches in nine different states. Management expects to end 2013 with 18 to 20 offices in 12 states. Initially, the company's 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.

States in Which Labor Smart Operates Branches



Source: Company reports

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.

While most of the early growth has been through new branch openings, earlier this month the company acquired the operating assets of Qwik Staffing Solutions, a small staffing company based in Florida. This acquisition added three Florida branches located in Jacksonville, Orlando and Tampa. These new locations are expected to be immediately accretive to EBITDA. Based on their historical performance, management anticipates that they will contribute more than $3.2 million in revenue and roughly $350,000 in EBITDA over the next 12 months. These metrics imply that Labor Smart paid roughly 1.0X EBITDA. By comparison, competitor True Blue recently acquired MDT, one of the largest on demand staffing companies in the industry, and has indicated that it paid 4.0X EBITDA.

Half of the purchase price for Qwik Staffing Solutions 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.

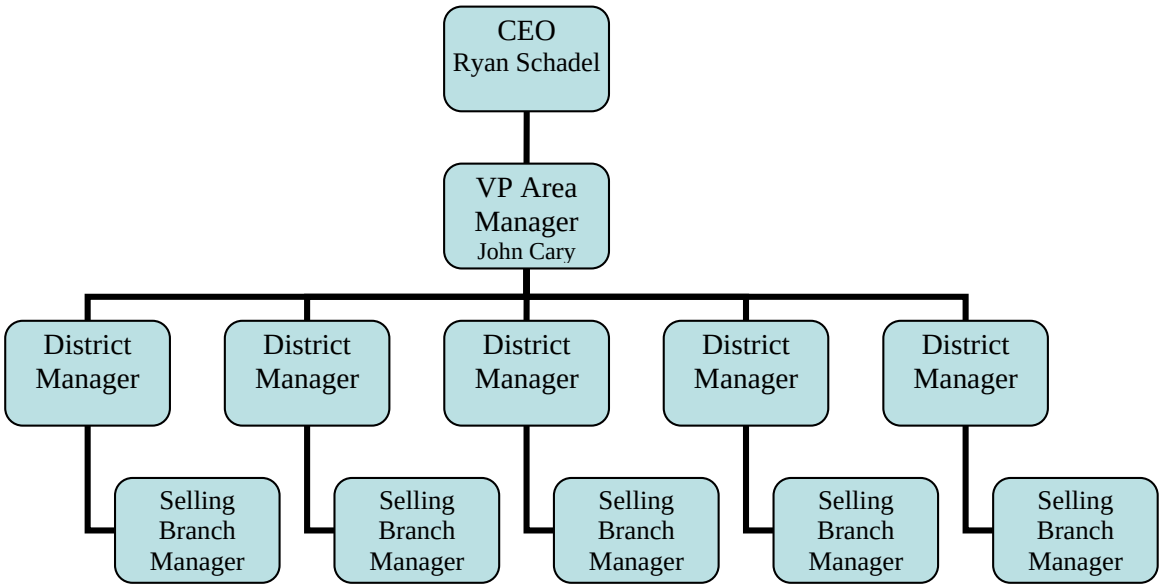
Florida an Attractive Market for On Demand Labor

However, we believe Qwik Staffing Solutions likely will meet or possibly exceed management's expectations. The 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."[2]

Team's Vast Experience Helping to Drive Growth

The acquisition also added an operating executive at the district manager level who will oversee the Florida operations. In all, Labor Smart now has five seasoned district managers who have a combined 65 years of experience in the temporary staffing industry. We believe this experience can help the company drive – and manage – its growth at this early stage and leverage the customer relationships the team has already established. Many of these managers came from larger competitors in the on demand staffing industry, likely attracted by the opportunity to build a newer, more aggressive platform, in our view.

Labor Smart Organizational Chart



Source: Company reports

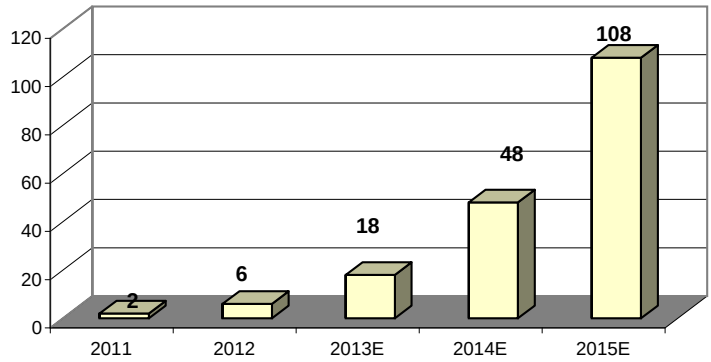
Moreover, whereas Qwik Staffing Solutions was primarily focused on the construction industry according to local media, Labor Smart is more diversified, with customers in a range of industries. Therefore, we believe that there are potential synergies to sell new services to existing Qwik Staffing Solutions clients, develop new clients and to service Labor Smart clients from other markets when they have projects or events in Florida that require on demand staffing.

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

GROWTH STRATEGY

Labor Smart's strategy is to drive revenue growth by: 1) opening new branches; 2) boosting revenue at existing branches as they mature by diversifying the services that they offer; and 3) leveraging customer relationships across markets.

Labor Smart's Growing Branch Network



Source: Company reports

Open New Branches

Labor Smart opened its first two branches in November 2011. The company expanded with four additional locations in 2012. Labor Smart operates 14 branches currently and is on-track, we believe, to meet or exceed its target of 18 to 20 in operation by year-end 2013. Labor Smart intends to open another 25 to 30 locations in 2014. Management's expansion plans imply a footprint of at least 108 branches by the end of 2015. Having initially focused on the southeast region, the company now has branch locations as far west as Kansas City, Missouri and plans to establish a nationwide presence over time.

Before opening a branch, management researches the market to determine how much demand exists for on demand labor. During this research process, the company also assesses how much competition already operates in the market and the availability of experienced people to manage the branch. It costs an estimated $7,000 to open a new branch. 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.

Boost Branch Revenue

A key aspect of Labor Smart's growth strategy is to broaden and diversify its customer base. 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. Therefore, their workforce needs fluctuate considerably. As the branch matures, the manager is expected to grow the customer base. Other industries that frequently turn to on demand staffing to fill their workforce needs include hospitality, warehousing, manufacturing, logistics and events, among other things. For example, when hotel occupancy rates spike during peak seasons or holidays, hotels often add workers on a short term basis. In addition, the company tries to generate sales with existing customers in new verticals. Using the hospitality industry as an example again, Labor Smart could supply temporary workers for housekeeping or service positions during peak occupancy periods, as noted, and skilled workers when the hotel is doing light maintenance construction.

Leverage Customer Relationships

The temporary staffing industry is highly fragmented. A handful of global players such as Manpower and Kelly Services compete with a few national operators and myriads of small mom and pops. **Few compete in the on demand niche in which Labor Smart operates and which is more specialized**. Management believes its expanding footprint can provide a competitive advantage that can enable Labor Smart to leverage its marketing efforts and work with customers across several verticals and several markets. As its footprint expands, the company can complement marketing efforts done at the branch level with regional and potentially even national marketing campaigns.

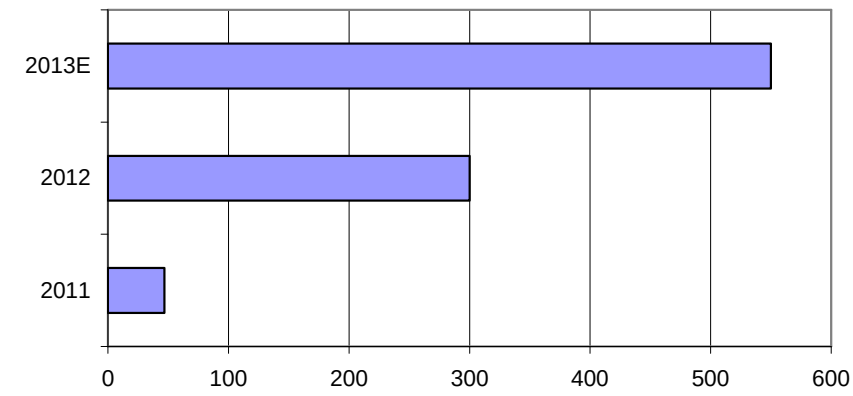
While the industry has few barriers to entry, we believe that experience and relationships are crucial to the success of an on demand staffing organization. Labor Smart's founder and CEO has about 13 years of industry experience, the five district managers have a combined 65 years of operating experience and the company is assembling a strong, seasoned Board of Directors. Key factors to obtain and retain customers, according to management, are: 1) cost of services, 2) quality of the on demand workforce and 3) timely and efficient response to customers' needs. Management also believes that once it can service larger customers nationally, it may attain greater pricing power.

BRANCH ECONOMICS

Before a new branch office opens, management researches the local market to determine the need for temporary and on demand labor, as noted. Then Labor Smart recruits an experienced person to manage the branch and enrolls that person in a two-week training session. Each branch generally also has a customer service representative or account executive in addition to the branch manager.

Each branch manages its own sales and marketing efforts, with the branch manager having primary responsibility for securing new customers. In fact, branch managers are given the title *Selling Branch Manager*, which conveys the importance of securing and retaining customers as a key aspect of the job. The company expects branch managers to contact some 125-200 potential customers each week. This tactic has helped fuel significant growth in the customer base. In 2011, Labor Smart had 47 customers. In November 2012, the company announced that its customer base exceeded 300 and we estimate that it is closer to 500 or more now. Revenue growth is highly correlated to the expansion of the customer base, in our opinion.

Labor Smart's Growing Customer Base



Source: Company reports, Zacks estimates

As Labor Smart continues to expand, new branches can leverage the base of regional and national customers that have already done business with a different branch. For example, a branch manager in Tampa can introduce the Tampa branch to a customer that has used Labor Smart services in Chattanooga and leverage that existing corporate relationship. We believe that during employee training, management stresses customer service as a key to customer retention.

Because the research and trainings process occurs before the branch opens, management expects a location to generate revenue early on. Branches average weekly operating expenses of roughly $3,000, excluding wages, taxes, and workers compensation costs. In addition, the company targets a 28% gross margin at the branch level. These metrics imply that a branch needs to reach roughly $11,000 in weekly revenue to become profitable, according to management.

Labor Smart Estimated Weekly Branch P&L	
Weekly revenue to reach profitability	$11,000
Estimated payout to on demand workers	$7,920
Targeted gross margin	28%
Weekly operating costs	$3,000
Estimated branch profit	$80

Source: Company reports, Zacks SCR estimates

People seeking work apply to a Labor Smart branch office to secure temporary placement. If their skills match a customer's needs, they are assigned to a job or project. Generally, it is the branch manager who conducts this matching process. The branch manager also makes sure that the temporary worker has the appropriate equipment he or she needs for the assignment, placing particular emphasis on any safety equipment needed. Many customers request workers in advance. Some assignments, however, are requested on short notice and Labor Smart seeks to fill those on demand. This on demand segment of the temporary staffing industry is more specialized than traditional placement.

INDUSTRY OUTLOOK

Our outlook for the temporary and on demand staffing industry is positive. The temporary staffing industry began in the boom years following World War II. In 1946, William Russell Kelly launched Russell Kelly Office Service in Detroit with three employees and 12 customers. Kelly offered to pick up typing work from customers and have his staff complete the work at his office. Over time, he conceived the idea of dispatching clerical help to work on-site temporarily at customers' offices, generally for short or last-minute assignments. Thus, the temporary staffing industry developed to meet businesses' needs for flexible staffing.

Russell Kelly Office Service changed its name to Kelly Girl Service, Inc. in 1957 to reflect that the majority of assignments it filled were secretarial. Not only was demand primarily for secretarial assistance, but a growing number of women wanted flexible options to work part-time outside of the home. Over time, Kelly Girl Service expanded the types of services its temporary staff could do and also began to find temporary assignments for a growing number of men.

In 1966 the company changed its name to Kelly Services. Manpower Inc. was founded a year after Russell Kelly Office Service in Milwaukee by two attorneys: Aaron Scheinfeld and Elmer Winter.

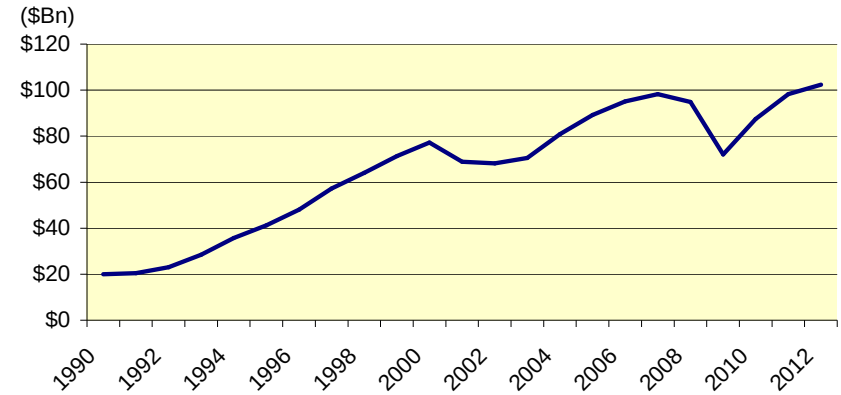
Key Drivers

Demand for temporary services is highly correlated to the economy and to the labor markets. Not surprisingly, during periods of economic growth, demand for temporary services tends to rise. Conversely, during economic downturns, demand for temporary labor slows. Historically the U.S. staffing industry has grown faster than the general economy. Over the past 20 years, for example, real GDP has averaged 2.5% growth per annum while temporary and contract staffing employment has averaged 4.8% growth per annum.

During this current economic recovery, the industry has enjoyed solid growth. Interestingly, since the recent recession ended, the U.S. staffing and recruiting industry has created more jobs than any other single industry in America, according to BLS (the Bureau of Labor Statistics). From June 2009 to July 2012, staffing companies added more than 786,000 jobs. To put that metric in context, BLS estimates that the entire healthcare sector, which represents nearly 11% of the U.S. nonfarm work force, added 829,000 jobs during the same period including hospitals, private physician offices, nursing homes, HOPDs (hospital outpatient departments), etc.

This outperformance is consistent with historical trends. In the early stages of an economic recovery, companies first look to temporary and contract workers to help meet growing demand. This explains the rapid uptick in staffing employment since the recession ended. Nevertheless, the growth the domestic staffing industry has experienced in this recovery has been more robust than it was following the previous two recessions that ended in 2001 and 1991, respectively. According to the ASA (American Staffing Association), staffing employment grew 4.1% in 2012, as U.S. staffing companies employed an average of 2.9 million temporary and contract workers per day that year. The fourth quarter of 2012 marked the twelfth consecutive quarter of year-over-year staffing job growth since the end of the recession, according to ASA.

Temporary and Contract Staffing Sales



Source: American Staffing Association

Despite robust growth over the past three years, U.S. staffing industry employment has not recovered all of the jobs lost during the recession. ASA data illustrates that domestic staffing firms lost nearly 1.2 million jobs during the recession, which equates to 36% of the temporary and contract work force. According to the ASA, the industry is still nearly 250,000 people short of its pre-recession work force. Moreover, the temporary staffing industry still accounts for less than 2% of total domestic jobs, according to BLS data. We believe this implies continued room for growth, as this metric has exceeded 2% in prior years.

We believe there are several factors that will drive continued sector growth. These include cyclicality and seasonality that characterize many industries, growing demand for flexibility by both employers and employees, the uncertain economic outlook and the pending impact of the Affordable Care Act.

Cyclicality The on-demand labor industry helps firms that need flexible staffing options. Many businesses operate in a cyclical environment and need to add workers during periods of peak production or activity. In addition, many companies also need to temporarily replace full-time employees who are absent for short periods because illness, vacation or other factors. On-demand labor offers employers a flexible option to meet their labor needs without having to add full time employees.

Seasonality Some businesses, such as construction, are generally seasonal because of factors such as weather. These businesses often turn to temporary or on demand staffing to help with short term staffing needs. Labor Smart focuses on the commercial construction industry during its initial outreach to obtain potential customers when it opens a new branch.

Cost containment Competitive pressures have prompted many businesses to reduce costs, which sometimes translates into reduction of full time employees. On demand staffing allows companies to add workers as needed without having to employ people on a full time basis.

The Affordable Care Act President Obama's healthcare initiatives are generally expected to drive demand for temporary and on demand staffing. When these initiatives go into effect in 2014, companies that employ more than 50 full-time workers will need to provide health care coverage to them or pay penalties of up to $3,000. According to an article in the *Washington Post*, "By requiring employer coverage only for those who put in at least 30 hours a week, the act appears to create an incentive for companies to do less with permanent workers and more with part-timers, which are the main focus of staffing agencies."

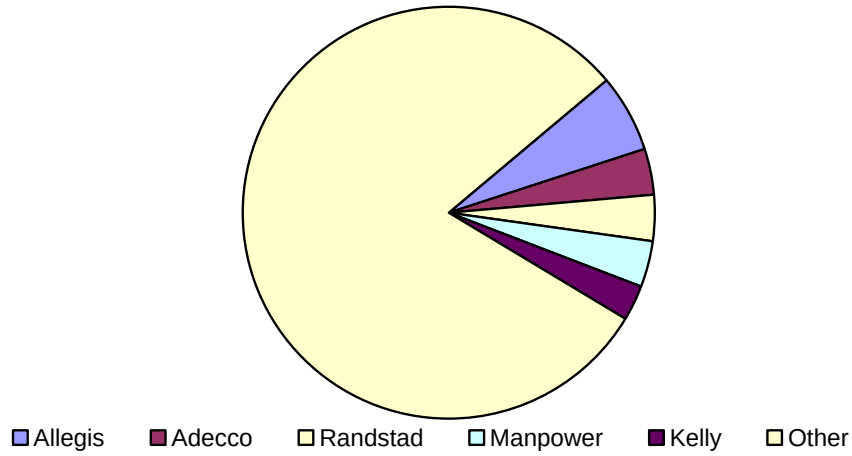
Driven by these factors, particularly by the impact of pending regulatory changes to the healthcare system, temporary staffing is generally expected to continue to outpace general economic growth. Staffing Industry Analysts projects that staffing industry revenue will grow by 6% per annum over 2013-14. **Labor Smart operates in a highly specialized niche within this industry (see below) and we believe it will benefit from these economic and structural tailwinds.**

COMPETITION

The temporary staffing industry is highly fragmented. As illustrated in the figure below, the top five competitors account for only about 20% of total industry revenue, according to Staffing Industry Analysts data. A handful of global players such as Manpower and Kelly Services compete with approximately 100 companies that operate nationally and myriads of small mom and pop local companies. Very few of these companies compete in the on demand sector in which Labor Smart operates. We believe the company's primary direct competitors in the on demand space are True Blue, Command Center and privately held Labor Finders, as well as mom and pops.

The industry has and continues to develop specialized market segments to match customers' needs. One example would be Kelly Services, which started by placing temporary secretarial help and expanded to place other types of temporary workers, as mentioned. Robert Half began with a focus on placing workers with accounting or financial skills.

Temporary Staffing Industry is Highly Fragmented



Source: Staffing Industry Analysts

In general, these agencies fulfill requests for temporary workers that customers place in advance. Conversely, Labor Smart specializes in placing skilled and unskilled workers on-demand. Customers frequently call a Labor Smart branch to request that a worker be dispatched in a matter of hours and Labor Smart branch managers reach out to the pool of temporary workers to fill the request. This is a specialized niche within the temporary staffing sector in which few – if any – of the larger players compete.

VALUATION

As noted, only True Blue and Command Center are true direct competitors to Labor Smart in the on demand segment, in our view, but there are 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. We expect Labor Smart to benefit from these same exogenous drivers as it executes its expansion plans. 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 could be a catalyst for the shares. Our $0.80 price target equates to EV / projected 2014 revenue of 0.5X, which is in-line with True Blue.

Labor Smart Peer Analysis

Company	Ticker	5/22/2013 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	0.21	0.45	0.18	98	103	109	0.01	0.01	$0.02
Insperity, Inc.	NSP	30.70	34.20	23.94	2,160	2,290	2,500	1.67	1.54	1.84
Kelly Services	KELYA	17.31	18.99	11.26	5,450	5,490	5,650	1.34	1.46	1.60
Kforce, Inc.	KFRC	14.86	16.65	10.34	1,080	1,120	1,210	0.85	0.85	1.04
Labor Smart	LTNC	0.39	0.82	0.10	7	16	29	($0.03)	($0.11)	($0.10)
Manpower Group	MAN	58.23	57.75	30.53	20,680	20,150	20,830	2.96	3.38	3.84
On Assignment	ASGN	26.50	26.91	14.48	1,240	1,650	1,800	1.03	1.10	1.34
Resources Connection*	RECN	11.08	13.68	10.58	-	558	581	0.48	0.51	0.64
Robert Half	RHI	35.27	37.75	25.10	4,110	4,250	4,610	1.55	1.80	2.08
TrueBlue, Inc.	TBI	23.00	22.40	11.84	1,390	1,640	1,760	0.84	0.99	1.27

	Shr Price YTD (%)	Mkt Cap ($M)	EV / Revenue 2012A	EV / Revenue 2013E	EV / Revenue 2014E	P/E 2012A	P/E 2013E	P/E 2014E
Command Center, Inc.	-16%	12	0.1x	0.1x	0.1x	21.0x	21.0x	10.5x
Insperity, Inc.	-6%	776	0.4x	0.3x	0.3x	18.4x	19.9x	16.7x
Kelly Services	8%	639	0.1x	0.1x	0.1x	12.9x	11.9x	10.8x
Kforce, Inc.	2%	506	0.5x	0.5x	0.4x	17.5x	17.5x	14.3x
Labor Smart	-15%	7	1.0x	0.5x	0.2x	nm	nm	nm
Manpower Group	34%	4,410	0.2x	0.2x	0.2x	19.7x	17.2x	15.2x
On Assignment	20%	1,400	1.1x	0.8x	0.8x	25.7x	24.1x	19.8x
Resources Connection*	-8%	451	-	0.8x	0.8x	23.1x	21.7x	17.3x
Robert Half	-3%	4,780	1.2x	1.1x	1.0x	22.8x	19.6x	17.0x
TrueBlue, Inc.	39%	901	0.6x	0.5x	0.5x	27.4	23.2	18.1

*FY ends May
Source: Company reports, Yahoo Finance, Zacks SCR

MANAGEMENT

CEO Has Extensive Industry Experience

Labor Smart founder Ryan Schadel is the company's President and CEO. He has about 13 years of experience in the temporary staffing industry, having begun his career in the industry in January 2000 as a sales representative with a national temporary staffing company. From 2008 to November 1, 2011, Mr. Schadel was CEO of recruiting firm Staff Smart Concepts, Inc. Prior to that, he left the temporary staffing industry for a short period and was a vice president with a real estate investment firm, The Connor Group, from November 2007 to August 2008. From September 2006 to September 2007 Mr. Schadel was District Manager with WTS, Inc. a blue collar staffing services company.

As Does the Area Vice President …

In November 2012, the company hired John Cary III, an industry veteran with roughly 14 years of experience, as its new Area Vice President. Prior to joining Labor Smart, he was a senior manager at competitor True Blue for over 10 years. His role at Labor Smart is to oversee the District Managers as Labor Smart drives branch and district expansion.

… And the District Managers

Earlier this year, Labor Smart hired Brian Middleton to head regional operations in Missouri, where the company currently operates one branch. We believe Labor Smart intends to expand its operations in this region over time and Mr. Middleton will help supervise that operation. He has over 12 years of industry experience with True Blue. When he left True Blue, he had attained the level of Regional Vice President.

Board Also Gets Stronger With New Directors

We view Labor Smart's recent initiatives to expand and strengthen its board of directors favorably. On February 21, 2013, Labor Smart elected Matthew Rodgers to its Board. From 1998 until 2003, he was Executive Vice President and COO of Labor Ready, a subsidiary of True Blue. Subsequently from 2003 until 2012, Mr. Rodgers was the President and CEO of Interim Healthcare Staffing. He was also President of privately held employment screening firm iprospectcheck.com, which is based in Folsom, California.

On March 8, 2013, Ms. Shannan Manix was elected to Labor Smart's Board of Directors. She is the Director of Sales and National accounts at Payscale, an online salary, benefits and compensation information company. Prior to Payscale, she was a Regional Vice President at Labor Ready, where she worked from 1998 to 2012.

FINANCIAL HISTORY

Recent Results, 1Q13 Summary

Labor Smart recently reported results for the first quarter ending in March 2013. Revenue of $2,503,872 was up from $1,183,716 registered in the first quarter ending in March 2012. This equates to an impressive 112% increase versus the prior year, as the branch footprint and customer base continue to expand.

The company recently announced that it had achieved revenue of $1.0 million for the month of April 2013 versus $0.52 million in April 2012. This represents a 94.6% year-over-year increase and further illustrates, we believe, the momentum that Labor Smart enjoys. Management has provided guidance for 2013 revenues of $15.5 million. Given the growth illustrated in the first quarter of 2013, as well as in April, and the consolidation of Qwik Staffing Solutions, we believe the company can attain or possibly exceed this goal.

The company registered an operating loss of $406,485 for the first quarter ending in March 2013, as total operating costs increased by 383%. This included a 548% rise in Professional fees. Much of that is related to the use of outside consulting to help staff new branches. Over time, as the company grows and scales, we believe management's plan is to take this function in-house, which likely will mitigate Professional fees considerably. Moreover, two noncash expenses, Stock based compensation and Loss on sale of receivables, also contributed to the significant year-over-year rise in total operating costs. Excluding these, we estimate that the operating loss would have been roughly $120,000. Below the operating line, the company recorded Financing costs of $233,746, another noncash item that primarily relates to the valuation of warrants. Excluding the noncash expenses, we estimate that Labor Smart registered a net loss of about $127,000 in the first quarter ended March 31, 2013. On a GAAP basis, the company's net loss came in at $646,762.

RECENT NEWS

On April 12, 2013, Labor Smart entered into an agreement with Intelliace Group for the sale of $400,000 of debentures. The company cancelled the agreement on April 26, 2013 when Intelliace did not fund the first debenture. Intelliace returned the shares that Labor Smart had issued pursuant to the agreement. Subsequently on April 25, 2013, Labor Smart entered into a shareholder loan agreement with CEO Ryan Schadel. He agreed to refinance his original loans and accrued interest, which were in default, into a new interest free loan that is due on demand.

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 maintain 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. The company maintains workers' compensation insurance for its on demand workers and stresses safety, focusing on prevention. Management believes this will help control long term worker's compensation costs and mitigate risk.

INSIDER OWNERSHIP

Ryan Schadel holds about 78% of LTNC shares, which we believe aligns his interests with those of public shareholders. The company has been able to attract a number of fairly senior people to its team and to its Board. These people are highly incentivized to help the company grow and attain profitability, we believe, through bonus payouts and share compensation.

PROJECTED INCOME STATEMENT & BALANCE SHEET

Labor Smart, Inc.
Income Statement and Projections ($)

	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**	**$3,762,713**	**$4,777,979**	**$4,472,082**	**$15,516,647**	**$29,481,628**
Cost of services	986,484	1,431,248	1,776,081		1,761,866	5,955,679	2,152,476	3,198,306	4,013,503	3,711,828	13,076,113	24,322,343
Gross Profit	**197,232**	**279,076**	**376,162**		**367,697**	**1,220,167**	**351,396**	**564,407**	**764,477**	**760,254**	**2,440,534**	**5,159,285**
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 comp					210,600	210,600	250,616	248,110	245,629	243,172	987,527	1,580,043
Payroll expenses	68,565	93,061	184,081		203,664	549,371	160,076	301,017	430,018	357,767	1,248,878	2,270,085
Bad debt expense			62,104	E	2,214	64,318					-	
G&A	71,577	142,408	169,326		144,646	527,957	249,167	376,271	477,798	447,208	1,550,444	2,505,938
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	1,023,150	1,250,937	1,145,389	4,177,358	6,686,449
							548%					
Operating income/(loss)	40,293	(825)	(116,100)		(222,899)	(299,531)	(406,485)	(458,743)	(486,460)	(385,135)	(1,736,824)	(1,527,164)
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)	(243,152)
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 inc (exp)	(5,525)	(7,427)	(18,489)		(118,493)	(149,934)	(242,658)	(31,937)	(31,968)	(31,999)	(338,563)	(283,589)
Net before taxes	34,768	(8,252)	(134,589)		(341,392)	(449,465)	(649,143)	(490,681)	(518,429)	(417,135)	(2,075,387)	(1,810,753)
Income tax expense	5,172	-	-		-	-	-	-	-	-	-	-
Net income (loss) after taxe	29,596	(8,252)	(134,589)		(341,392)	(449,465)	(649,143)	(490,681)	(518,429)	(417,135)	(2,075,387)	(1,810,753)
Unrealized gain on marketable securities		2,278	2,989		985	6,252	2,381	2,381	2,381	2,381	9,524	9,810
Comprehensive inc (loss)	29,596	(5,974)	(131,600)		(340,407)	(443,213)	(646,762)	(488,300)	(516,048)	(414,754)	(2,065,863)	(1,800,944)
											-	
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)**
											-	
Avg 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
Gross margin	16.7%	16.3%	17.5%		17.3%	17.0%	14.0%	15.0%	16.0%	17.0%	15.7%	17.5%
Payroll expenses % revenu	5.8%	5.4%	8.6%		9.6%	7.7%	6.4%	8.0%	9.0%	8.0%	8.0%	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%	8.5%
Y/y revenue increase (%)							111.5%	120.0%	122.0%	110.0%	116.2%	90.0%

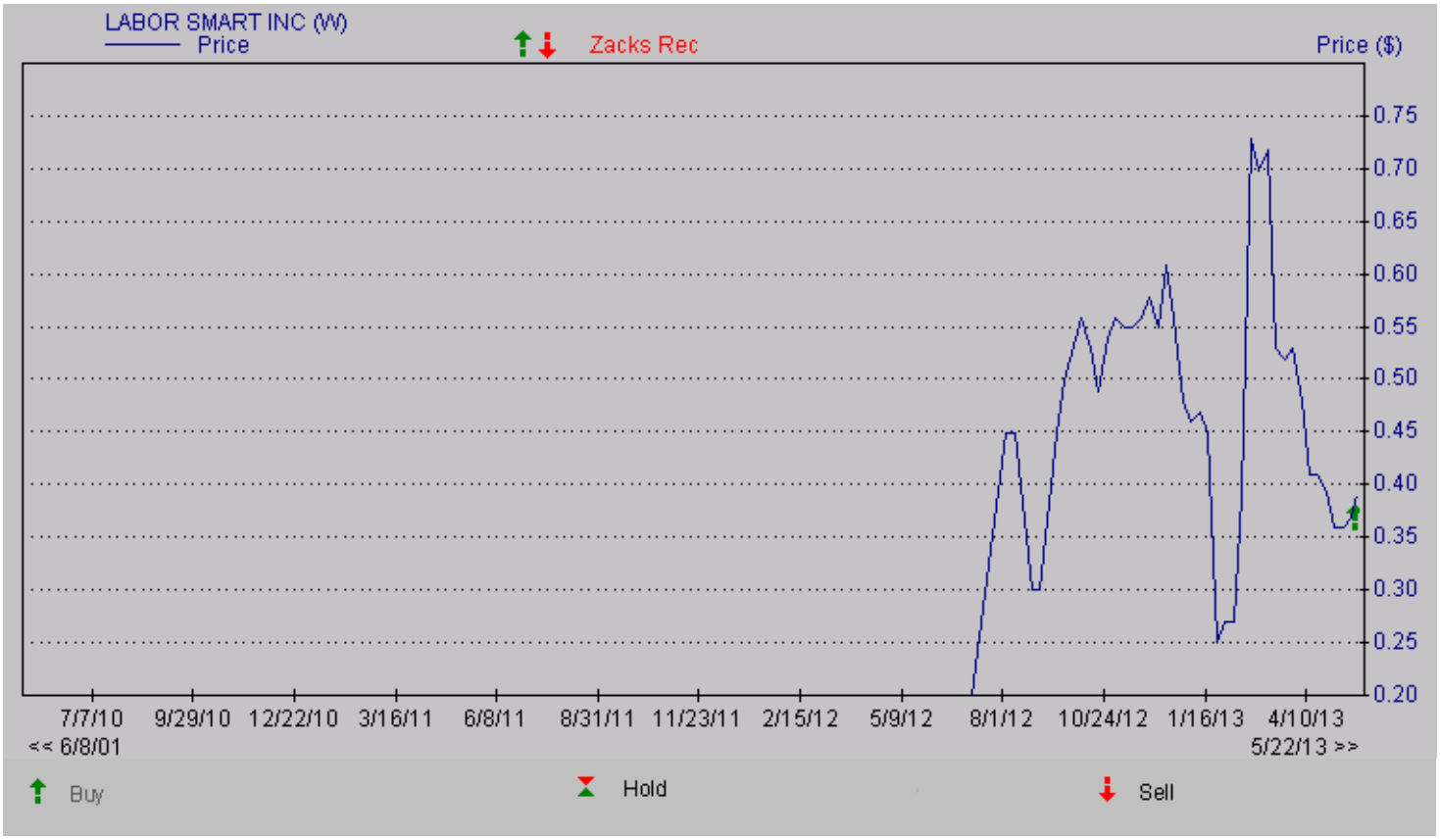
Source: Company reports, Zacks SCR estimates

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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