Trickle Research

Every raging river, every great lake, every deep blue sea starts … with a trickle

Earnings Update: Q1-Fiscal 2018

Report Date: 05/15/18

12- 24 month Price Target (split adjusted): $.9.60

Allocation: 4

Closing Stock Price at Initiation (Split Adjusted Close 09/08/17): $4.44

Closing Stock Price (Close 05/15/18): $5.75

Command Center, Inc.

(OTC Stock Symbol: CCNI)

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Command Center ("CCNI") reported a bit of a mixed bag for Q1 Fiscal 2018 (ended March 30,2018). They missed our revenue estimate by about $1.3 million or about 5% ($22.47 million vs. $23.78 million) and they reflected a net loss of $1.22 million versus our estimate of a gain of $391,000.

Revenues were essentially flat to slightly higher for the year-over-year quarterly comp. The Company attributed the flat revenue comparison to some national account projects that positively impacted 2017 versus 2018. We're not sure what to make of that, on the other hand, lumpy revenue items are not exactly atypical in the microcap space, so its not particularly surprising. That sort of lacking visibility is what causes us to use higher discount rates when we boil down our DCF based price targets. To that end, we have made a few adjustments to our forward revenue assumptions in the model (which we will address further) but for the most part, we remain comfortable with our basic revenue assumptions going forward despite the small miss.

The earnings miss was more extraordinary. The largest item was a $1.54 million charge related to the bankruptcy/liquidation of a prior workman's compensation insurance carrier; Freestone Insurance Company. In short and as we understand it, in the past Freestone required collateral deposits from CCNI as a provision of their workman's compensation insurance. in prior reporting periods, the Company's (legal) position regarding Freestone's bankruptcy/liquidation was that they were not ordinary creditors, and therefore should be afforded priority in the liquidation. After further consideration, the Company has obviously decided to write the assets down, and the $1.54 million represents that charge. We think they likely decided the resources required to fight in the context of the probability of a positive outcome were not congruent. Secondly, The Company noted on the call that they also took an additional one-time charge related to the severance/replacement of CEO Bubba Sanford. Frankly we need a bit of clarity on that line item because the 10Q suggests the amount was higher than their math implies. The point is, absent these items SG&A came in about $170,000 lower than our estimate once we adjusted for the revenue mix. They have in our view always done a good job of managing costs.

To net this out, when we adjust for the items above, we estimate that they would have reflected EPS of about $.05 versus our estimate of about $.08. Further, that suggests that without the extraordinary charges, EPS would have improved by about $.01 per share. While the revenue miss was a bit disappointing, we are not making any stark changes to our model (which we think included some modest assumptions to start with) except for a more favorable tax rate, which we still need to ascertain. We will be sitting down with management next week and that is on our list.

Looking ahead, we have had an opportunity to meet new CEO Rick Coleman, as he was gracious enough to present at our recent conference even though he was still trying to get situated. We are not going to delve into the management change other than to say that our sense is that Rick appears to be a suitable replacement and seems up to the task. That task will include trying to find ways to grow the business, which will (still) include organic growth, new branch starts and potential acquisitions. It is not an easy task by the way, although we believe it can be done or we would not be covering the name. We continue to believe opportunities exist across all three endeavors. Moreover, we also continue to think there is considerable leverage in the operating model such that modest increases in revenues should lead to greater marginal increases in net income.

Secondly, we are encouraged by the settlement of the disagreements between management and certain shareholders. Again, without getting in the middle of the merits of either side, (which we are not in a position to address even if we were inclined), the fact that it is in the rear-view mirror is clearly a positive. There is no question that it has been a distraction, although there is no way to quantify that, and we think.

Lastly, we remain steadfast in our view that CCNI is undervalued at current levels. The stock trades at a discount to most notable metrics of its industry peers (although most of those are considerably larger, which may compromise the relevance of such comparisons) but it also trades at discounts to broad equity market valuations as well. Further, we have applied discounts to our DCF derived targets that we tend to believe exceed their effective cost of capital. That is, if they can continue to perform in line with our expectations, we are comfortable that related intrinsic values will likely reflect levels *beyond* our current target. Clearly the Company concurs with that assessment as they continue to purchase shares in the open market under their share repurchase plan. As we have noted in the past, the Company has disclosed that they have established a strategic alternatives committee amongst the board, which tells us they are actively seeking additional ways to more fully realize the valuation discounts we suspect here. As we have noted in some of the prior research, we continue to believe that an acquisition of the Company by a competitor or other strategic entity may be the optimal endgame here. We would add, the strategic alternative committee has engaged an investment banker to assist with their "alternatives" search.

We reiterate our allocation of 4, and our 12-24 month target of $9.60 as we look forward to assessing the new leadership's approach to what we think is a solid base of business around a .

Projected Operating Model

Income Statement						
Projected Operating Statement						
Command Center, Inc.						
By: Trickle Research LLC	(actual)	(estimate)	(estimate)	(estimate)	(estimate)	(estimate)
	3/30/18	**6/29/18**	**9/28/18**	**12/28/18**	**Fiscal 2018**	**Fiscal 2019**
Revenue	$ 22,467,398	$ 25,635,150	$ 27,363,150	$ 25,029,200	$ 100,494,898	$ 106,373,046
Cost of staffing services	$ 16,873,331	$ 19,095,232	$ 20,231,192	$ 18,797,969	$ 74,997,725	$ 79,578,952
Gross Profit	$ 5,594,067	$ 6,539,918	$ 7,131,958	$ 6,231,231	$ 25,497,174	$ 26,794,094
Selling, general, and administrative expenses	$ 7,213,620	$ 5,382,570	$ 5,648,210	$ 5,444,796	$ 23,689,195	$ 22,751,136
Depreciation and amortization	$ 92,591	$ 92,665	$ 90,692	$ 88,762	$ 364,710	$ 336,551
Income from operations	$ (1,712,143)	$ 1,064,683	$ 1,393,056	$ 697,673	$ 1,443,269	$ 3,706,408
Interest expense and other financing expense	$ 2,163	$ -	$ -	$ -	$ 2,163	$ 0
Impairment of goodwill	$ -	$ -	$ -	$ -	$ 0	$ 0
Change in fair value of derivative liability	$ -	$ -	$ -	$ -	$ 0	$ 0
Net income before income taxes	$ (1,714,306)	$ 1,064,683	$ 1,393,056	$ 697,673	$ 1,441,106	$ 3,706,408
Provision for income taxes	$ (496,618)	$ 266,171	$ 348,264	$ 174,418	$ 292,235	$ 926,602
Net Income	$ (1,217,688)	$ 798,513	$ 1,044,792	$ 523,255	$ 1,148,871	$ 2,779,806
Earnings per share:						
Basic	$ (0.24)	$ 0.16	$ 0.21	$ 0.11	$ 0.23	$ 0.56
Diluted	$ (0.20)	$ 0.16	$ 0.21	$ 0.10	$ 0.22	$ 0.54
Weighted average shares outstanding:						
Basic	$ 4,983,157	$ 4,977,690	$ 4,971,937	$ 4,965,730	4,974,628	4,952,091
Diluted	$ 5,968,762	$ 5,079,030	$ 5,091,060	$ 5,101,320	5,310,043	5,123,076

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Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals $250) and 10 representing 10 investment units or $2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit $25,000 to buying micro-cap stocks, that would assume an investment of $1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to perhaps add another 5 of the names from our profiles). We generally start initial coverage stocks with an allocation of 4. Thus, at $1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same $250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting $1000 into the position ($250 * 4). If we later raise the allocation to 6, you might consider adding two additional units or $500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

A Trickle rating of 1 thru 3 would best correspond to a "Speculative Buy" although we would caution that a rating in that range should not assume that the stock is necessarily riskier than a stock with a higher rating. It may carry a lower rating because the stock is trading closer to a price target we are unwilling to raise at that point. This by the way applies to all of our ratings.

A Trickle rating of 4 thru 6 might best (although not perfectly) correspond to a standard "Buy" rating.

A Trickle rating of 7 thru 10 would best correspond to a "Strong Buy" however, ratings at the higher end of that range would indicate something that we deem as quite extraordinary..... an "Extreme Buy" if you will. You will not see a lot of these.