Trickle Research

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

Price Target Increase

HIREQUEST™

HireQuest, Inc.

(Nasdaq Symbol: HQI)

Report Date: 04/20/21

Allocation: 4

12- 24 month Price Target (split adjusted): * $23.00

Closing Stock Price at Initiation (Split Adjusted Close 9/08/17): $4.44
Closing Stock Price at Allocation Increase (Close 11/13/18): $3.88
Closing Stock Price at Price Targe Increase (Close 10/05/20): $7.73
Closing Stock Price at Price Target Update (Close 02/08/21): $13.15
Closing Price at Price Target Update and Allocation Downgrade (Close 02/16/21): $14.84
Closing Price at Price Target Increase (Close 04/19/20): $19.48

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HireQuest reported Fiscal 2020 results a few weeks ago, but we did not get around to updating those as they were largely in line with our estimates. Specifically, revenues were $13.8 million versus our estimate of $13.9 million. Operating Income was $4.98 million versus our estimate of $5.18 million, and Net Income was $5.36 million versus our estimate of $5.08 million. The net income difference was related to Miscellaneous Income. All told as we noted, the numbers were in line with our estimates, and were quite favorable in that despite the pandemic, the Company posted fully diluted earnings of $.39 for the year, and they ended the year with just under $14 million in cash.

The above noted, since the release of the year end numbers, HQI's shares have (once again) breached our upgraded 12-24 month price target ($20 per share), so we need to address that.

Just to recap, HireQuest has made two major acquisitions since the beginning of 2021. Readers can refer to the two updates we provided around each of those acquisitions, but we raised our price target(s) following each acquisition to levels that we thought were congruent with a "sum-of-the-parts" approach. However, in our last update we also noted that *beyond the "cumulative" approach we are taking (1+1+1 =3), we think the addition of this new commercial staffing approach, may create some synergies (1+1+1 =4) that we are not including here.* After digesting the fiscal 2020 numbers and thinking through some of the narrative from their year end call, we have sharpened our pencil a bit and tried to rationalize what some of the potential synergies of these acquisitions might be.

In that regard, one of the issues the Company has raised with respect to these acquisitions, is that the two acquired enterprises both focus on the commercial (traditional) staffing side of the industry as opposed to the direct dispatch segment represented by their legacy business. Because these represent two distinct segments of the temporary service business, we believe the Company may have opportunities to cross pollinate its existing markets with one or the other approach. For instance, we think the Company believes that some if its existing direct dispatch franchisees may benefit from adding commercial staffing franchises as well. Further they believe that the geographic breadth of these additions will make their brand(s) more attractive to larger national accounts. To that end, as we understand it, the commercial staffing side of the business is more applicable to larger accounts in general. The following is some narrative from the Company regarding the two acquisitions that we think is particularly additive to these assessments:

> *"HireQuest continues to identify strategic inorganic opportunities to deploy our capital to create long-term, sustainable value," added Mr. Hermanns. "These acquisitions should also accelerate organic growth as our existing franchisees also seek expansion opportunities. The two recently announced pending acquisitions will help diversify our revenue streams and solidify our competitive position."*

To unpack this, if we understand it correctly, *inorganic opportunities* suggest the potential for more acquisitions. Secondly, the reference to the acquisitions *accelerating organic growth* amongst existing franchisees may speak to our cross-pollination notion above and third, we think *solidifying our competitive position* references in part that potential access to larger national accounts we noted. The point is, as we said, our prior targets were based on our initial (simple) "sum-of-the-parts" analysis. However, it is clear to us that these acquisitions are intended to provide some added organic synergies. Furthermore, while our discussions with management have certainly left us with the notion that they intend to remain patient and discerning with respect to additional acquisitions, if the narrative above is any indication, we think additional acquisitions are likely.

Lastly, as we noted in the prior updates, the breadth and rate at which the temporary staffing business can recover from the pandemic remains a wild card. Our assumption therein is that 2021 will show marked improvement over 2020, but we do not see it returning to pre-covid normal until 2022. That said, because of some of the synergy issues we noted above (and did not include in our recent targets) we have recast our model to reflect some added organic growth. To be clear, the changes are not substantial increases, but they are meaningful in terms of generating higher assumed targets. In addition, as those familiar with our research are likely aware, we tend to use a basic DCF/NPV framework to our valuations, with some consideration for other unique company specific elements or perhaps other industry comparable metrics that we think might be applicable. In that regard, many of our coverage companies are in the early stage of commercialization and generally lack visibility with respect to near and even medium-term revenue and cash flow projections. As a result, we tend to apply high relative discounts rates to our NPV analysis to reflect that poor visibility and in effect discount or handicap the NPV conclusions. However, as the visibility of these companies begins to improve, we often adjust our discount rates to approximate their appropriate levels, which are typically supposed to be in line with their theoretical costs of capital. We submit, in the case of HQI, part of our ongoing analysis has involved raising price targets as a result of lowering assumed discount rates due to the Company's improving visibility, financial performance, financial condition and ultimately its (lower) assumed costs of capital.

As a result of the above "pencil sharpening", we are establishing yet another new 12-24 month price target of *$23.00 per share based some of the model changes we noted. At the same time, we are maintaining our allocation of 4, and we will revisit these conclusions as new data points emerge.

Projected Operating Overview

Income Statement							
Projected Operating Statement							
HireQuest, Inc.							
By: Trickle Research LLC	*(actual)*	(estimate)	(estimate)	(estimate)	(estimate)	(estimate)	(estimate)
	Fiscal 2020	**3/31/21**	**6/30/21**	**9/30/21**	**12/31/21**	**Fiscal 2021**	**Fiscal 2022**
Franchise Royalties	*$ 12,792,793*	$ 3,915,123	$ 5,630,850	$ 6,587,655	$ 6,811,055	$ 22,944,683	$ 30,635,694
Service Revenues	*$ 1,016,332*	$ 208,043	$ 255,908	$ 309,813	$ 367,115	$ 1,140,879	$ 1,825,435
Total Revenues	*$ 13,809,125*	$ 4,123,166	$ 5,886,758	$ 6,897,468	$ 7,178,170	$ 24,085,562	$ 32,461,129
Selling, general, and administrative expenses	*$ 8,700,446*	$ 2,183,047	$ 2,626,579	$ 3,006,806	$ 3,386,365	$ 11,202,798	$ 16,019,011
Depreciation and amortization	*$ 129,182*	$ 33,003	$ 32,713	$ 32,418	$ 32,126	$ 130,261	$ 125,637
Income from operations	*$ 4,979,497*	$ 1,907,115	$ 3,227,465	$ 3,858,244	$ 3,759,679	$ 12,752,503	$ 16,316,482
Interest expense and other financing expense	*$ (49,664)*	$ (17,084)	$ (18,945)	$ (22,074)	$ (22,392)	$ (80,495)	$ (91,790)
Other Miscellaneous Income	*$ 1,170,619*	$ -	$ -	$ -	$ -	$ 0	$ 0
Net income before income taxes	*$ 6,100,452*	$ 1,890,031	$ 3,208,520	$ 3,836,170	$ 3,737,287	$ 12,672,008	$ 16,224,691
Provision for income taxes	*$ 741,038*	$ 434,707	$ 737,960	$ 882,319	$ 859,576	$ 2,914,562	$ 3,731,679
Income From Continuing Operations							
Income From Discontinued Operations							
Net Income	*$ 5,359,414*	$ 1,455,324	$ 2,470,561	$ 2,953,851	$ 2,877,711	$ 9,757,446	$ 12,493,012
Earnings per share:							
Basic	*$ 0.40*	$ 0.11	$ 0.18	$ 0.22	$ 0.22	$ 0.73	$ 0.99
Diluted	*$ 0.39*	$ 0.11	$ 0.18	$ 0.22	$ 0.22	$ 0.72	$ 0.98
Weighted average shares outstanding:							
Basic	*13,542,403*	$13,628,675	$13,628,675	$13,382,017	$13,149,375	13,447,186	12,639,600
Diluted	*13,654,128*	$13,654,620	$13,665,378	$13,428,681	$13,205,263	13,488,485	12,715,314

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Portions of this publication excerpted from company filings or other sources are noted in *italics* and referenced throughout the report.

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.