Long Ideas | Healthcare

Fitlife Brands Is About To Show The Full Turnaround Impact

May 13, 2019 8:43 AM ET66 comments
by: Maarten Pieters

Summary

- During 2018, Fitlife Brands turned around under new leadership of the current CEO, Dayton Judd, by reducing operating expenses by 25% and returning to revenue growth in Q3 and Q4.
- The full impact of cost saving measures implemented in 2018 will be visible in the Q1 2019 financials to be reported in May. Q1 is seasonally the strongest quarter.
- I expect that full impact of savings combined with return to growth on the seasonally strongest quarter will open investors eyes by showing the earnings power of the restructured business.
- Fitlife Brands shows strong growth in their online channel. This has the potential to become a solid future growth driver and reduces the dependency on their largest (troubled) customer GNC.
- The CEO shows confidence in the business by a really significant amount of insider purchases as well as other actions.

All figures are corrected for the recent (April 16 2019) reverse/forward stock split unless otherwise noted. The reverse/forward stock split is explained in more detail later in the article.

The company and market

Fitlife Brands is a company that owns a portfolio of several nutritional supplement brands. The products help people to build muscle, burn fat, improve endurance or to increase energy. Production is fully outsourced. The company derives a significant amount of sales from retailer GNC (78% in 2017 and 77% in 2018), primarily from their franchise locations.

The nutritional supplement market is a very competitive market. Most of Fitlife Brands products compete in the more expensive segment of the market. New entrants can easily start a business and sell similar products by contracting a 3rd party supplier. Brand perception is critical.

A combination of events and failures triggered the need for a turnaround of the business

From FY11 to FY14 the company grew revenue from $12.1m to $20.0m and net earnings per share from $0.30 to $2.00. This resulted in a share price of more than $24 before the problems started.

FY14-FY17 actuals

Values in $m	FY14	FY15	FY16	FY17
Revenue	20.0	17.9	25.3	17.8
Net income (loss)	1.7	(1.2)	0.4	(9.8)

Source: company financials and own research

- From FY14 to FY15 revenue decreased from $20.0m to $17.9m despite the merger with iSatori at the start of the 4th quarter. This was primarily the result of a transition in distribution model. Fitlife Brands initially distributed products directly to GNC franchisees and had to move towards a model where they sell the products to the GNC distribution system at wholesale pricing which was ~15% lower. This resulted in a net loss of $1.2m (includes ~$0.8m in merger related one-off costs).
- From FY15 to FY16 revenue increased from $17.9m to $25.3m. This was a combination of ~10% growth of the core products and the full year contribution of the iSatori brand ($7.1m). The company was able to post a net profit of $0.4m.
- From FY16 to FY17 revenue decreased from $25.3m to $17.8m. This was the result of (1) lower same store sales at GNC franchisees, (2) inventory level adjustments at GNC from these trends and (3) a decrease of iSatori revenue from $7.1m to $4.1m. The merger with iSatori clearly failed. This resulted in a net loss of $9.8m (includes ~$5.9m in intangible assets write-offs related to iSatori and a $1.1m reserve for potential sales returns related to iSatori).

The former CEO John Wilson resigned from his position on February 18, 2018. The company appointed Dayton Judd, already a member of the board and a shareholder, as interim CEO. He owned approximately 83,000 shares at the time.

Under leadership of Dayton Judd serious measures have been taken to turnaround the business by reducing operating expenses and by developing e-commerce capabilities

FY17 and FY18 actuals

Values in $	Q1-17	Q2-17	Q3-17	Q4-17	Q1-18	Q2-18	Q3-18	Q4-18	FY17	FY18
Revenue	5,589,354	5,022,000	4,026,000	3,161,991	4,614,286	4,379,000	4,583,000	3,500,714	17,799,345	17,077,000
Cost of goods sold*	(3,668,790)	(3,499,000)	(2,551,000)	(1,889,670)	(2,698,618)	(2,573,000)	(2,831,000)	(2,229,382)	(11,608,460)	(10,332,000)
Gross margin	**1,920,564**	**1,523,000**	**1,475,000**	**1,272,321**	**1,915,668**	**1,806,000**	**1,752,000**	**1,271,332**	**6,190,885**	**6,745,000**
General and administrative	(1,160,069)	(1,010,000)	(1,030,000)	(979,876)	(870,382)	(856,000)	(784,000)	(822,618)	(4,179,945)	(3,333,000)
Sales & marketing	(947,386)	(913,000)	(829,000)	(835,816)	(806,109)	(718,000)	(547,000)	(618,891)	(3,525,202)	(2,690,000)
Depreciation and amortization	(119,338)	(117,000)	(99,000)	(74,138)	(18,840)	(18,000)	(16,000)	(16,160)	(409,476)	(69,000)
Total operating expenses	**(2,226,793)**	**(2,040,000)**	**(1,958,000)**	**(1,889,830)**	**(1,695,331)**	**(1,592,000)**	**(1,347,000)**	**(1,457,669)**	**(8,114,623)**	**(6,092,000)**
Operating inome	**(306,229)**	**(517,000)**	**(483,000)**	**(617,509)**	**220,337**	**214,000**	**405,000**	**(186,337)**	**(1,923,738)**	**653,000**
Other expenes (interest & other)	(26,661)	(34,000)	(28,000)	(31,542)	(2,947)	(44,000)	(40,000)	(46,053)	(120,203)	(133,000)
Tax		-	-	-		-	-	(11,000)		(11,000)
Net income**	**(332,890)**	**(551,000)**	**(511,000)**	**(649,051)**	**217,390**	**170,000**	**365,000**	**(243,390)**	**(2,043,941)**	**509,000**
Estimated fully diluted share count***	1,269,008	1,269,008	1,269,008	1,269,008	1,269,008	1,269,008	1,269,008	1,269,008	1,269,008	1,269,008
Net income per share	(0.26)	(0.43)	(0.40)	(0.51)	0.17	0.13	0.29	(0.19)	(1.61)	0.40
Gross margin %	34.4%	30.3%	36.6%	40.2%	41.5%	41.2%	38.2%	36.3%	34.8%	39.5%
EBITDA %	-3.3%	-8.0%	-9.5%	-17.2%	5.2%	5.3%	9.2%	-4.9%	-8.5%	4.2%
YoY revenue					-17.4%	-12.8%	13.8%	10.7%		-4.1%

* Excluding $1.1m reserve for return of iSatori products in FY17
** Excluding warrant costs in Q4-18 (covered by diluted share count) and iSatori intangible asset write-off in FY17
*** Excluding options exercisable > $10 and restricted common stock

Source: company financials and own research

Reduction of operating expenses

Operating expenses reduced from $8.1m in FY17 to $6.1m in FY18. This represents a reduction of more than 20% in both G&A expenses and in sales and marketing expenses. So far, these reductions have not had a negative impact on operations or sales. Cuts in marketing costs could have a delayed impact on revenue.

Annualizing the average of Q3 and Q4 FY18 operating expenses results in a run-rate of $5.6m. In Q1 2019 the company took further measures by reducing board expenses and a replacement of the CFO by an internal employee with a lower salary, lowering annual costs by ~$300k. This results in an annual run-rate of $5.3m in operating expenses (all else remaining equal, e.g. no significant investments in e-commerce capabilities). The company also mentioned in their press releases that they continue to reduce costs.

E-commerce capabilities and online sales growth

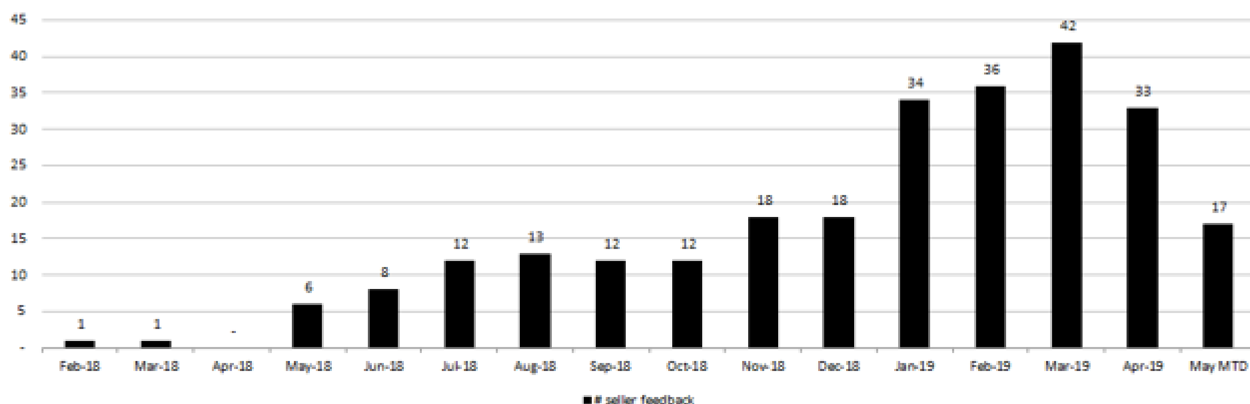
Despite declining sales at GNC, Fitlife Brands has been able to return to sales growth in Q3 and Q4 of FY18, partly thanks to growth of online sales.

Fitlife Brands started their new omni-channel approach early in 2018. Since then they have been able to grow online sales significantly. Especially via the Amazon store front. They also recently launched a new website to grow online sales. By selling more products via the company's own platform, the company is able to collect detailed end-customer data and thereby improve customer intelligence and marketing and sales effectiveness. This is not possible via Amazon or Ebay.

The company intends to provide a breakdown of revenue into online revenue and wholesale revenue for the first time in Q1 2019. This to me indicates that online sales have become material. Comments in the FY18 annual report also shows management's confidence towards both the short-term and long-term potential of the online channel.

> Management also believes that its focus on developing its ecommerce capabilities will drive additional incremental sales in the short-term, while yielding substantial benefits in the longer-term.

The amount of seller feedback of Fitlife Brands on Amazon also shows strong growth with a big step up in Q1 2019 (Source: own research).



A back of the envelope calculation results in ~$100k-$300k in incremental operating income from the online sales channel in Q1 2019, or ~$0.10-$0.30 per share. Assumptions:

- Seller feedback on 1-3% of orders: based on input from sellers of low value goods on Amazon
- Gross margin of 45%: Fitlife Brands indicated that margins via Amazon are higher than wholesale margins, which were ~40% in 2018.
- Average order size of $60: estimate based on product range.

The CEO shows great confidence in the business

The CEO, Dayton Judd, actions show great confidence in the business:

- He bought a total of ~188k shares (18% of the Dec-17 number of shares outstanding) in the open market and via private transactions
- In November 2018, he provided $525k in financing via the issuance of series A preferred stock and warrants. This financing was required at the time and I believe that it is difficult for a company this size, with high customer concentration and a recent history of operating losses to obtain this financing at good terms. Nevertheless, I believe that the conditions of the financing and especially the series A preferred stock were too favorable. This is a first red flag in how he treats other shareholders. If he converts all preferred stock (at $4.60 per share) and exercises all warrants (at $4.60 per share) he will increase his number of shares owned by ~148k (14% of the Dec-17 number of shares outstanding).
- In December 2018, additional financing was required as their bank terminated the factoring agreement. The CEO provided $800k in credit notes with an interest rate of 9% (currently $500k outstanding), which is appropriate for this business and fair towards shareholders in my opinion. Providing these notes is another strong signal that he believes in the future of the business and is not that worried about a serious downturn of the business.
- In April 2018, he implemented a reverse/forward stock split and thereby cashed out all shareholders holding less than 8,000 shares (pre reverse/forward stock split, equivalent to 800 shares post reverse/forward stock split) at the volume weighted average trading price of the last 5 days (~$5.60 at the time). It was timed in such a way that shareholders had no opportunity to increase their holdings above the threshold of 8,000 shares. Normally companies cash-out minority shareholders at a premium to the trading price and ask for a fairness opinion from an independent company in this process. I see this reverse/forward stock split as a very aggressive and minority shareholder unfriendly move by the CEO to buy back shares at low prices. This just before posting Q1 2019 results, which I expect to be very good. According to the company there were approximately 1,000 shareholders holding less than 8,000 shares. If we assume that the average minority shareholder held 1,000 shares, this has resulted in a share reduction of 1,000,000 or 100,000 post

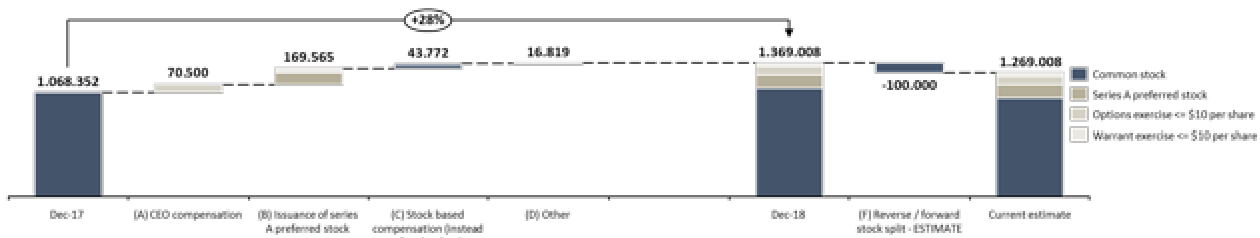
reverse/forward stock split (9% of the Dec-17 number of shares outstanding).

All these actions point towards great confidence by the CEO about the future of the business and that the shares are currently significantly undervalued. At the same time it casts doubts about his integrity and how he will treat shareholders in the future. He holds over 40% of shares outstanding and is therewith, more or less, in full control of the company.

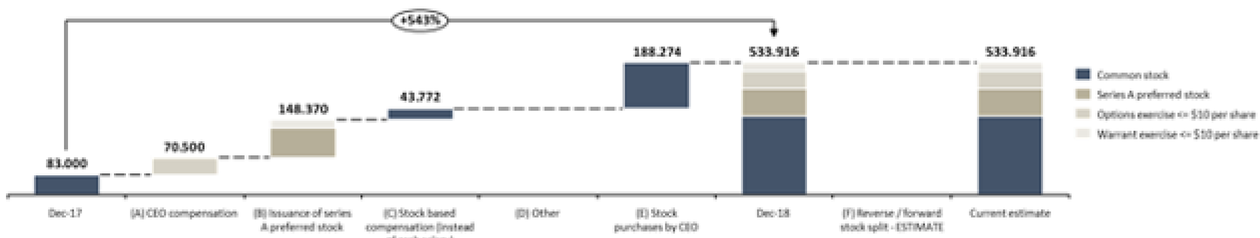
The above actions, including executive compensation in the form of options resulted in the number of shares outstanding and ownership of the CEO displayed in the graphs below (Source: company financials and own research). His incentives are in principle very well aligned with those of shareholders.

Please note that the figures exclude all options exercisable at prices above $10 per share and exclude 45,000 shares in restricted common stock granted to the CEO. These vest if the 30 day average trading price exceeds certain targets (15,000 vest if it exceeds $12; 15,000 vest if it exceeds $18 and 15,000 if it exceeds $24).

Shares outstanding



Ownership CEO



There are two major risks, the dependency on GNC and the treatment of shareholders by the CEO

Dependency on GNC

While most sales to GNC are to franchisees, Fitlife Brands has one accounts receivable position at GNC. They manage the inventory and distribution for all their own and franchisee stores. GNC has no direct liquidity concerns as it received new financing in November 2018. However, if sales continue to deteriorate this could become a problem in the future. Something to monitor closely.

All franchisees have the freedom whether they want to sell Fitlife Brands products or not. While the number of GNC franchisee stores shows a negative trend, Fitlife Brands has been able to grow the number of franchisee stores served. This indicates that Fitlife Brands products deliver value to the franchisee (e.g. requested by customers, better margins). Therefore, I don't believe that a sudden significant drop in sales is likely. All the products sold by GNC franchisees require approval by GNC. There is thus a possibility that GNC blocks certain Fitlife Brands products and thereby affect sales significantly. As long as the franchisees like to sell Fitlife Brands products this also seems unlikely, as it would jeopardize their relation.

The growth of online sales slowly lower the dependency on GNC.

Treatment of shareholders by the CEO

There have been two red flags on how the CEO treats shareholders. More shareholder unfriendly moves are a real possibility. Most likely in the form of dilution (issuance of more series A preferred stock) or an attempt to take the company private at a low valuation.

Potential

Applying 2018 gross margins, a revenue growth rate of 10% (below the YoY growth rate in Q3 and Q4 2018) and operating expenses as discussed earlier in this article would result in FY19 earnings of $1.49 per share while shares currently trade at $6.80. A forward PE multiple < 5. The company has $28m in federal NOLs to offset future income tax.

Despite the significant risks involved, I believe that the shares are significantly undervalued. If the company can return to sustainable revenue growth with their omni-channel approach and lower the dependency on GNC, significant multiple expansion is likely.

I can't find comparable listed companies of Fitlife Brands size. One of the key competitors, whose products rank on the top pages on Amazon and are sold in GNC stores is Glanbia Plc. This is a much more diversified company with revenues of €2.4b. They have a similar EBITDA margin of 11-12% and significantly lower gross margins of 28%. Fitlife Brand should be able to achieve higher EBITDA margins if they can increase scale. Glanbia trades at a PE multiple of 19 and a PS multiple of 1.9 (compared to a forward PE of 5 for Fitlife Brands and a forward PS of 0.5). A difference of 280%.

FY17 and FY18 actuals and FY19 estimate

Values in $	Q1-17	Q2-17	Q3-17	Q4-17	Q1-18	Q2-18	Q3-18	Q4-18	Q1-19	Q2-19	Q3-19	Q4-19	FY17	FY18	FY19
Revenue	5,589,354	5,022,000	4,026,000	3,161,991	4,614,286	4,379,000	4,583,000	3,500,714	5,075,715	4,816,900	5,041,300	3,850,785	17,799,345	17,077,000	18,784,700
Cost of goods sold*	(3,668,790)	(3,499,000)	(2,551,000)	(1,889,670)	(2,698,618)	(2,573,000)	(2,831,000)	(2,229,382)	(2,968,480)	(2,830,300)	(3,114,100)	(2,452,320)	(11,608,460)	(10,332,000)	(11,365,200)
Gross margin	1,920,564	1,523,000	1,475,000	1,272,321	1,915,668	1,806,000	1,752,000	1,271,332	2,107,235	1,986,600	1,927,200	1,398,465	6,190,885	6,745,000	7,419,500
General and administrative	(1,160,069)	(1,010,000)	(1,030,000)	(979,876)	(870,382)	(856,000)	(784,000)	(822,618)	(803,309)	(728,309)	(728,309)	(728,309)	(4,179,945)	(3,333,000)	(2,988,236)
Sales & marketing	(947,386)	(913,000)	(829,000)	(835,816)	(806,109)	(718,000)	(547,000)	(618,891)	(582,946)	(582,946)	(582,946)	(582,946)	(3,525,202)	(2,690,000)	(2,331,782)
Depreciation and amortization	(119,338)	(117,000)	(99,000)	(74,138)	(18,840)	(18,000)	(16,000)	(16,160)	(16,000)	(16,000)	(16,000)	(16,000)	(409,476)	(69,000)	(64,000)
Total operating expenses	(2,226,793)	(2,040,000)	(1,958,000)	(1,889,830)	(1,695,331)	(1,592,000)	(1,347,000)	(1,457,669)	(1,402,255)	(1,327,255)	(1,327,255)	(1,327,255)	(8,114,623)	(6,092,000)	(5,384,018)
Operating income	(306,229)	(517,000)	(483,000)	(617,509)	220,337	214,000	405,000	(186,337)	704,980	659,346	599,946	71,211	(1,923,738)	653,000	2,035,482
Other expenses (interest & other)	(26,661)	(34,000)	(28,000)	(31,542)	(2,947)	(44,000)	(40,000)	(46,053)	(36,000)	(36,000)	(36,000)	(36,000)	(120,203)	(133,000)	(144,000)
Tax		-	-	-		-	-	(11,000)	-	-	-	-		(11,000)	-
Net income**	(332,890)	(551,000)	(511,000)	(649,051)	217,390	170,000	365,000	(243,390)	668,980	623,346	563,946	35,211	(2,043,941)	509,000	1,891,482
Estimated fully diluted share count***	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008	1,209,008
Net income per share	(0.26)	(0.43)	(0.40)	(0.51)	0.17	0.13	0.29	(0.19)	0.53	0.49	0.44	0.03	(1.61)	0.40	1.49
Gross margin %	34.4%	30.3%	36.6%	40.2%	41.5%	41.2%	38.2%	36.3%	41.5%	41.2%	38.2%	36.3%	34.8%	39.5%	39.5%
EBITDA %	-3.3%	-8.0%	-9.5%	-17.2%	5.2%	5.3%	9.2%	-4.9%	14.2%	14.0%	12.2%	2.3%	-8.5%	4.2%	11.2%
YoY revenue					-17.4%	-12.8%	13.8%	10.7%	10.0%	10.0%	10.0%	10.0%		-4.1%	10.0%

* Excluding $1.1m reserve for return of iSatori products in FY17
** Excluding warrant costs in Q4-18 (covered by diluted share count) and iSatori intangible asset write-off in FY17
*** Excluding options exercisable > $10 and restricted common stock
Source: company financials and own research

Downside

If margins would go back to a level of 35% as in 2014 and 2015, Fitlife Brands requires approximately $15m in revenue at the current operating expenses level to break-even. Downside scenarios beyond such a sales and margin decline belong to a realistic set of outcomes in my opinion seen the dependency on GNC and their recent performance (not to mention the very competitive market in general). Although there is not a lot of debt on the balance sheet, I believe that downside protection is limited. The balance sheet mainly consists of accounts receivable to GNC (which have a certain risk as described above) and inventory which liquidation value is likely far below the balance sheet value.

Estimate of current balance sheet

Values in $	dec-18	Q1 2019 net income	Reverse / forward stock split	Current estimate
Cash	259,000	668,980	(560,000)	367,980
Accounts receivable	1,433,000			1,433,000
Inventory	3,523,000			3,523,000
Other	223,000			223,000
Total current assets	**5,438,000**	**668,980**	**(560,000)**	**5,546,980**
Fixed assets	424,000			424,000
Total assets	**5,862,000**	**668,980**	**(560,000)**	**5,970,980**
Accounts payable	2,628,000			2,628,000
Notes payable - related party	500,000			500,000
Other	420,000			420,000
Total liabilities	**3,548,000**	-	-	**3,548,000**
Stockholders equity	2,314,000			2,422,980
Total liabilities and stockholders equity	**5,862,000**	-	-	**5,970,980**

Source: company financials and own research

Looking at the upside potential and considering all the risks, I believe that Fitlife Brands presents a very good investment opportunity if sized appropriately.

Disclosure: I am/we are long FTLF. I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.

Editor's Note: This article covers one or more microcap stocks. Please be aware of the risks associated with these stocks.

Should I pick up FTLF?

Seeking Alpha Premium makes it simple. If our 3 scores flash green – Quant Ratings, SA author rankings, Wall Street calls – it's an easy decision.

Unlock FTLF Ratings Now »

Comments (66)

Maarten Pieters

Author's reply » Super strong quarter. Excluding the one-off (which they might recover) they are on track to get to c. 3.50-4.00 earnings this year I think.

COVID might be a net positive due to the significant online sales growth acceleration (100% now) and some accelerated restructuring.

Unbelievable that even the offline sales are growing at low single digits compared to last year - given the headwinds of COVID and franchisee store closures.

13 Aug 2020, 03:51 PM

Maarten Pieters

Author's reply » The risk profile of the investment increased significantly with both COVID-19 and GNC specific problems (fueled by COVID-19).

FTLF is not the only company drawing credit line. Without the GNC issue, they would probably have done the same. IT is therefore difficult to assess how worried management is about a real bad scenario with GNC.

GNC (excl. COVID-19 impact) generates a lot of cash prior to interest payments. I am therefore pretty sure that the business will continue, possibly via a chapter 11 bankruptcy. I am not sure what would happen to FTLF's AR position in this scenario.

Q4 results were really strong (first profitable fourth quarter in a long time). I also liked the following text of the 10-K:

"The anticipated increase in incremental sales attributable to ecommerce is anticipated to be offset by a projected short-term decrease in sales through the GNC franchise and company-owned system, as well as through other wholesale and retail distribution channels, principally due to the recent COVID-19 outbreak, which the Company anticipates affecting sales beginning in the quarter ended March 31, 2020 through at least the quarter ending June 30, 2020. Management cannot predict the magnitude of the anticipated impact of COVID-19 on its sales in the short-term or whether sales through traditional retail channels will be negatively impacted in the long-term; however, management currently expects such impact in the short-term to be material, and will likely accelerate the shift toward more sales through the Company's ecommerce channels."

Online sales growth seems to continue and the company expects this to accelerate in the current environment.

I believe that the most likely scenario is that they will survive the current problems. However a permanent loss of capital is also one of the scenario's to take into account.

30 Mar 2020, 06:20 PM

Anshay
seekingalpha.com/...

This looks like a real speed bump in the recovery path for FTLF. They are going to have to write off some AR when GNC goes bankrupt

16 Mar 2020, 09:12 PM

Maarten Pieters
Author's reply » This doesn't look good indeed. The best scenario is that Harbin steps in and takes the company private. seekingalpha.com/...

In case of a bankruptcy they indeed have to write-off AR (I estimate this at c. 1.6-2.4m) and based on the appetite of the franchisees decide whether to continue the brick and mortar business or transform into an online pure play.

17 Mar 2020, 05:17 AM

Anshay
It looks to me like March 16 GNC announces that they won't have the cash to pay debt maturing. March 18 GNC releases earnings. March 20 FTLF pulls their whole line of credit. Means Dayton and crew are not optimistic.

27 Mar 2020, 09:09 PM

Connor Davis
Yeah just saw that filing. Agreed Anshay, does not look promising.

29 Mar 2020, 11:43 AM

Maarten Pieters
Author's reply » I wrote some notes with regard to expected sales growth on my blog: investmentlonglist.com/...

30 Dec 2019, 03:40 PM

Connor Davis
Thanks Maarten. Good work as always.

02 Jan 2020, 05:56 PM

Maarten Pieters
Author's reply » Very shareholder friendly move by the CEO to voluntarily convert all his preferred stock into common stock.

Also some further repurchases since last time (c. 21k shares at a price of c. $12.50 per share).

There are no more Series A preferred stock outstanding. Very positive as these yielded 12%.

www.otcmarkets.com/...

23 Dec 2019, 05:45 PM

Connor Davis
This is huge. It absolutely is very shareholder friendly to convert his Preferreds to common. Also, the number of shares outstanding has now decreased by more than 10% just since 6 weeks ago.

Good work as always, Maarten.

24 Dec 2019, 03:51 PM

Maarten Pieters
Author's reply » Some further DD via Instagram showed the following:

- They held a large event in Costa Rico with all large multi-store GNC franchisee operators to thank them for the support and market / introduce /

educate about (new) products (probably a good investment, but could easily reduce Q4 EPS by $10ct)

- The Sirenlabs product line will be rebranded with a much fresher design (more of this time). In line with what the company did with the PMD product line this year, which I believe had had a good impact on sales

- A full new product line will be introduced (no further details available at this time, but the design looks good)

It is good to see that the company makes proper efforts to maintain/increase the value of the existing brands and invests in new product lines.

07 Dec 2019, 05:34 AM

Connor Davis

Thanks for staying on top of this one, @Maarten Pieters . Well done.

08 Dec 2019, 10:30 PM

Maarten Pieters

Author's reply » I am not too worried about acquisitions. So far all of Dayton's moves were really calculated. I expect him to go for companies in line with the old fitlife (where he can apply the same trick) or more likely small online players which lack scale.

13 Nov 2019, 08:27 AM

Maarten Pieters

Author's reply » Great Q3, I believe that the shares are still undervalued, despite the 35% run-up since the release. Trading at a PE < 6 with several growth drivers (Walmart, online sales growth, acquisitions). Continued insider buying/buybacks confirms this.

12 Nov 2019, 01:17 PM

Connor Davis

If FTLF can diversify away from GNC and grow online sales, this could be more than a double.

12 Nov 2019, 01:57 PM

Anshay

My target at this point is about $20 per share. My main concern at the moment is the possibility of a poorly done acquisition. This almost bankrupted the company once. I think Dayton has his head on right and

won't do something like that, but acquisitions often turn out to be much more complicated to integrate than originally planned.

Great quarter though, and really impressed that they paid back debt and redeemed 16% of shares since the beginning of the year.

12 Nov 2019, 09:17 PM

Maarten Pieters

Author's reply » Close to 50k shares volume today (c. 9% of the free float). I expect the company to be a big buyer.

30 Sep 2019, 04:42 PM

Connor Davis

Did you see in the Schedule 13D/A that 25 shares were purchased at over $2,180 each? Have you ever seen that before? Has to be a mistake, right?

30 Sep 2019, 07:48 PM

Maarten Pieters

Author's reply » Yes, that's for the series A preferred stock. These are worth 1000 each, but are also convertible into c. 217 shares. So that price translates to c. 10 USD per share, which makes sense.

01 Oct 2019, 01:24 AM

Connor Davis

Ah, I see. Thank you.

01 Oct 2019, 01:16 PM

Maarten Pieters

Author's reply » The company bought back c. 4% of shares outstanding, increased the repurchase program to $1m and now has c. $2.5m available via a new line of credit for further repurchases or small acquisitions. Quite bullish in my opinion.

29 Sep 2019, 10:20 AM

Connor Davis

@Maarten Pieters , is this new? Or is this confirmation from the last ER?

30 Sep 2019, 09:23 AM

Maarten Pieters

Author’s reply » This is news, purchases occurred between August 16 and September 26. and the line of credit is new.

www.otcmarkets.com/...

30 Sep 2019, 03:16 PM

Connor Davis

Perfect, thank you so much Maarten. I need to subscribe to filings.

30 Sep 2019, 07:25 PM

Connor Davis

Agreed these updates are very bullish. Dayton also made the company more professional by getting a line of credit with a bank instead of through his investment fund / personal accounts.

Thank you for the heads up Maarten.

30 Sep 2019, 07:29 PM

Maarten Pieters

Author’s reply » The company released earnings yesterday. An OK quarter, but after a blow-out quarter like Q1 I hoped for more.

Offline revenue was $4.0m vs. $5.3m last quarter. I think that GNC's inventory management is a large contributor to this. If not it would be worrisome, however I don't expect this, especially seen Dayton's very recent share purchases at $9.75 per share.

Online sales showed nice quarter over quarter growth ($590k to $620k) while Q2 is seasonally weaker than Q1 for the business.

Interested in your thoughts.

10 Aug 2019, 06:11 AM

Connor Davis

Great thoughts @Maarten Pieters. Agreed with all of them. Was hoping for more, but not bad. I would give the quarter a ~5.6/10.

10 Aug 2019, 12:26 PM

Lares Capital

You need to keep in mind that FitLife has historically had weaker quarters after great ones. In Q1, they had very large orders from franchisees,

which pulled some demand forward. So Q1 overstates the performance while Q2 understates. Also, GNC's franchisees had a good Q1 (up YOY same store sales) but weaker Q2 (down same store sales).

A good way to appreciate performance is to look Q1 + Q2 and compare to 6 month last year. Or look at trailing 12 months numbers numbers which would still indicate significant improvement.

10 Aug 2019, 07:50 PM

Connor Davis

Agreed with you @Lares Capital. Well said.

They need to keep up the direct to consumer growth. That will be key for FTLF.

11 Aug 2019, 06:56 PM

Maarten Pieters

Author's reply » And another c. 48,000 share (equivalents) at $9.75 from Grant Dawson and probably other board members as well. I am trying to get in contact with Grant Dawson to understand if he will remain on the board.

www.otcmarkets.com/...

09 Aug 2019, 11:19 AM

Lares Capital

Grant Dawson wasn't the seller of 48K shares. You can see his holding before on the proxy.

10 Aug 2019, 07:55 PM

Maarten Pieters

Author's reply » Dayton just bought another 52000 shares (4.1% of fully diluted shares outstanding) at a price of $8.50. All in private transactions.

www.sec.gov/...

11 Jul 2019, 02:56 AM

Connor Davis

Thanks @Maarten Pieters .

11 Jul 2019, 09:53 AM

Maarten Pieters

Author's reply » Based on the Amazon feedback I track Q2 online sales should be comparable to Q1. One of their relatively new products (Coreactive Syphon Fat Burner) recently entered the top 30 within the fat burner supplement category on Amazon, after which is was quickly sold out. They are now restocked and climbing the ranks again. If they can get back to this rank this could be a good growth driver for online sales. Being visible on the first page of a Amazon category can make a huge impact on sales.

With the shares back to the low $9's and a high likelyhood that the company will do $2 or more in earnings this year, I believe that the risk reward is still very favorable.

10 Jul 2019, 05:33 AM

Anshay

No wonder he was so eager to buy 9% of float from small holders. They really got robbed

15 May 2019, 08:25 PM

Lares Capital

I don't understand your point: large shareholders benefited at the expense of smaller ones. This seems actually fair to me. If you want to decide how the company is operated, buy more shares, get on the BOD, etc. This is not a democracy where a little guy gets the same one vote as a big guy. The more shares you hold, the more say you have.

You realize that the average position he bought out was worth something like $750. Do you think many of these shareholders would be able to even name the company?

15 May 2019, 09:07 PM

Anshay

When I first began investing when I was in college, I had more enthusiasm than money and my average position was $1000. I cared deeply about my portfolio back then and knew every single position well. I suspect some of the holders he terminated were like that. These kind of holders should have had a longer notification period than was given them to increase their holdings in a very illiquid stock.

Regardless, the whole thing is really constructed for Dayton to make out like a bandit. Dayton lent the company his money (at 9% interest) to buy back shares that he knew were cheap based on information not readily available to the rest of the market. He essentially lent the company money at 9% so that he could own a higher percentage of the company and do so at an advantageous price. He makes money on the interest and also

increases his stake in the company with money borrowed from him. All done by forced sales of small holders positions. Was it legal? Probably. Was it ethical. No

15 May 2019, 09:26 PM

Maarten Pieters

Author’s reply » I fully agree with you. If you want to implement this the right way, you have to obtain a fairness opinion. It is pretty obvious that $5.70 per share is not fair if you are able to post $1 in earnings in just the first quarter.

16 May 2019, 05:41 AM

Maarten Pieters

Author’s reply » They just posted $1 dollar per share in net income. Above all expectations. Wow! Didn't have the chance to read the report yet.

15 May 2019, 06:00 PM

Lares Capital

I have. Internet did really well with 10% overall and very high gross margin but also they got another 17% boost from franchise stores. Considering overall franchise revenue is flat, they must have captured some market share. This is a very strong report in all aspects. Can't really find anything negative. I wouldn't worry about high A/R, it repeats very year in Q1.

15 May 2019, 08:21 PM

Connor Davis

Any chance franchise stores were stocking up or FTLF was offering a discount in exchange for market share?

15 May 2019, 09:12 PM

Lares Capital

If these were the case, gross margins would have been down, the gross margins were up.

15 May 2019, 09:17 PM

Anshay

Obviously these results blew past our expectations. Dayton is to be commended for a phenomenal quarter. You did a lot of research for this article. What is your revised opinion for the year based on this new data?

I'm guessing that even if they just maintain their current market share online and in franchises, they can hit $2.00 per share in income this year. With any sort of momentum in these two distribution outlets, they may be able to do even better. In my opinion, this could easily double from its current level by the end of the year.

15 May 2019, 09:54 PM

Connor Davis

Ah yes @Lares Capital you are correct on the gross margin on discounting. What about stock-ups?

15 May 2019, 09:58 PM

Lares Capital

What would be the reason to stock up? In Q1 GNC replenishes inventory after drawdown at Q4, so Q1 tends to be a bit stronger than Q2 and Q3. So I wouldn't expect them to make a $1 in Q2 and Q3 unless internet sales keep on growing (which is possible). Seasonally weak Q4 is break-even at best.

It's conceivable that inventory at GNC warehouse got too low so it helped a bit. They did have a bad precedent in 2016 when after very strong Q1 and Q2 they had much weaker Q3 (Q4 is always bad), However, it was helped by selling discounted inventory during a GNC convention. I see no evidence of discounting here.

I'd say $2 a share in 2019 now a possibility with decent growth YOY which would imply ~$20+ a share stock.

15 May 2019, 10:48 PM

Maarten Pieters

Author’s reply » $2 per share is indeed possible. Online reviews continue to increase, indicating further online sales growth. The bigger marketing spend, indicated in the press release, to further growth online sales might depress earnings a bit in the short term (however I don't expect Dayton to scale this significantly without testing effectiveness). To me the big question is what type of earnings multiple to assign to an asset ligth company with revenue growth, 20% EBITDA margins and high customer concentration.

16 May 2019, 05:51 AM

Connor Davis

Perfect, thanks for the insight @Lares Capital .

I have been in and out of FTLF for a few years and remember the convention, etc. I may decide to do another write-up..

16 May 2019, 08:26 AM

Connor Davis

Agreed @Maarten Pieters , the multiple is a mystery. Not sure the products FTLF sells demand a significantly high multiple.

16 May 2019, 08:28 AM

Anshay

Fair value is certainly lower given the dependence on GNC for the bulk of sales. I would think a PE ratio in the 7-8 range is fair. However, never underestimate the power of momentum and FOMO with a microcap like this. If they start doing canniboids like Lares mentioned in an earlier quote or other things that create the impression of branching into new markets, wild eyed momentum chasers could drive this multiples beyond fair value. I would think this stock could probably go up to $10.00 per share on this news and not be overvalued. I wouldn't be surprised to see momentum kick in though and take it higher. Fun times

16 May 2019, 08:52 AM

Lares Capital

For a multiple, think of it as two businesses. 7-8 EBITDA for no-growth franchise business seems fair, I could even price it 5 EBITDA if the secular trend is still down. The question how would you value internet business which went from 1% to 10% in one year and doesn't depend much on GNC? This is a low-capital requirement high margin business since Amazon only takes 10%. It should be about $2-2.5 million in revenue in 2019 if the trend holds. EBIT margin on this could easily be 40% because gross margins are probably ~70%. If you think it can contribute up to $1 million in EBITDA with, say, 10-20% growth rate going forward, would you value it at 15x? That alone could be $15 million which exceeds its current market cap.

The key going forward is to prove it's not a one off great Q like it was in 2016. If they can show at least 50-60c. in Q2 and Q3 and break even in Q4, this could bring in new investors.

16 May 2019, 10:50 AM

Connor Davis

Excellent analysis. Thanks @Lares Capital .

16 May 2019, 11:58 AM

Anshay

Excellent history and analysis of this company. I initiated a position in December of 2016 and continued buying until August of 2018. I completely agree with your assessment of the risks. I appreciate very much that the current CEO saved the company from bankruptcy, but also consider some of his moves in the last year to have been highly unfriendly to shareholders. I was particularly vexed by the Class A Shares. The share split was poorly announced and was implemented in a shareholder unfriendly manner. The sudden move up 40% after the split occurred means that the small holders who were bought out had no opportunity to buy back in at the price which they were bought out at. I think that if the CEO engages in further shareholder unfriendly practices, this position should be sold.

13 May 2019, 09:09 AM

Lares Capital

@Anshay , @Maarten Pieters. Here are my thoughts:

I agree that preferred stock issuance was a mistake. In (some) defense of the management, the lender, Compass, just told them that they didn't want to renew the agreement so they were under liquidity pressure and probably couldn't issue regular debt because of covenants. They learned their lesson and issued straight debt afterwards. Given CEOs large equity stake, it helped no one and the authorization to issue more preferred still hanging over common. I'd like to see this authorization withdrawn.

I disagree that buying out small shareholders was shareholder-unfriendly - they got a nice bump on the sale the illiquid stock - what's to complain about? Those were tiny accounts. While this may be theoretically 'unfair' to former shareholders, the current shareholders 'benefited' at their expense.

Also note that on the change of control, such taking company private, they might lose NOLs. Their other option is to "go dark" (basically delist the company) which would save some 200-300K on not having a board and auditors but would make stock even more illiquid and remove "checks and balances". Probably not a good idea. A better idea is to accumulate some cash and roll up a few smaller, Internet sellers to gain some scale, but this would take time as the balance sheet is not yet strong enough.

Some of your numbers are a bit too optimistic. Expecting 10% growth rate this year may not be realistic. I'd be happy with the same revenues as in 2018. The improvement of Q3/Q4 was on the back of terrible second half of 2017. It will be harder to repeat this year.

There are some hopeful signs on GNC where in last Q franchisers showed improvement in same store sales and flat revenues YOY but still closed some stores. There may be a sign franchises stabilized at a lower level and longer a drag.

Expenses this year should be more favorable than in 2018. Mike Abrams left and the loan refinancing is on better terms (they don't have to pay for undrawn amount) but preferred dividend will be a bit of headwind.

They key going forward I think is Instagram sales and CBD. They just redesigned their web site, got a new CMO, and should start on picking up some "influencers".

By the way, gross margins on Amazon are probably more like 70%+. Amazon only takes 10% cut and all this powder takes only a few dollars to produce.

13 May 2019, 12:14 PM

Connor Davis

Thanks for the insight @Lares Capital . Been involved with the story for a while?

13 May 2019, 12:47 PM

Lares Capital

Yes, I am a large shareholder.

13 May 2019, 12:49 PM

Connor Davis

Good luck. Hope it returns to success.

13 May 2019, 01:00 PM

Anshay

Overall, I agree with you Lares. However, I differ with you regarding whether the reverse split was shareholder friendly. It was good for me and you because we own a higher percentage of the company than we did prior to it happening, but it was not a fair transaction for the people who were forced out of this position. There was very little warning with regard to the reverse share split. If you were holding 5,000 shares and wanted to increase above 8,000 to maintain your position, there was very little time to purchase extra shares. Keep in mind that this is a very low volume stock, so building positions takes a lot of time. There was no reason the reverse split couldn't have been announced with a press filing at least a month before the event. I agree with Mr Pieters that there was probably a

sense of time pressure from the management to get this done before Q1 earnings are released.

13 May 2019, 01:13 PM

Maarten Pieters

Author’s reply » Hi @Lares Capital , thanks a lot for providing additional insights.

Hereby my view on a couple of items.

Your comment: "I agree that preferred stock issuance was a mistake. In (some) defense of the management, the lender, Compass, just told them that they didn't want to renew the agreement so they were under liquidity pressure and probably couldn't issue regular debt because of covenants. They learned their lesson and issued straight debt afterwards. Given CEOs large equity stake, it helped no one and the authorization to issue more preferred still hanging over common. I'd like to see this authorization withdrawn."

The Compass announcement was after the issuance of preferred stock. The company explained the need for the issuance of this preferred stock by money required for the seasonally difficult fourth quarter and the buildup of inventory for the seasonally strong first half of the year. I question to what extent this was required.

They had no other debt than the factoring agreement with Compass at the time. After the announcement that Compass didn’t want to renew the factoring agreement the company solved this via regular debt from Sudbury Capital (100% owned by Dayton Judd) and directly from Dayton Judd. Dayton could have issued credit notes the first time as well, instead of the issuance of preferred stock + warrants.

Your comment: "I disagree that buying out small shareholders was shareholder-unfriendly - they got a nice bump on the sale the illiquid stock - what's to complain about? Those were tiny accounts. While this may be theoretically 'unfair' to former shareholders, the current shareholders 'benefited' at their expense."

I don’t think that they received a nice bump. It was at the last 5 day VWAP. I know several small shareholders who also perceived it as very shareholder unfriendly.

Your comment: "Also note that on the change of control, such taking company private, they might lose NOLs. Their other option is to "go dark" (basically delist the company) which would save some 200-300K on not having a board and auditors but would make stock even more illiquid and remove "checks and balances". Probably not a good idea. A better idea is to accumulate some cash and roll up a few smaller, Internet sellers to gain

some scale, but this would take time as the balance sheet is not yet strong enough."

I also believe that there are nice opportunities to roll up smaller internet sellers. Especially if they are able to improve their online capabilities.

You comment: "Some of your numbers are a bit too optimistic. Expecting 10% growth rate this year may not be realistic. I'd be happy with the same revenues as in 2018. The improvement of Q3/Q4 was on the back of terrible second half of 2017. It will be harder to repeat this year."

Last year they sold to 900 national and 900 international franchisees according to the 10-K, this year it stated 1000 national and 1000 international. If we combine that with the new online sales, 10% seems achievable in my opinion.

You comment: "They key going forward I think is Instagram sales and CBD. They just redesigned their web site, got a new CMO, and should start on picking up some "influencers"."

What do you mean by CBD? Cannabidiol? Are they planning to start selling CBD products?

Your comment: "By the way, gross margins on Amazon are probably more like 70%+. Amazon only takes 10% cut and all this powder takes only a few dollars to produce."

I would be happily surprised if margins on Amazon are 70%+.

13 May 2019, 04:52 PM

Lares Capital

@Maarten Pieters just because Compass announcement wasn't made before preferred stock issuance doesn't mean that FTLF management wasn't engaged in a discussion with Compass about extending the agreement and had an idea that it won't be extended.

In any case, Compass deal was bad for two reasons: they could only get money once they had account receivables but not to finance the inventory needed for Q1 after seasonally weak Q4. In the meantime, they were paying a full Libor + 5.5% on 3 million even though they couldn't really borrow due to the absence of A/R. You can check their cash balance at the end of Q3 and Q4 which makes it quite clear that they needed more capital.

12% on preferred wasn't unseasonable given this is subordinate to debt, attached warrants in my view were excessive (and dillutive).

Regarding the store count. I see it's up from last year but devil is in details as not all franchise stores are equal. There is also an unfortunate dynamic with closing GNC franchise stores: when a franchise store closes,

inventory often goes back to GNC parent, while it can't be returned, GNC can wait until it expires and then FTLF must take it back and write it off. Or going out of business franchise may dump it on eBay at fire-sale prices. So any franchise turnover is really hurtful. Franchise stores are still closing even though same store sales showed an unexpected improvement in Q1.

One of the less obvious reasons for Amazon is that prices there are actually higher that in GNC store (!). A GNC customer, who decided to check if he can get it cheaper on "the internet", sees Amazon's HIGHER prices (and good reviews). This is a great marketing tool.

All in all, having a HBS educated CEO with McKinsey experience and CPA to boot running a tiny company (and betting a farm on it) is a clear positive. I wouldn't say he is excessively compensated given his very modest salary of 250K (I believe). I have zero problem treating large shareholders better than (former) small ones - it's just business. Preferred was a mistake, but you can take solace that he issued straight debt after that, not more preferred.

So I think I am more bullish on CEO than you but somewhat less bullish (but still cautiously optimistic) on business.

13 May 2019, 05:48 PM

Maarten Pieters

Author’s reply » They are about to launch their first CBD product as part of the ISatori line.

20 Nov 2019, 04:03 PM

Connor Davis

Thanks, @Maarten Pieters . Where did you find this information?

20 Nov 2019, 04:47 PM

Maarten Pieters

Author’s reply » The instagram account of iSatori. What is also interesting is that they are increasing there efforts to find more instagram "ambasssadors" for Fitlife Brands: fitlifebrands.com/... A couple of people with a following of c. 10,000 people joined during Q3. Would be interesting if they can attract real "influencers" from the health/fitness scene.

21 Nov 2019, 03:38 AM

Connor Davis

Very cool. Thank you for sharing Maarten.

Yes agreed that will be interesting. They actually had a relationship with an old but pretty famous pro wrestler a few years ago, but I can't remember whom..

21 Nov 2019, 10:43 AM

Lares Capital
@Finsight Funds Brian Shaw, the former winner of strongman.

21 Nov 2019, 11:32 AM

Connor Davis
Hahaha, that's exactly him. Well done @Lares Capital

21 Nov 2019, 12:05 PM

Lares Capital
Singing up with iSatori on 2016 made him less strong ad he never won again:

www.muscleandfitness.com/...

21 Nov 2019, 06:25 PM