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OTC Bi-Weekly Newsletter #1

NOL SHELL, 'DISTRESSED' REAL ESTATE, INSURANCE BROKERS & UNCLAIMED FILMS

Summary of the report

- Today's favourite is an NOL cash shell trading at an interesting valuation with a clear catalyst as the biggest shareholder is ready to take advantage of the NOL base and buy out minority shareholders thus the time-adjusted ROI is likely to be attractive.
- The second pick is a company focused on a network of insurance brokers/agents, which has solid track record, pays out an interesting dividend and could generate meaningful cash flow.

First of all, I want to welcome members to the first ever issue of this new OTC Newsletter and I thank you for your interest in the research.

As I have stated in my announcement I hope that these reports will enable you to build a watchlist of companies that are potentially showcasing an opportunity in the OTC space. Through this you will be able to 'screen' the OTC space a bit more efficiently as on top of your own research you will always be able to come here and see what are some interesting tickers to research. One could think of it as Walker's Manual for the 21st century.

Over time this effort should lead to a formidable watchlist of the majority of OTC stocks that are running a sensible business and thus with every report the efficiency of screening the space should increase. I already covered 48 stocks in my previous reports where I provided a good starting point for further research but this included only a fraction of stocks that I have already gone over.

In every report, I will also highlight any previously covered stocks that might slowly become an investment opportunity or that at least deserve your attention.

Thus as per usual, without further ado, here are three stocks that I found in the past two weeks or so and that I believe could lead to actionable investment opportunity.

Before I dig in, I feel obliged to say; Caveat Emptor! Always do your own due diligence, and do not take the following tickers as a solicitation to buy.

Igo Inc. (IGOI)

Current Market Capitalization: $9.44 million
Tangible Book Value: $7.45 million

This company which used to focus on providing power accessories for electronic devices such as laptops or smartphones is now what could be called an equity stub or an NOL shell. The company does not have any operations and its balance sheet looks the following way;

iGO, Inc.
Balance Sheets
(Dollars in thousands)

	December 31, 2016	December 31, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,153	$ 5,689
Short-term investments	2,164	2,163
Accounts receivable, net	93	119
Inventories	25	59
Prepaid expenses and other current assets	21	42
Total current assets	7,456	8,072
Intangible assets, net	-	1
Total assets	$ 7,456	$ 8,073
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Accounts payable	$ 4	$ 2
Total liabilities	4	2
Stockholders' equity:		
Common stock, $0.01 par value; authorized 10,000,000 shares; 2,924,208 and 2,884,379 shares issued and outstanding, respectively	29	29
Additional paid-in capital	175,711	175,668
Accumulated deficit	(168,213)	(167,566)
Accumulated other comprehensive income	(75)	(60)
Total equity	7,452	8,071
Total liabilities and stockholders' equity	$ 7,456	$ 8,073

Source: IGOI's Press Release located at its website

As pointed out the stock has a significant amount of 'deficit' which should usually mean a significant NOL base. As it happens IGOI has roughly $180 million of net operating carryforwards which at the current tax rate could represent around $60 million worth of 'tax shields'. All this while the stock is trading at only a slight premium to net cash.

These entities are an interesting target for the enterprising investors/companies that want to shield their own profits from taxes as they can technically buy the entity and utilize the NOLs. The trouble most of the time is that this takes a significant amount of effort as NOLs are subject to a challenging amount of legislation and can evaporate if 'mis-treated'.

The good thing about IGOI is that such an investor already started to 'perfect' the entity for utilization of the NOL base and is in the last 'inning'. The majority shareholder is none other than

Steel Partners led by Warren Lichtenstein a group which seems to be continuously interested in these types of entities as can be witnessed by for example the action around MLNK, another NOL-rich entity (though which still has operations).

They have held IGOI for roughly three years now which allows them to proceed with the utilization through increasing ownership to near 100% by buying out the rest of minority shareholders, ‘inputting’ a profitable business (through various instances of shares-for-business transactions) and enjoying a tax-free income.

The interesting part in this for us is, of course, the buyout as SPLP will need to offer a reasonable price for the public shareholders. Why reasonable? Because if they were to try to take IGOI at a ‘low-ball’ price they would risk triggering appraisal rights or lawsuits attacking the price. Now, this does not mean that they are going to give investors significant premium, but it is safe to imagine that a premium larger than the current $2 million would certainly be reasonable. In the end unless the share price skyrockets to an unsustainably high price, it is almost a necessity for SPLP to take out minority shareholders at a premium. This would then present the upside in the stock.

A good write-up on Value Investors Club looks at the technical steps in a bit more detail and highlights several other transactions that SPLP did in the past and also mentions that the group could use IGOI soon due to SPLP’s consolidation of HNH, a holding company with substantial pre-tax operating income. Others pondered about the splitting of HNH and thus allowing each of the NOL shells owned by SPLP to effectively take care of the income.

The main risk to IGOI is that the time-adjusted ROI might not be that attractive. It could take SPLP too long to proceed with the buyout and thus any premium might be offset by the time investors had their stake in the company. This though could be slightly countered by the following argument. First, the company is pressed by time. Any NOL only lasts 20 years and IGOI has some that go back to years prior to 2000 and thus a sizeable amount (perhaps around $40 million given the 10K from 2000) could expire in around 2020.

Therefore only dubious trading could make the investment significantly loss-making (i.e. if IGOI investors start to sell - potentially to realize profit before buyout - people with higher cost base might not be taken out at a premium) but the downside would be limited given the necessity for a premium buyout and the balance sheet which should prevent trading below roughly $2.50 per share (which is the value of net cash) at least for a prolonged amount of time.

At the end of each stock description, I will always share some of my questions that I have not necessarily answered by the amount of research that I have done so far. This might help others that are interested (or already know about the stock).

- Are there any other scenarios where SPLP could take advantage of the NOL base while not performing the buyout and potentially diluting shareholders? I am not sure why would SPLP want to do this as they want to control the entity, but it might be important to understand the impact of other scenarios.
- What would an analysis of previous buyouts by SPLP show in terms of premium? This should be really helpful in determining the potential upside.

- Could I be missing anything material from the tax standpoint? Could there be a scenario which could completely prevent SPLP gaining benefit from the NOL base? It does not seem likely, but this risk should be looked at more closely.

P.S. This reminds me of WTLC an NOL shell that I have written about on Seeking Alpha. WTLC even trades at a discount to cash, but unfortunately the catalyst is not as clear as here, I would still though recommend trying to build a small position.

Price: $3.24

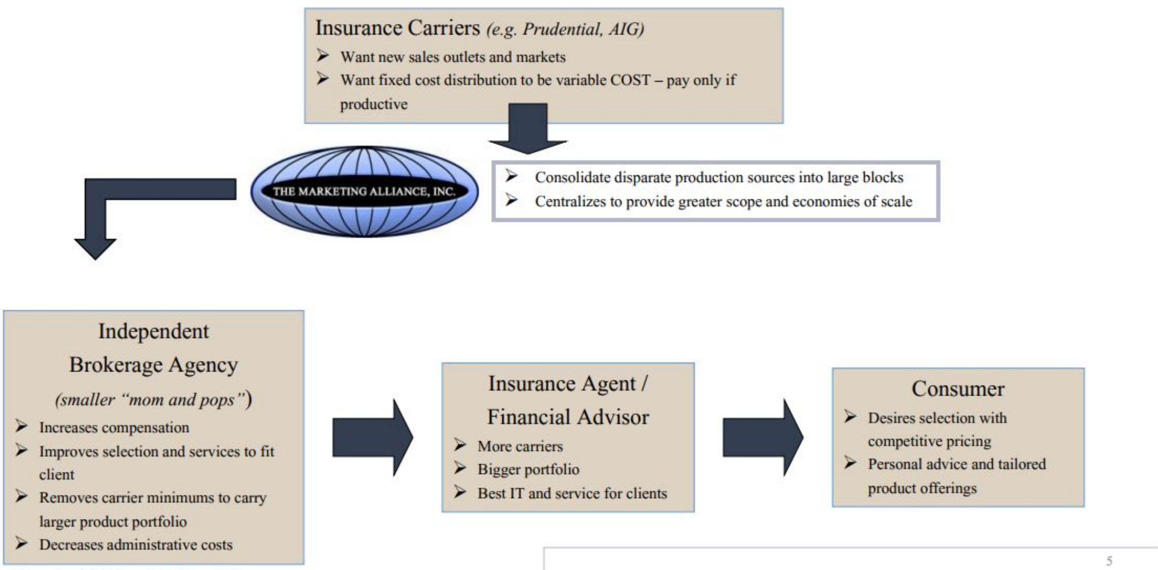
Volume (30-day average): 594

Reporting: Grey (but limited) - Website, SEC Available until 2013.

The Marketing Alliance (MAAL)

Current Market Capitalization: $19.679 million
Tangible Book Value: $10.5 million

This company has been able to significantly compound its earnings in the past due to a niche business model revolving around independent insurance brokers and agents. MAAL provided these 'mom and pops' operations with solid back office infrastructure and connected them to large insurance carriers which were interested in shifting portion of their fixed cost to a variable one. The following diagram is helpful in understanding the operations.



Source: December 2016 Investor Presentation

When one looks at the financial performance of MAAL they can see that the company has been able to build a slight 'network' effect as they have been able to grow their revenue (went from $15 million in 2007 to $27 million in 2014), maintain solid profitability (operating margin over 10%) and create meaningful stream of cash flow (generated over $2 million in 2015 and 2013) which is usually returned to shareholders via dividends (yield of which is now roughly 8%). This would then make the current premium acceptable and would make MAAL an interesting 'income' play.

Recently though this success has been under pressure and operational results from the past nine months are breaking the past trend.

The reason for this is mainly tied to the decline in revenue (MAAL reported $19.2 million in the past nine months as opposed to $21.35 million last year) which then weighs down on their profitability and cash flow. The reason for this decline is that Genworth, one of the insurance carriers, stopped providing several insurance products (life insurance and annuity policies) that agents connected to MAAL used to sell. The company does mention in their usual commentary that they believe the agents will be able to tap into new carriers which will make up for the shortfall and they did show that they are able to regain profitability in Q3.

The question though here is are they going to be able to sustain their dividend because of this slight 'downturn'? While it does not seem that the margins or the business model should be immediately threatened, the cash flow will need to return fast as their annual dividend comes at $1.47 million. In the past nine months though the company only generated $0.63 million of operational cash flow. They do have cash and investments (which look to be fairly liquid) on their balance sheet as seen below;

The Marketing Alliance, Inc.
March 3, 2017

Page 6

Consolidated Selected Balance Sheet Items

	As of	
Assets	**12/31/16**	**3/31/16**
Cash & Equivalents	$ 6,348,889	$ 5,535,256
Investments	6,841,572	5,802,222
Receivables	7,659,455	8,387,938
Other	1,256,843	1,325,135
Total Current Assets	**22,106,759**	**21,050,551**
Property and Equipment, Net	2,691,631	3,088,588
Intangible Assets, net	1,348,479	1,502,004
Other	883,970	978,783
Total Non-Current Assets	**4,924,080**	**5,569,375**
Total Assets	**$ 27,030,839**	**$ 26,619,926**
Liabilities & Stockholders' Equity		
Total Current Liabilities	$ 10,916,556	$ 10,561,554
Long Term Liabilities	4,382,593	4,643,386
Total Liabilities	**15,299,149**	**15,204,940**
Stockholders' Equity	**11,731,690**	**11,414,986**
Liabilities & Stockholders' Equity	**$ 27,030,839**	**$ 26,619,926**

Source: OTCMarkets.com Disclosure by MAAL

But this was partially increased by borrowing $4.5 million in the past year. The management though certainly seems confident as they even increased the dividend last year.

In the end I believe that this will be interesting stock to follow because it will either be able to sustain its dividend which could then make it an opportunity to earn a nice yield while being backed up by relatively stable business (which would be supported by their ability to sustain current operations despite Genworth) or it could struggle and would have to cut its dividend. This would probably force the shares to drop and it might be that the premium could be cut to a point where the stock could be an opportunity on the basis of valuation and the fact that the business is unlikely to completely die off.

An important event that could show us more will be the release of the annual report in mid-August. I will certainly write up a quick update once this happens to see whether the situation has changed.

Previously MAAL was covered by Dave back in 2013 and by one SA author who provided a quick overview of the company in 2011.

My outstanding questions are the following;

- The company also has two smaller businesses. Earth-moving company and business focused on child centers (think bouncy castles etc.). These investments that MAAL made in the past few years were actually profitable and did not act as a drag on the performance. Will this continue? What is the potential here? The earth moving business is at a cyclical low, but 'bouncy castles' seem to be doing fine. Most importantly one should look at the acquisition prices and compare it to the performance.
- What is the competition situation like regarding the insurance business? They might have a network in place which should be relatively safe, but I wonder if someone wants to disrupt that or whether the margins could be in long-term danger.

Price: $2.8

Volume (30-day average): 1,006

Reporting: Grey - Website & OTCMarkets.com

--End of Sample--

If you want to see the third pick of the report, updates from the watchlist and much more consider joining the newsletter here!

Financial Disclosure: I do not own any shares in the aforementioned tickers.