Svenda's Manual of OTC Stocks
Abridged

SAMPLE VERSION

Written by Jan Svenda, published on 17/10/2018

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The author could be a shareholder of some of the companies highlighted in the manual. Disclosure about his positions at publication date (of reports) can be seen at the end of each report.

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Foreword

First of all, I would like to thank you for showcasing interest in my research. I greatly appreciate it!

For the past year and three months, I ran a newsletter focused solely on the Over-The-Counter (OTC) market in the US.

During that time, I scoured the notoriously inefficient market for companies that are meaningful and exhibit an investment opportunity. No frauds, no pump and dumps. Only companies that are of interest for the serious *enterprising* investor (I tip my hat to Mr. Graham).

I like to think that I looked at every company in the OTC market at least twice. I went the A to Z route a couple of times, I maintained many simple screeners, I tracked Form 25s, 15s and much more. Given the sheer size of the market, one can't be completely sure of his/her coverage of the market, but I believe my reach is formidable.

As I expected, I stumbled upon many completely forgotten businesses that were either undervalued on the basis of their tangible book, cash flow or exhibited a special legal opportunity that one can take an advantage of. The following document is a compilation of my effort.

I present you with the Svenda's Manual of OTC stocks - Abridged which consists of all in-depth reports I wrote for the newsletter. These in-depth reports include 76 stocks which I believe/ed represent/ed investment opportunity.

Some of these long ideas have moved already, but 32 stocks did not yet register a meaningful move in their share price. Thus, I believe that there could still be valid investment opportunities in these reports. I include a quick up to date commentary for each stock highlighted in the reports.

In any case, I like to say that simply knowing about an OTC stock means you are halfway there. I have talked with many seasoned OTC investors that had no idea about some of the stocks I highlighted in the reports.

This can be extremely costly as most of the meaningful OTC stocks will exhibit an investment opportunity at some point in time of their existence.

This document will allow you to minimize the risk of this. If you want to further minimize this risk, please consider purchasing the full Svenda's Manual at jansvenda.com which includes an expanded coverage of the market with reports about 351 stocks.

If you are sceptical about the OTC market and want to know why I believe investing in OTC makes sense, please see the chapter 'How to argue about OTC at parties'.

Finally, as always, buyer beware! Please do your own research before buying any stock and do not use this report as an investment advice. It is merely a guide to parts of the hidden corners of the OTC market.

Acknowledgments

I would like to mention a couple of people that were indispensable in my investing/research journey. Some of the people I have met in real life, but most just through email or Skype.

Firstly, I would like to thank my father for asking which stocks I would invest in 2007 and thus starting my interest in the markets. I picked EA if anyone is wondering (it recovered in mere six years after the crisis).

Secondly, I would like to thank Tom Beevers and Tim Insko of StockViews who gave me great feedback. They taught me how to write investment research, form an investment thesis and most importantly through cooperating with them I was able to form my own view on valuation.

Thirdly, I would like to mention Thomas Braziel, whose brilliant research of Ethanex showed me the potential of the OTC market and got me into this niche.

I would also like to thank investors that have put out a significant amount of public OTC research such as Nate Tobik, Dave Waters, Dan Schum, Geoff Gannon, Safety in Value, or Maj Soudeian and his team over at GeoInvesting.

Fourthly, I would like to thank all members of the OTC investing community.

Among the people I can name are Nick Bodnar, Jim R., Thomas Niel, Ruerd Heeg, Dave A., David C., Eric S., Mark S., Chuck Gillman, Joe Sullivan, Richard K., Anthony W., Todd B., Thinley Wangchuk, Carl H. and many others.

Last but not least I would like to thank many members of Seeking Alpha, Value Investors Club and Corner of Berkshire and Fairfax with whom I routinely interacted and who certainly can’t be omitted.

I hope that the whole community will be even more vibrant in the coming years.

Table of Contents (Summaries of Reports)

Issue #21

Companies Highlighted

- Castle Group (CAGU)
  - **Business Description –** Hotel Management
  - **Opportunity -** Fundamental Value (Tangible Book & Cash Flow)
- Citizens Bancshares (CZBS)
  - **Business Description –** Community Bank
  - **Opportunity -** Fundamental Value (Tangible Book)
- International Baler (IBAL)
  - **Business Description –** Niche Manufacturer (Baling Equip.)
  - **Opportunity -** Fundamental Value (Tangible Book)

Summary of the report

- My favourite stock from this report is a manufacturing company focused on baler equipment. They operate a simple business that is generating a meaningful amount of cash flow yet the company trades at only around the tangible book. This valuation is unreasonable not only because of the profit, but because the balance sheet is also not accurately reflecting the value of their properties. While there is no clear catalyst ahead, the management might want to take the company private eventually.
- I also write about possible opportunities in a company that operates hotels in Hawaii and New Zealand and a community bank which trades at a significant discount. The hotel management company might now have a catalyst in place as the main shareholder passed away recently which could spur unlocking of the balance sheet value. The community bank recently improved its operations and is likely to start continuously generate ROE of above 10%.

Publication Date – 11/05/2018

Performance since Publication Date

- Castle Group (CAGU) – 33.3%
- Citizens Bancshares (CZBS) – 10.7%
- International Baler (IBAL) – 7.5%

Issue #24

Companies Highlighted

- Vulcan Corporation (VULC)

Business Description - Holding Company

Opportunity - Fundamental Value (Tangible Book)

Summary of the report

- Vulcan Corp. value is predominantly in a large stock portfolio amassed in the past three decades. They are hiding it from investors as shareholders are required to sign NDAs.
- The lack of information is no longer a significant problem as their 2016 financials recently surfaced.
- Their liquid stock portfolio is discounted by the market by at least $22 million. If we add their real estate assets there could be an upside potential of 76% here.
- The management is happy with the status-quo and disrespects the minority shareholders. While they do not actively burn the value of the company, they are not utilizing it.
- The situation might change. VULC is likely liable to file 13F form which could add transparency without the need of change in management's attitude. This would act as a catalyst.

Publication Date - 22/06/2018

Performance since Publication Date – 21.7%

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OTC Bi-Weekly Newsletter #21

HOTELS, BALERS & CLASSIC COMMUNITY BANK

Publication Date – 11/05/2018

Update Comment

- International Baler Corp. (IBAL)

The shares have failed to move so far. This is clearly because the company did not really announce anything that would change the current narrative. The investment thesis continues to be long-term and will likely rely on the management taking action and either selling the business or rolling it up into the related businesses of the insiders.

- Castle Group (CAGU)

They have seen wild swings in their share price which allowed investors to unlock at least part of the upside that materialized. The trading was likely fuelled by the fact that the company is going dark and will deregister from the SEC which could help them to save a material amount of money.

- Citizens Bankshares (CZBS)

These bank shares have not performed well despite the fact that the company is showing material improvements in net income and the discount to tangible book is still present. Perhaps investors might be worried about parts of the loan book which might deteriorate as interest rates rise.

Summary of the Report

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- I also write about possible opportunities in a company that operates hotels in Hawaii and New Zealand and a community bank which trades at a significant discount. The hotel management company might now have a catalyst in place as the main shareholder passed away recently which could spur unlocking of the balance sheet value. The community bank recently improved its operations and is likely to start continuously generate ROE of above 10%.

International Baler Corp. (IBAL)

Current Market Capitalization: $10.37 million

Tangible Book Value: $9.04 million

Price: $2.00

Volume (30-day average): 369

Reporting: SEC

I have added this manufacturing company to the database in late August of last year due to its valuation and operations. Since then the stock has not moved yet the company still exhibits the same positive factors.

Investment Thesis

I believe that investors are going to benefit from accumulating a position in IBAL due to the following points;

- First and foremost, the company is well managed and is able to maintain its meaningful cash flow stream even if the revenue can be volatile. In 2017 they were able to generate $1.51 million of free cash flow. These operations then helped to grow the tangible book which is up $6 million since 2007. They also now have a cash position of over $4 million.
- The balance sheet is presenting a sufficient margin of safety as the company holds its PP&E at underappreciated value. They own a 62,000 square feet facility in Florida. The whole PP&E is carried at $1.3 million. The facility alongside the equipment could be worth around $3 million. Thus, the current slight premium to tangible book is not an issue. They also have zero debt.
- The insiders who own the majority of the company could have an incentive to merge IBAL with other baler-related companies that they own. Thus, the final catalyst could be clear here.

On the other hand, one has to be aware of the following risks;

- While the long-term catalyst could be present, short-term catalysts might be missing. Their operations are doing fine, yet the shares have been stuck at the same valuation for the past four years. This could mean that the next two to three years might be similar if the management does not act.
- The insiders might be tempted to low-ball the offer for the company. This could present a risk that investors can hold IBAL for the long-run and after several years might receive immaterial investment return. However since IBAL is still reporting to SEC and the insiders have not acted against the interest of minority shareholders the risk of this could be low.

I believe that the downside risk here is limited. The operations are unlikely to suddenly collapse and the balance sheet is presenting a sufficient margin of safety. The upside potential is clear and not offset by the aforementioned risks. However, there is clear uncertainty as to the unlocking of that upside potential. Thus, I would label IBAL as a classic OTC 'buy and hold' stock.

Company Overview & Financial Performance

This company is focused on recycling equipment, namely balers which work with various materials from plastics to paper. This is a relatively simple business that might sound as obscure as mail inserting machines that SORT was producing. However, I would wager that the need for baler equipment is unlikely to be in decline when the focus on recycling has been increasing in the past few years.

While the technology is relatively primitive I have not found any alternative to it. Thus, the product is unlikely to become obsolete in the near future. Note that compactors which aim for a similar outcome are mainly used for different materials.

What is also positive is that IBAL has been able to position itself well in this relatively 'unexciting' market. They focus on high-end custom balers which produce above-average margins. A quarter of their revenues also come from repairs and maintenance which support the revenue stream and profitability.

However, their revenue can be slightly volatile due to this focus as they rely on the higher-end products to drive increased profitability. This effect can be clearly seen when one scrutinizes IBAL financials.

In the years since the financial crisis the company routinely registered annual revenues higher than $15 million which resulted in an annual net income around $1 million. In the last two years however, their revenue has slipped and stayed around $10 to $11 million which lowered their net income to $0.1 million. The reason for this is the lack of high-end orders.

While this might seem negative I would point out that the revenue is resilient and that despite the lower net income in the last two years I do not expect the downturn to continue. Their sales order backlog is stable. The recent quarter also showed double the amount of revenue than in Q1 of last year. They generated $0.2 million of net income in that quarter alone.

Even during the financial crisis, the company only generated a small loss in 2009. They generated significantly lower revenue but were able to benefit from the right-sized operations which prevented continuous losses. Thus, the stock should trade above its tangible book given the cash flow it can generate even if the actual generation can be lumpy.

This is especially true when their tangible book is over depreciated and their whole PP&E item which includes 62,000 square feet facility in Florida is carried at only $1.3 million. One can easily search for property offerings which assign a higher value to the property. Even this basic warehouse with no equipment is valued at $1.5 million. I believe that their property could be sold closer to $3 million especially when they likely own equipment that might not be worthless.

While it is challenging to assign a valuation for the company due to the lumpiness of the revenue, one can easily see that the shares should trade higher. At the very least the downside protection should be sufficient.

Management incentives

The reason for the stock to trade at the current valuation could be due to the lack of catalyst. The company has been able to report stable results but that failed to meaningfully move the share price for the past four years as can be seen below.

However, that did not stop the insiders to further accumulate their ownership. The largest owner is now Leland Boren who owns 78.1% of the company and who started to accumulate his position in the early 2000's.

I believe that this fact could be the ultimate catalyst here. While it is uncertain when it could occur, it is likely that the insiders would want to take the company private. This is especially relevant since Mr. Boren owns a controlling stake in Avis Industrial which is a company that owns at least three competitors of IBAL. They own American Baler and two other subsidiaries both of which were acquired in 2014 as can be seen here and here.

While it seems perfectly natural for Avis to buy IBAL, I believe one should ask the question why did not they do so yet? Maybe they are just waiting to have excess capital as they could have depleted their reserves for those two acquisitions three years ago.

However, it could also be that the insiders are continuously increasing their ownership of IBAL so that they can take the company private at a low-ball price. Since Mr. Boren controls Avis, the results of IBAL could be tied to how the other three competitors behave in the market. While they might be focused on slightly different products, it is slightly disconcerting to see this setup.

One could certainly counter this and say that Mr. Boren has interest in all companies. Thus, he needs to make sure that they all prosper, but then I wonder why did he not buyout the rest of the shareholders already. They could certainly realize savings from the merger.

Therefore, it seems that the insiders could potentially have conflicting incentives that might hurt the minority shareholders. Although as of now this is not an issue. The operations continue to be stable and the company does not seem to make any reckless moves that would somehow impair the value of IBAL, i.e. the insiders do not seem to act under the influence of either incentive for now.

I would also point out that Mr. Boren is 94-years old. His son, who is a director of IBAL is likely to take his place eventually. I am not sure whether this would change the behaviour of the insiders.

Conclusion

Despite the potential for slightly conflicting incentives, IBAL is showcasing an upside potential and clear downside protection. Their operations are stable and able to generate a meaningful amount of cash flow which justifies the current premium to tangible book. Moreover, this tangible book is unlikely to be accurate as their facility in Florida should be more valuable than their entire PP&E item.

The question is when will the management move to unlock the value via a buyout. As with many OTC stocks this is not clear, but that is unlikely to hamper the eventual investment return.

Finally, I would point out that the company changed its language regarding its dividend policy. Before 2017 they stated that they do not expect to pay any dividends in the near future. They removed this sentence in the latest annual report.

The outstanding research questions are the following;

- Why did not they merger with Avis yet?

Castle Group (CAGU)

Current Market Capitalization: $3.02 million

Tangible Book Value: $2.01 million

Price: $0.30

Volume (30-day average): 376

Reporting: SEC

I have added CAGU in middle of September 2017 due to the attractive cash flow and valuation. Safety in Value also shared a report with our newsletter and pointed out to the upside potential. The upside realized as the shares did trade at $0.5 per share for a while after the addition. However, now the shares are back at the initial price which prompted me to research the name myself.

Investment Thesis

I believe that investors are likely to benefit from accumulating a position in Castle Group due to the following points;

- First and foremost, the operations are strong and present upside potential. They constantly increase their tangible book since 2007, most recently by $0.3 million in a year. They are likely to continue to do so if the macro environment does not dramatically deteriorate. Even if it should their performance during the crisis was positive. They were able to generate cash flow each year and generated losses mainly due to forex movements.
- The balance sheet acts as a margin of safety. They are able to shed their debt and their New Zealand property which was originally purchased for $8 million could even be over depreciated. They also hold other investments which could further support this point.
- On their own these two points are strong, but what I believe could accelerate the share price appreciation is the fact that the CEO and the largest shareholder has passed away just a few days ago. This could spur savings on executive compensation and the estate of the CEO might want to unlock the value through a sale.

On the other hand, one has to be aware of the following risks;

- There could be uncertainty as to how the management will run the company. There is also a risk that certain contracts might be forced to be renegotiated as they were connected to entities owned by the CEO. However other insiders own 19.1% of the company and they are likely incentivized to maintain the status quo.
- The revenue of the New Zealand property is shrinking. Part of that is due to the foreign exchange rate, however it is likely that the results are stagnating. While it is not hurting the operations now, it should be on investors mind.

I believe that the risks are not offsetting the otherwise strong fundamentals which create value for shareholders. Even if the insiders and the estate of the CEO do not decide to pursue a sale, the operations are likely to drive further increases in tangible book which should equate to an increased share price.

Company Overview

This company started out as hotel management company in Hawaii in the 1990's. They take care of the facility and generate revenue from the underlying contracts. They have been able to successfully grow these operations and kept on adding new hotels or resort condominiums in Hawaii since the start of the company.

In early 2000's they started to expand outside of Hawaii and purchased a part of a hotel in New Zealand (Spencer at Byron, 4-star hotel with decent reviews) for $8 million. They also invested $1 million in another entity in 2010. Most recently they put up $0.2 million for a small stake in another New Zealand entity. They also tried to manage hotels in Asia before the financial crisis, but they discontinued this focus.

Valuation & Financials

Their business efforts have resulted in the generation of shareholder value. Most importantly the company has been able to continuously grow its tangible book since 2009. After the crisis, the company had tangible book of roughly negative $3 million compared to the current tangible book of $2 million or $5 million increase in 9 years.

This translates to an average increase of $0.5 million a year which is material when the current market is roughly $3 million. Most recently they grew the book by $0.3 million. The reason I am using the tangible book is to adjust for the working capital cycle of the company.

While it is clear that the operations are exposed to the macroeconomy, the company was actually able to generate cash from operations even during the crisis when adjusted for the forex movements. This shows that they might be operating high-end hotels and resorts which are not as susceptible to a deteriorated economy.

In any case, one can track the 'health' of tourism in Hawaii through their monthly performance reports. So far it seems that the growth should not stop as the tourist spending increased 10% and the number of total visitors was up 9.4%.

Due to all these points, the Hawaiian operations point to a clear upside should the status quo remain.

The New Zealand property then provides a margin of safety. While the operations tied to the hotel are not generating as much cash flow as Hawaii operations and have been declining recently (partially due to the forex movements), it is unlikely that the real estate should lose its original value. If anything, it should increase since 2004.

However, we can be conservative and assign acquisition price to the property which would already increase the tangible book by at least $2 million as the whole PP&E item (which includes other investments) is held at $6 million.

While one should take into consideration the preferred shares of the company which are resembling a simple loan and have a face value of $2.4 million, the company owns other investments that could at least partially offset the preferred shares.

Thus, CAGU is able to generate tangible book growth somewhere in the realm of 6x to 10x the current market capitalization and owns property that at the very least provides sufficient margin of safety.

Current Management Situation

As I have mentioned in the thesis the operations alone could spur share price appreciation should the results continue. However, as the CEO who was also the biggest shareholder (held over 33% of the stock) passed away recently there could be a catalyst for accelerated share price appreciation.

The estate of the CEO might be interested in unlocking the value of the company and push for a sale in order for them to monetize the asset. The company is not paying dividends and thus a sale would probably be the most straightforward step. I am not certain whether the CEO has any descendants, however they certainly were not involved with the company. Thus, the estate is so far not generating any salary from the company either.

While this could result in just the estate selling their stake, I believe it could be easier to sell the whole company or sell it for parts (the Hawaii operations and the New Zealand hotel).

I would also point out that the CEO's compensation was material at around $0.2 million annually which could help the underlying results of CAGU for at least this year. They do seem to look for a replacement as stated in this article.

However, there could also be risks involved as the CEO was likely to be the 'key person' behind the business strategy and should they remain public the company might struggle to keep up with the past performance. As of now, this is unclear, and the other insiders own enough of stock (roughly 19%) for them to be incentivized to maintain status quo.

Conclusion

Even if the insiders and the estate do not push for a sale, I believe the upside should be realized eventually. Their New Zealand property presents a clear margin of safety as it is likely held at over depreciated value on the balance sheet.

The operations in the US present the potential upside as they have been able to continuously increase their tangible book. Barring a financial crisis this should not stop. The balance sheet is also ready for a crisis-like environment.

Finally, I would like stress that due to relative illiquidity it might take time to accumulate position at the right prices as the bid/ask spread is quite significant. There were a handful of trades at around $0.21 per share, but the stock did jump around $0.30 per share as well recently.

As always limit orders are a necessity. I also believe that this is a 'tradeable' stock. You can enter at around $0.20 per share and then set up a sell order for around $0.40 or $0.50 per share.

The outstanding research questions are the following;

- Would the management be willing to share detailed financials for New Zealand operations?

Citizens Bancshares Corp. (CZBS)

Current Market Capitalization: $29.42 million

Tangible Book Value: $40.04 million

Price: $12.99 per share

Volume (30-day average): 387

Reporting: FDIC / Website

I have added this community bank roughly two weeks ago due to its intriguing valuation which warranted further research.

Investment Thesis

I believe that Citizens Bancshares (CZBS) is a good statistical addition to investors' community bank portfolio due to the following points;

- Most importantly the bank has been able to regain its material profitability from before the financial crisis. Recently they got rid of their TARP preferreds, acquired a new loan portfolio and improved their cost structure. Without the one-time effect of the new tax bill they would generate ROE of around 10%. They are likely to maintain this profitability as Q1 of 2018 seems to point to similar results. This means that the company is likely to trade below 10x P/E in the near future.
- The current discount to tangible book then creates a margin of safety and could present a catalyst should the operations continue to operate at similar profitability levels in the next year or two. Their tangible book also grew since the financial crisis as the bank was able to attract new deposits.

On the other hand, one has to be aware of the following risks;

- Their loan concentration could become an issue in the next crisis. Out of the roughly $400 million assets they hold $50 million in church loans. While they do not have a meaningful portion of either OREO or nonaccrual loans, the church loans could be pressured more than the rest of their portfolio in a crisis environment.
- The areas they serve, Georgia and Alabama are also not showcasing stellar performance on a macroeconomic level and should there be a recession the areas are likely going to get hit again.

While the risks are certainly visible, I would point out that the company has a better capital position than prior to the financial crisis and their asset base could be better diversified. Thus, the discount is unlikely to be justified, especially when they are now able to maintain a strong profitability.

Core ratios

- T1 Capital Ratio (last quarter) – 14.8417%
- Return on Equity (ROE, trailing twelve months) – 5.12%
- Return on Assets (ROA, trailing twelve months) – 0.55%
- Efficiency Ratio (trailing twelve months) – 77.02%
- Net Interest Margin – 3.63%

Overview of the bank activities

Citizens Trust Bank is a community bank operating in Georgia (mainly Atlanta) and Alabama (mainly Birmingham).

They focus on commercial loans, commercial mortgages and single family residential loans. Their loan book is now worth roughly $253 million of which $67 million is tied to single-family loans. $100 million is tied up in commercial mortgages and roughly $37 million in commercial loans. The rest is a mix of construction loans, small portion of multi-family residential loans and others. Part of this loan portfolio was acquired in 2017. I would also point out that the bank is focused on the African American community.

Other than their loan portfolio they also hold $101 million in securities which consists of $20 million in US govt. securities. The rest is mostly mortgage securities backed by the government. They hold only $11 million in commercial MBS which are still guaranteed by the government. They also hold $19 million in interest-bearing cash and $15.3 million in federal funds sold.

This relatively conservative setup allows them to achieve sufficient capital ratios.

They fund this asset base mostly through non-brokered deposits (FDIC states they had $20 million of brokered deposits), they hold an immaterial amount of borrowing connected to their properties. Out of the $366 million in deposits, $126 million of the total amount was non-interest bearing.

Financial Crisis Performance

CZBS had clear issues during the financial crisis although they started to feel the challenges after 2009. They were forced to take significant provision for losses and accumulated a significant amount of nonaccrual loans (top was $16 million in 2009, but in 2011 they still had $13 million) and a large OREO asset ($10 million in 2011). This forced the operations to report losses in 2010, 2011 and 2012.

I believe that the performance was mainly driven by the relatively poor quality of their loan portfolio. They held roughly $40 million in church loans during the crisis which likely performed badly. The areas that the bank is operating in are also an issue as neither Georgia or Alabama are states with robust economies.

However, I would point out that the losses were relatively small. They never generated an annual loss bigger than $1 million and they continued to pay dividends throughout the crisis. They took TARP worth $12 million, but I believe that they would survive without it.

Scenarios going forward

Unlike in other community banks I have highlighted, if the status-quo prevails it should easily point to share appreciation. They were able to get rid of the problematic loans and their balance sheet is now clean.

Thus, they are now likely optimized to generate roughly $1 million in net income per quarter (this was the Q1 result). This would mean that they could generate roughly $4 million in a year (which they almost did in 2017 should one discount the tax bill effect). This would mean that at the current price they would trade at P/E of 7.5x which is certainly attractive valuation in the current market.

This profitability could also allow the company to grow their tangible book which could then again support share price appreciation.

While one could raise issues with their asset base, I believe that the picture is different from the one prior to the financial crisis. Thus, the current discount presents a sufficient margin of safety.

Their reliance on loan performance is not as crucial as their capital position is better. Their total assets are higher by $90 million compared to 2007 and most of that increase is in securities and interest-bearing cash. The loan portfolio is up only $10 million.

Their nonaccrual loans are also smaller. In 2007 the company already had $5 million of loans in nonaccrual status. Now CZBS has only $1.6 million of nonaccrual loans. Their OREO was also larger in 2007 at $2.4 million compared to just $0.6 million in the current quarter.

I would also point out that their asset base was encumbered by borrowings which are now missing. This could allow better financial flexibility should they face a challenging environment.

Thus, the performance of the bank in a crisis-like scenario could be materially better than during the last one.

Conclusion

I believe that CZBS is a good addition to a portfolio of community banks. While their asset base might not be as conservative as in some other banks, their profitability is offsetting this. The current discount to tangible book is providing investors with sufficient margin of safety.

I also believe that the state of their financials is materially better than before the last financial crisis. Thus, the repeat of the same challenging performance might not be likely if worst comes to worst.

The outstanding research questions are the following;

- How did they maintain their church loan portfolio? Did they originate loans to new entities or have they supported the older ones?

Financial Disclosure: I do not own shares in any of the aforementioned companies at the publication date.

OTC Bi-Weekly Newsletter #24

EPITOME OF DARK COMPANY

Publication Date – 22/06/2018

Update Comment

VULC has seen an important press release in early October 2018. The management decided to liquidate the company which should provide a clear catalyst for unlocking of the upside. However, there are a couple of moving parts (stock portfolio, taxes, value of operations etc.) and thus shareholders should continue to closely scrutinize what is going to happen.

Vulcan International – Epitome of a Dark Company

Summary

- Vulcan Corp. value is predominantly in a large stock portfolio amassed in the past three decades. They are hiding it from investors as shareholders are required to sign NDAs.
- The lack of information is no longer a significant problem as their 2016 financials recently surfaced.
- Their liquid stock portfolio is discounted by the market by at least $22 million. If we add their real estate assets there could be an upside potential of 76% here.
- The management is happy with the status-quo and disrespects the minority shareholders. While they do not actively burn the value of the company, they are not utilizing it.
- The situation might change. VULC is likely liable to file 13F form which could add transparency without the need of change in management’s attitude. This would act as a catalyst.

Investment Thesis

I believe that Vulcan International (VULC) is presenting investors with an attractive opportunity even despite having one of the most obscure corporate setups out there in the 'public' OTC market.

The company is deregistered from the SEC and forces shareholders to sign a non-disclosure agreement (NDA) when they want to see VULC's financials. The family that still owns a significant stake in the business is not open to minority shareholders and defends their secretive way of operating the business in court. In other words, VULC is the epitome of a 'dark company'.

However, there are clear signs that at the current share price the business is still undervalued as the 2016 financials has recently surfaced and allowed the broader public to see what the company owns.

- While the company is operating a small rubber & foam manufacturing facility, the core value is in its stock portfolio which has materially appreciated since the financial crisis. It provides both a material dividend stream and a clear upside potential for investors. In 2016 the portfolio provided the company with $3 million in dividends and is now likely valued at around $161 million as per updated Nate Tobik's assessment. This compares well with the current market capitalization of roughly $106 million.
- The portfolio is not the only valuable asset. Their real estate holdings are overdepreciated. Despite the fact that the manufacturing facility is losing money, the underlying real estate is likely to be valuable and could be worth at least $4 million as per property tax assessment. They also own large timber holdings in around Michigan which could add up to $14 million. Lastly, they develop real estate from time to time which is troublesome to track without the update financials but could add at least $7 million (based on property tax assessment) to the valuation.
- One might think that the current discount to the potential value of the assets could be partially justified given the OTC trading, family control and lack of information. However, there could be a catalyst that could force the management to be more transparent. The catalyst is tied to form 13F which is regularly filed by investment companies which own over $100 million in securities. The form shows their exact positions. VULC is likely to be liable to file this form even though they are not registered with the SEC and they are not an 'investment company' per se. If they file such form the market might be more comfortable in repricing the shares higher and closing the discount.

On the other hand, one has to account for the following risk;

- The corporate governance is terrible. As mentioned the insiders are treating minority shareholders as something to be dealt with in court and through NDAs. They also do not seem to be open to strategic alternatives as the state of the business remained the same for the past few years with the dividend stream being burdened by the money-losing manufacturing facility. At least they do not burn cash and do pay out a small dividend.

While the corporate governance is far from ideal, it does not fully offset the upside potential. The management is not actively destroying any of the value, it is just not utilizing it well and tries to hide it.

Company Background

Before VULC became the infamous dark company in the OTC circles, it was able to build a successful rubber shoe product business that in the 1970's operated 28 factories throughout the US. However, as the foreign competition entered the market in the 1980's the business started to face increasing challenges which ultimately forced VULC to exit most of the operations.

During this tumultuous period, the company was steered by the previous management team which mainly revolved around Benjamin Gettler and Lloyd Miller II., father of the famous small-cap investors Lloyd Miller III.

After the downturn, they sold most of the operations and put proceeds into the stock market. Since the end of 1980's they only maintain a manufacturing facility in Clarksville, Tennessee which is generating a small amount of revenue at a loss.

The story complicates in the early 1990's after Lloyd Miller II. died and his son succeeded him. Due to what likely was a troublesome relationship with the board, Lloyd Miller III. decided to exit the investment. He got paid for most of his shares and signed a release form. At this point, the Gettlers became the key shareholders and control more than 50% of the shares.

One can read about the whole situation in the biography of Benjamin Gettler.

In the 1990's VULC continued to stagnate. There were no significant developments in the manufacturing business. Their income from dividends was the major reason for their profitability in that period as per their SEC filings.

As there was no change to be seen at the beginning of the 21st century, the company decided to deregister from the SEC to save cost and lessen the regulatory burden.

Miller's Lawsuit

Since then they were operating in the dark. Only shareholders had the opportunity to understand what has been happening and only if they signed the NDA.

The stock might still lay dormant and unnoticed if it hadn't been for Lloyd Miller III. who started to buy shares of VULC again sometime in the 2000's. He accumulated a meaningful position and wanted to see how the company is doing. Thus, he requested financials.

He faced an uphill battle as the management was not forthcoming and declined to give him the information. In the meantime, Benjamin Gettler died and his son Thomas Gettler, a lawyer, became the main voice of the company. He acts as a legal counsel for the company and is on the board of directors.

Miller resorted to filing comprehensive requests based on Section 220 of the Delaware General Corporation Law, but even this did not work. The main argument of the management was that Mr. Miller signed a release in 1991 which prevents him from making any claims. Mr. Miller started to sue VULC and the judge was not impressed by VULC's argument, however Miller and VULC decided to settle the case out of court. The court filings can be accessed via PACER.

Increasing Interest

While this could have stirred an interest in the company, the main issue around 2014 was still the fact that shareholders that have seen the financials were tied by the NDA they were forced to sign. Thus, the increased interest could not replicate.

The first major break for the company came in 2015 when Nate Tobik wrote about the company on his blog. He did not provide specific numbers as he did not see the financials but he alluded to what could be the value of the company (the stock portfolio) and he provided basic background information.

The share price jumped, and more OTC investors started to scrutinize the company.

The share price languished in 2016 but since 2017 has been increasing continuously until it reached the current highs.

Release of Financials

As we have learned in May of this year the share price action was completely justified. One day Nate received an envelope containing the raw audited financials of the company for 2016 and 2015. Apparently, it came from the sister of Thomas Gettler.

The tangible book of the company in 2016 was $102 million which roughly matches the current market as can be seen below.

Consolidated	
Assets (in millions)	Q4 2016
Inventories	$ 0.08
Current Marketable Securities	$ 1.55
Cash and Cash Equivalents	$ 2.96
Prepaid Income Tax	$ 0.01
Assets Held for Sale	$ 2.55
Account Receivables	$ 0.52
Deferred Income Taxes	$ 1.31
Total Current Assets	$ 8.98
PP&E	$ 1.04
Marketable Securities	$ 137.94
Other Assets	$ 0.03
Total Assets	$ 147.99
Liabilities (in millions)	
Notes Payable	$ 2.01
Accounts Payable	$ 0.21
Accured Salaries	$ 0.09
Accured Other Expenses	$ 0.32
Total Current Liabilities	$ 2.63
Deferred Income Taxes	$ 41.14
Other Liabilities	$ 0.77
Total Liabilities	$ 44.54
Current Market Cap.	$ 106.70
Tangible Book	$ 102.14

Source: Audited Company Data

Note: VULC has a defined benefit pension plan, however, the asset base is small, and the underfunded liability is only $0.7 million.

The income stream was unchanged as the manufacturing facility kept on losing money and the dividend stream acted as an offsetting factor.

(in millions)	2016	2015
Net Sales - Rubber / Foam	$ 4.02	$ 4.06
Real Estate - Timber	$ 0.14	$ 0.30
Real Estate - Commercial	$ 0.79	$ 0.63
Total Revenue	$ 4.94	$ 4.99
Cost of Sales	$ 3.36	$ 3.47
Operating Expenses	$ 0.99	$ 0.97
G&A	$ 2.06	$ 2.29
Interest Expense	$ 0.04	$ 0.03
Total Expenses	$ 6.44	$ 6.75
Operating Income / Loss	$ -1.49	$ -1.76
Operating Margin	-30.21%	-35.30%
Dividends and Interest	$ 3.02	$ 2.88
Net Gain on Sale of PP&E	$ 0.20	$ 0.04
EBT	$ 1.73	$ 1.16
Provision for Tax (benefit)	$ 0.12	$ -0.07
Net Income	$ 1.62	$ 1.24
Number of Shares	0.91	0.91
EPS	$ 1.77	$ 1.35
Cash Flow From Operations	$ 1.27	$ 1.27
Cash Flow From Investing	$ 2.17	$ -1.01
Cash Flow From Financing	$ -0.94	$ -0.59

Source: Audited Company Data

The valuation

While the share price action was justified, some might now be wondering why I believe that there is still plenty of upside left. The company trades at its tangible book from 2016 and generated only minuscule profit that does not really ask for a significant premium.

However, one has to remember the nature of the balance sheet. Most of the value is in a stock portfolio. Thus, one needs to adjust the value for the share price developments of their holdings. Unfortunately, the financials do not break down each position, however Nate has shared an assessment of their portfolio based on positions from 2000's.

According to Nate, other VULC's shareholders have confirmed that this is a relatively accurate assessment. One can support this assertion by looking at the income statement or cash flow which did not show any realization of the positions in either 2016 or 2015. Thus, management is unlikely to trade frequently.

I have updated the assessment to reflect the current prices.

Stock Position	Shares	Share Value as of 19/06
Vodafone Airtouch PLC (VOD)	16027	$ 393,302.58
Verizon (VZ)	40823	$ 1,971,342.67
Frontier Communications Corp. (FTR)	17000	$ 132,090.00
AT&T (T)	213204	$ 6,907,809.60
Cincinnati Bell (CBB)	42820	$ 610,613.20
Convergys (CVG)	182000	$ 4,579,120.00
Duke Power (DUK)	14313	$ 1,082,635.32
NextEra Energy (NEE)	64750	$ 10,502,450.00
CenturyLink (CTL)	2534	$ 46,752.30
Consolidated Communications (CNSL)	468	$ 6,172.92
Enbridge (ENB)	12300	$ 391,755.00
PNC Financial (PNC)	659090	$ 93,491,916.50
U.S. Bancorp (USB)	783441	$ 40,229,695.35
Prudential Financial (PRU)	259	$ 25,216.24
Principal Financial Group (PFG)	6165	$ 343,267.20
Piper Jaffray (PJC)	7834	$ 627,346.72
Grand total		$ 161,341,485.60

Now one must remember that this portfolio value does not take into account the capital gains tax liability which was standing at $41 million in 2016. As the marketable securities were valued at only $137 million then, one should expect this liability to change.

However, one must account for the recent change in the tax code which lowered the tax rate thus, the liability is lower than in 2016 in the end. It could be around $33 million (current gains * tax rate). Thus, the net value of the portfolio in a liquidation scenario would be around $128 million.

There are ways for VULC to side-step the liability and try to either eliminate or minimize the effect of taxes. One example strategy could be to exchange some of the stocks in the portfolio for VULC. A potential acquirer could also perform a stock exchange which would result in a similar tax minimizing effect.

This portfolio then provides a straightforward and strong margin of safety and clear upside potential.

What makes VULC even more attractive is the rest of the balance sheet which is overdepreciated and hidden in the PP&E item.

As mentioned VULC still owns and operates the Clarksville facility. While the business is unlikely to have much value, the underlying real estate certainly does. One can take the appraised value of the county property assessor which stands at $3.87 million.

The company also holds a material investment in timberland around Michigan. VULC still owns 14,000 acres as per 10K from 2005. One can see that the asset value for timberland in 2016 is the same as in 2005. One can check Keweenaw Land Association (KEWL), a timber company operating in the area, for price per acre which comes to about $1,000 per acre, or $14 million for VULC. One has to remember that this would also be subject to corporate tax in the event of liquidation.

VULC also ventures into real estate developments. Probably their most valuable holding could be the Cincinnati Club building which they hold at the balance sheet since at least 1996. The market value assessment comes out at $4.39 million (due to this and this assessments which are for different parts of the building). One can't forget the Florida asset held for sale on the balance sheet which was valued at $2.5 million in 2016.

They also bought a mall for $3.8 million in 2017. However, the value of that could be relatively the same since the acquisition thus I am not going to include it in the valuation.

Finally, there is $4.5 million on the balance sheet which comprises of the cash and current marketable securities in 2016.

Putting all this together we can come up with a solid upside potential.

Valuation		
Main Assets		
Stock Portfolio	$	161.31
Michigan Timberland	$	14.00
Potential Tax Liability	$	-35.46
Other Assets		
Clarksville Facility	$	3.87
Cash + Current Stocks	$	4.50
Cincinnati Club	$	4.39
Florida Asset	$	2.50
Total Other Liabilities	$	-3.40
Total Value with Tax	$	151.71
Upside to Current Price	43%	
Total Value without Tax	$	187.17
Upside to Current Price	77%	

As you can see even if one takes the tax liability into account there is a solid opportunity currently present. However, as aforementioned, it is likely that VULC would be able to eliminate or minimize such a liability and significantly increase the upside.

13F Form as a Catalyst

As mentioned in the thesis, investors might be sceptical about the upside. They can argue that the discount is rightfully in place given the attitude of management towards the minority shareholders and the unknown status of the financials. Not many people are willing to take an investment decision without knowing the exact current situation.

This could change soon, and we might not need to wait for the insiders to understand how a management team of a public company should behave.

The reason behind this is a 13F form which VULC is likely liable to file with the SEC. Before I get into a more detail argument, one should be aware of the fact that form 13F is exempt from the deregistration from the SEC as per this helpful paper. Thus, even if VULC is deregistered they are still liable to report these.

The 13F is normally filed by investment companies that have over $100 million in their portfolios. The form shows all of their stock positions. However, companies such as Daily Journal, an entity that operates a publishing business, files 13F as well due to their sizeable stock portfolio (roughly two-thirds of their assets and valued over $100 million). They tried to argue about this with the SEC.

The core of the argument that VULC is liable to file revolves around the Investment Company Act of 1940 which dictates which entity should be regarded as an investment company. Thus, liable to file 13F if the stock portfolio is over $100 million.

The case of Daily Journal is actually useful as it shows how the company argued that they are not an investment company despite having a large stock portfolio.

The core legal section of the act is the wording regarding exemption from the act which states that the exempt company needs to be 'primarily engaged… in a business… other than investing, reinvesting, owning, holding or trading in securities' (abbreviated for clarity).

Daily Journal was arguing that it passes the 'five-factor' test that is usually used to determine whether a company is exempt or not. I believe that VULC fails at least 2 if not 3 of the factors and certainly fares much worse than Daily Journal which did end up filing the 13F.

Note that the linked article about the five-factor test mentions that factor #4 and #5 are usually the most important ones. I believe VULC fails exactly these two factors.

The following are the individual factors;

1. The Company's Historical Development

I believe it is relatively clear that VULC has been unable to profitably run the manufacturing facility. Not only that, the revenues tied to the facility has been dwindling. While in the 1990's the company generated roughly $10 million from it, in 2016 they registered a mere $4 million revenue stream. The nature of the company has been tied to its stock portfolio over the past three decades. Without it they would not be in business as the income has always offset the losses.

In fact, one might be even able to argue that the insiders kept on running the facility in order to prevent the entity to be regarded as an investment company.

Thus, it would be dubious to say that the company passes this factor easily.

Sure, they are likely trying to be *engaged* in the manufacturing business, however they *primarily* make money from the securities portfolio. While this is a grey area, I believe VULC could potentially fail this factor.

2. The Way the Company Presents Itself to the Public

Well if we accept that the website of VULC is the way they present themselves to the public and we totally write off the fact that the company is anything but transparent, then one could make the argument that they are not portraying themselves as an investment company.

However, describing Vulcan Coporation as 'a rubber and foam manufacturing facility housing 272,000 square feet of manufacturing space with a total mixing capacity exceeding 50,000,000 pounds annually.' is dubious to say the least. Where is the part about the $160 million stock portfolio??

3. The Activities of the Company's Officers and Directors

Not much can be said here as we do not much about the roles etc. It is likely that VULC insiders could paint themselves as managers who accidentally bought some stocks and did not do any research etc.

4. The Nature of the Company's Present Assets

It should be clear that VULC will have a hard time defending itself on this factor as the portfolio represented 94.2% of the total assets (including the current stocks) in 2016. One argument that Daily Journal noted was the outsized value of the portfolio was due to appreciation. VULC could again try to paint themselves as lucky investors, however given the size of the portfolio I believe it is hard for them to do so.

I believe VULC should fail this factor.

5. The Source of Company's Present Income

The last factor is also the clearest. I believe that in any way you try to 'skin the cat' the result is the same.

VULC's profitability is solely based on the portfolio income. If they were to stop trying to be engaged in the manufacturing business their income statement would be better off. Their gross profit is abysmal when one compares it with the operating and general and administrative expenses ($0.7 million versus $3 million).

I have not been able to think of any argument that VULC could use here. Yes, they do from time to time sell real estate assets, but that is nowhere near the amount of dividends collected from the portfolio over the years. I also do not need to even use the 'comprehensive income' to prove my point here. Plainly put they generate a material amount of dividends and are profitable because of them.

Thus, VULC should easily fail this factor and more likely than not become liable to file a 13F if the entity is ever contested on this topic.

If you believe like I do that VULC should not be exempt from filing a 13F then you can alert the SEC and fill out a complaint.

Managerial Incentives

After all of this, one is likely to ask why on earth is the management so secretive about the company? They could increase their own wealth just by becoming more transparent and avoid potential problems.

I believe that it could be because of estate taxes. They want to keep the share price as low as possible in order to avoid increasing their tax burden. They could also prefer to sustain the status-quo, or in other words 'leave us alone' preference. This, in my experience, can be an underappreciated incentive of the management teams in the OTC world.

The insiders are likely paying themselves comfortable compensation and do not need to put much effort into the company, i.e. they value the long-term cash flow they can receive. While they are not burning value of the company, they are certainly not creating much. It is a 'symbiotic' relationship of sorts between the management team and the stock portfolio.

Other than that, I have not been able to find another reason. One might think about fraud here as the previous two reasons might seem weak at first. I believe that the possibility is low given the audited results from 2016. Their mid-sized local auditor is based in Ohio and does not seem to show any clear red flags.

How to request financials

If you are further interested in VULC and are willing to buy one share or already own some and would like to see the current financials in order to be more comfortable with the investment I am sharing a straightforward way to request the needed information. A simple email or a call is unlikely to suffice here, a letter is needed.

First, you need to use the following address; Thomas Gettler Law Office 950 3rd Ave, Floor 31, New York, NY 10022-2705

Secondly, in the letter, you need to state that you request the financials under the Section 220 of the Delaware Corp. law. Connected to this you need to state the purpose for the demand. One can read more about the purposes here. However, a simple purpose of 'performing a valuation of one's investment' is sufficient.

Thirdly, you need to show them proof of ownership. A broker statement (blacked out apart from VULC position) should be enough.

Finally, be aware that not all brokers allow the purchase of VULC shares.

Conclusion

The secrecy of Vulcan's management has unsurprisingly backfired and for a good reason. Even after the recent developments the shares continue to be undervalued. While the insiders might try to continue to hide and not utilize the value of the company, I believe that the situation is unsustainable.

The company is likely liable to file 13F form which could provide a clear catalyst as it would show their stock portfolio. This would certainly realize part of the significant upside potential.

Please note that I will post this article on Seeking Alpha roughly two weeks from now.

Financial Disclosure: I own shares in VULC at the publication date.

How to argue about OTC at parties

Tired of listening to your brother-in-law from a bulge bracket investment bank rant about how OTC is ridiculous or how anyone who holds 'penny stocks' is not a serious investor?

Well then, I present you with a set of arguments you can use to show that OTC market is an investable market.

- Argument #1 – Ignore him or support his view that OTC is uninvestable

The number one thing OTC investors do is that they do not talk about OTC.

This sort of Fight Club mentality (the first rule of fight club is that you do not talk about it) preserves the investment opportunities in the market. It as simple as that. The less people will understand the market, the more opportunities for the existing community.

Let him throw whatever arguments at you. Be patient and ignore him or even pat him on the back and tell him that you will transfer all of your VULC stock into his new inverse VIX ETN that will certainly not blow up this time.

- Argument #2 – Reputation of the OTC market is irrelevant

If you had enough and/or need someone to partner with to dislodge a low-balling management at an OTC company, then you can start with reputation.

In your OTC discussion with him, he will surely mention Wolf of Wall Street at least once. Either he will accuse you of being another Jordan Belfort (without a biopic directed by Scorsese) or he will say that you will probably run afoul to such stock pusher.

It is a fair, yet naïve, view. Pump and dumps are still present in the OTC market. However, the nature of these frauds is simple and even basic due diligence will uncover most of these fraudulent stocks.

One can look at recent cryptocurrency pump and dump schemes which were uncovered just by looking at the balance sheet of the company and comparing it to market capitalization.

One example for all can be Crypto Company (CRCW) which was at one point valued at $1 billion while having a tangible book of just $3.5 million. Makes sense. Is it the next elaborate scheme to concoct an Enron-like fraud? Hardly.

Most importantly, generalizing the pump and dump bias to every stock in the OTC is simply wrong and can be easily exposed as flawed logic. Sure, most OTC stocks might be crapshoots, but a meaningful amount of them are not.

While this reasoning is easy to follow, I would like to stress that due diligence in the OTC world is really everything and one needs to perform it carefully and patiently.

- Argument #3 – Obscurity is irrelevant as well

Your brother-in-law might become a bit more intrigued now. He might even pull up OTCmarkets.com (i.e. homepage of every OTC investor) and start searching for a stock. But all he sees, are these obscure companies that do not make much sense.

Who on earth would want to own a share of company solely producing candied fruit (PARF), or a unit of a trust tied to bunch of songs from the 1930's and 1940's (MMTRS)?

He usually does not answer himself and thus he returns to tweet about the latest earnings of $SNAP, a camera company.

However, it turns out that patient enterprising investors who perform detailed due diligence would want to own shares of these companies. It might take a special type of research to be able to get to the bottom of the stock's value, but obscurity on its own is not a challenge or an obstacle.

- Argument #4 – Data can be found and are reliable

Now your brother-in-law might actually try to get a balance sheet or income statement of some OTC companies. A lot of times this means that he will need to venture out of Edgar and find financial information on corporate websites, stock blogs or even the eccentric Investors Hub.

Sometimes he will not able to find anything (literally anything as was the case with ATCD for example) and will need to buy a share and then get the information.

Because of the way he was able to find the information he will start to doubt the validity and reliability.

However, over 98% of meaningful companies have audited results. Thus, there is similar accountability as for companies that are listed and are regulated by the SEC. Do not forget that a good portion of meaningful OTC stocks still file with the SEC (about 50% in this manual).

Couple that with proper due diligence and you can vastly minimize the risk of being exposed to a fraud that would obfuscate their results, like say a large pharmaceutical company that had some unfortunate ties to one pharmacy.

Lastly, one should also think about two things.

Why do some OTC companies want to remain hidden? Most likely because there is some value, not because they are a fraud.

Would an elaborate fraud make sense in the OTC land? Not really. For that you need visibility in order to push the shares up and meaningful volume to be able to sell these shares. The listed market is much more suitable for that.

- Argument #5 – Corporate Governance is not insurmountable issue

The first moment where you will not be able to brush your brother-in-law with a concrete answer is the question of corporate governance. He might accept the financials at face value.

However, he might say that the companies are controlled by single shareholders and sometimes misuse this control to benefit themselves.

This is a fair point, governance in the OTC space can be abysmal in some cases. Just look at Waxman (WXMN), insiders of which tried to buy out the company at 12% of book value.

The key point here is that you can always sue the insiders. You can appraise your rights or try to nudge the management through a fiduciary duty lawsuit. Now, this might seem daunting or even impossible for some people. However, activism is relatively alive in the OTC land and many times a collective effort can work. In the end, Waxman did not buy out the company.

Lastly, one can again minimize this risk through proper diligence and proper adjustment of liquidity expectations (am I okay with holding this amount in this company for three years if no catalyst materializes?).

This argument also shows why I am not using the words enterprising investor randomly. Investing in OTC can a lot of time can really be an enterprise.

- Argument #6 – Volume & Liquidity is present

Your brother-in-law might now say that even if he were to accept the corporate governance situation, he can barely buy anything! Everything is illiquid and there is not enough volume.

This point holds for people that have more than $10 million in their portfolio. Once you are large you simply can't enter the market because you would move every stock you would want to own or you would have to wait ages to build a meaningful stake.

For people that own less than $10 million I present the following table which looks at the long ideas presented in my newsletter (which you can find in the second PDF of the manual).

Ticker	Initiating Report	Share Performance	Volume Since Report
A17	Oct-17	206.67%	>$50,000
A33	Jul-18	98.36%	>$0.1 million
A15	Mar-18	78.57%	>$1 million
A11	Sep-18	66.39%	>$0
GANS:US	Sep-17	65.63%	>$1 million
A5	Dec-17	53.92%	>$1 million
A36	Nov-17	53.85%	>$1 million
A4	Sep-17	47.28%	>$1 million
A28	Aug-17	34.53%	>$1 million
A42	Sep-17	29.73%	>$0.5 million
A26	May-18	21.70%	>$0.1 million
A48	Dec-17	21.60%	>$0.1 million
A12	Aug-18	20.54%	>$0
SORT:US	Nov-17	20.00%	>$50,000
A32	Apr-18	19.70%	>$0.1 million
A27	Feb-18	17.65%	>$0
CAGU:US	May-18	16.67%	>$0.1 million
VULC:US	Jun-18	14.78%	>$1 million
A35	Sep-17	14.29%	>$0.5 million
A41	Sep-17	13.32%	>$1 million
A50	Nov-17	12.66%	>$0
A18	Aug-18	12.50%	>$0
A39	Aug-17	11.26%	>$1 million
A3	Aug-17	5.26%	>$0.5 million
A19	Apr-18	5.15%	>$0.5 million
A46	Mar-18	4.68%	>$0.5 million
A16	Jul-18	4.23%	>$0.1 million
A30	Oct-18	3.13%	>$0
A24	Jul-18	1.49%	>$0.1 million
A21	Mar-18	1.20%	>$1 million
A44	Oct-18	0.49%	>$1 million
A49	Oct-18	-3.16%	>$50,000
A10	Dec-17	-3.18%	>$0.1 million
A13	Sep-18	-3.33%	>$0.1 million
A31	Sep-18	-4.63%	>$50,000
A9	Mar-18	-4.94%	>$1 million
IBAL:US	May-18	-5.00%	>$0.1 million
A40	Feb-18	-5.21%	>$1 million
A22	Jan-18	-8.10%	>$0.1 million
A43	Apr-18	-11.06%	>$1 million
CZBS:US	May-18	-11.47%	>$0.5 million
A20	Jan-18	-14.00%	>$50,000
A25	Apr-18	-14.43%	>$1 million
A34	Feb-18	-16.67%	>$0.5 million
A7	Sep-18	-16.67%	>$0
A2	Oct-17	-16.67%	>$0.1 million
A45	Aug-18	-20.51%	>$0.1 million
A29	Jan-18	-22.73%	>$0.1 million
A6	Oct-17	-23.08%	>$1 million
A14	Mar-18	-23.34%	>$0.1 million
A38	Jul-18	-26.67%	>$0.1 million
A23	Aug-17	-34.16%	>$1 million
A47	Sep-17	-36.59%	>$0.1 million
AAIIQ:US	Feb-18	-50.63%	>$0
BDVB:US	Sep-17	-90.67%	>$0.1 million
PRXIQ:US	Dec-17	-97.68%	>$1 million

In this table you can see that while some situations were certainly limited to smaller portfolios of below $1 million due to the volume being just around $0.1 million, six of them had volume bigger than $1 million.

The summary table confirms the idea of investable ideas.

Volume	# of Stocks
>$1 million	18
>$0.5 million	7
>$0.1 million	18
>$50,000	5
>$0	8

- Argument #7 – Academic Papers are Misleading

If for some reason your brother-in-law has a penchant for reading academic papers about the stock market, he could pull one more argument and point to papers such as 'Outcomes of OTC investing' by the SEC or 'Asset Pricing in the Dark'. These point to the absolute underperformance of the stocks in the OTC market and point out that generally you stand to lose money.

These studies are objectively correct. If you look at the whole market, it is no wonder that you would lose money because you are going to include the classic pump and dumps or meaningless stocks which weigh down the fundamentally sound businesses which are in a minority.

However, no one in their right mind would try to invest in the whole OTC market. Just the existence of this manual and its predecessors point to the fact that you need to carefully choose a minority of stocks that you want to look at. I highlight 351 stocks in this manual while the OTC market counts roughly 7,000 or 8,000 US-based stocks.

By doing this selection you are applying your own subjective view about whether the stock is meaningful or meaningless. Academic papers are unable to do that, because they would have to try to define meaningless companies or try to have a system to identify pump and dumps.

Thus, all they can do is be objective in a market where no one is. A classic problem of academia.

If your brother-in-law actually made it all the way here, by now he should be only able to say that his portfolio is either too large or his preference for liquidity does not match the OTC standard. That is it. These arguments are completely acceptable, but these are personal arguments.

I am not saying that anyone who has below $10 million should invest in the market.

There are many unique risks that one has to properly understand, but this is again tied to personal capabilities (**prior experience**, due diligence ability etc.) and circumstances (liquidity, portfolio etc.).

Index of Stocks Highlighted

Here you can find a simple index of all tickers mentioned in the manual.

- CAGU
- CZBS
- IBAL
- VULC