Letter to Shareholders

Q4 2022 Letter to Shareholders - Annual Report

Dear Shareholders

The fourth quarter of 2022 continued upon our prior successes in terms of stabilizing our business and preparing this company for the next steps in this adventure that you've all joined us for. Key to this is that we've continued to have positive operating income, before changes in property valuations and our public securities portfolio. Following a period of heightened legal, tax, and consulting expenditures, we anticipate that our overall spending levels will decline, which should aid in this profitability. Most importantly, we have continued to maintain and grow a very healthy and increasingly liquid capital base from which to reinvest for the future.

Based on current subscriber trends at KEDM, we believe that our company will show positive operating income going forward (excluding one-time expenses).

We now segregate our business lines into three categories (Investment Properties, Subscription Business Products, and Corporate Division, which includes our investment portfolio).

Investment Properties:
It continued to be a difficult year for our Mongolian property operations. During the year we reported $798,826 (2021- $679,091) of leasing revenue and $100,572 (2021 - $190,850) of other revenue (primarily 3rd party), offset by $757,220 (2021- $759,100) of expenses in Mongolia. Unfortunately, we have zero visibility into the future trajectory of the economic crisis in Mongolia.

Subscription Business Products:
During the year, KEDM, our subscription data business, which tracks various Event-Driven strategies, recognized $3,174,031 of revenue while taking in $3,685,713 of gross subscription receipts, representing a 236% revenue growth when compared to the previous year which began earning revenue in July 2021. As noted in the prior quarter, we have now begun to experience an increase in overall subscriber churn. This level of elevated churn has continued into 2023. We believe this churn is tied to a volatile investing environment where overall research budgets have been reduced amongst our subscribers. Additionally, we have seen a decline in new subscribers—somewhat offset by the increase in pricing that we initiated during the prior year. However, we believe that we erred in raising subscription pricing to a level that turned out to be unaffordable to some subscribers. Our goal is to continue to offer the maximum value to subscribers, while regularly reviewing our pricing methodology in order to maximize the revenue of a business that has elevated fixed costs.

Despite these challenges, recognized revenue continued to increase during the year and has continued to increase into the fourth quarter, though the overall subscriber count has stayed relatively constant. As of the date of this letter, we have taken in over $6 million in gross subscription proceeds.

Having spoken with many financial publishing insiders, we believe that KEDM has now reached a more mature state and current revenue levels are unlikely to increase at a rapid pace from here, as new subscribers are likely to be offset by churn from existing subscribers. Despite this fact, we intend to continue to focus on new marketing approaches to grow the subscriber count.

Given the success to date of KEDM, we believe that there are ancillary services that we can launch and monetize, providing further value to KEDM subscribers. These services will likely be a cost center as they are conceived and grown before eventual monetization. To learn more about KEDM, go to www.KEDM.COM. Additionally, the company is considering acquiring other subscription products that would be complementary to KEDM.

Corporate Division:
Our public securities portfolio produced a $1,031,997 unrealized gain and a $8,792,881 realized gain during the year. I would like to caution you strongly that returns, as we have recently experienced, are highly unlikely to be repeated in future quarters and are likely to be rather volatile given our elevated exposure to oil futures call spreads, which have appreciated substantially since we acquired them. Our portfolio is currently concentrated in investments in oil futures and futures options (including fully offsetting futures call option spreads), an oil ETF, energy services companies, uranium, and the housing sector. We view these investments as highly liquid, inflation-protected, alternatives to holding cash and we intend to liquidate various investments should we find additional businesses to launch or in which to acquire stakes.

Business Update

For multiple years, I have mentioned that there are tax and regulatory reasons why our public securities portfolio cannot continue to increase. As a public company, we are required to have a substantial portion of our assets invested in operating businesses that we hold in excess of 25% over which we exert some degree of control. Unfortunately, we have been unable to find any such operating business that interests us, and this causes something of a dilemma as we cannot continue on the current path. As a result, we have invested substantial time and expense looking for viable structures (hence the elevated spend on legal) and continue to explore various options. However, we have struggled to find an alternative and we are now of the view that we may not find an acceptable path forward.

When Gen and I originally decided to diversify this business, we envisioned a company that would allow us to pivot between public and private investments, bridging the frequent gaps in valuation between them. We saw an enterprise that could incubate businesses and grow them so that they could one day be set free on public markets. We saw a world full of opportunity, but at the time, we lacked the capital to implement these dreams. Fast forward to today, and we are flush with capital and the opportunity set appears to have disappeared.

Unfortunately, the world has arrived in a place that we did not expect. With Private Equity aggressively bidding for private operating businesses, we simply cannot find anything in the private space that is attractive for our investment capital. Why would an intelligent owner ever sell 25% or more of a company to you for less than it was worth? Meanwhile, that scenario happens daily on the global stock exchanges, with the caveat that it is difficult to purchase 25% or more of a business. However, we frequently purchase a few percent for a stunningly good price.

Now, as the world looks to enter a recession, the gap between public and private valuations has become even more extreme as global equities have sold off dramatically, while Private Equity funds continue to raise record amounts of new capital to deploy. We do not know when or if this gap will swing back in the other direction, but we refuse to purchase a private business at a premium valuation to a comparable public business—particularly as a public markets business affords us instant liquidity, allowing us the optionality to redeploy capital into any future opportunity that presents itself.

We had hoped that this gap in valuation would swing back in the other direction eventually. Instead, it has become even more extreme. Unfortunately, we have something of a ticking clock on our business as we have to eventually own more private business assets or large stakes (25% or more) in public companies. Unfortunately, during 2023, hard decisions must be made. I refuse to make a bad investment decision simply to check a regulatory or tax box. As a result, if we cannot find anything intelligent to do, we'll be forced by legal and tax statutes to begin returning capital to shareholders.

Unfortunately, we are subscale as a public company. Gen and I fought hard to get to this point where we have the heft to execute on our business plan. If we are forced to return capital, we'll never be in a position to execute on this business plan, should an opportunity eventually come up. At the same time, it seems silly to burden our current equity holdings with the operating costs of a public company, spread amongst a much smaller capital base, as shareholders would be far better off investing in similar securities in their own personal accounts. As a result, if we start the process of returning capital, we'll likely end up returning a majority of the excess capital at the same time. I want to make it clear that we are not going to be forced sellers of any securities. If we do take the route of returning capital to shareholders, we'll only do so after individual investments have matured.

As we get closer to the moment where we have to deal with this issue, I wanted to more fully detail our current dilemma and thinking so that I can have more fulsome conversations with shareholders and seek out a possible solution to our conundrum. Our path here is not set in stone and we are hopeful that we can either find a solution or find an investment that interests us. However, it would be unfair to you if we sprung a large capital return on you, when you expected us to be growing this business instead. It would be even worse if we made a bad investment out of necessity to extend our timeline.

We had a dream of building a unique sort of business, but it may prove to be impossible due to regulatory limitations.

KEDM Restructuring

For over a decade, this company, my personal life, and my business life have been oddly intertwined. I have always known that related party transactions should be avoided at all costs, but over the years, there have been a variety of related party transactions, which MGG entered into. In all circumstances, I have done my best to ensure that MGG always came out ahead, often at my own expense. I even faithfully served as Chairman and CEO for zero compensation during the majority of MGG's lifetime. I bring this up, as once again we have entered into a related party transaction and this one is large.

As of November 2022, an entity that I control and am president of, has become a Registered Investment Advisor (RIA) in the USA. Unfortunately, this has multiple complications for KEDM, as RIAs are highly regulated entities and all of my finance facing business interactions must be contained within the RIA and the RIA's compliance process. As a business, MGG came to something of a fork in the road where we had three very unpleasant choices in front of us, characterized in terms of the worst option first; we could disband KEDM and return everyone's subscriptions (which would lead to a multi-million dollar outflow from the company along with forgoing millions in future revenue), we could let KEDM continue without my involvement (which would likely entail a rapid acceleration in subscriber churn and a dramatic decline in revenue), or we could have my RIA produce KEDM for MGG to distribute. After spending far too much capital and an inordinate amount of our time seeking out a fourth option that did not involve a very substantial related party transaction, we have decided that the least bad option is for my RIA to produce KEDM.

As a reminder, MGG previously had engaged an arms-length third party to produce KEDM. That party had its expenses reimbursed along with earning a 20% revenue share on all quarterly revenue in excess of USD $125,000 each quarter. My RIA has now employed many of these same individuals and will shoulder the costs of producing KEDM along with passing through the revenue share to these employees. Unfortunately, due to the costs of coexisting within a highly regulated RIA, the costs of producing KEDM will increase somewhat. This is caused by added expenses for compliance, legal and IT—costs that I've mostly shouldered over the past few years, often not realizing that I was paying these expenses. In the agreement that was approved by the Board of MGG, my RIA will receive USD $50,000 a month along with 20% of all revenue in excess of USD $125,000 each quarter. The contract was structured to ensure that my RIA earns a very modest profit, as the overall costs of producing KEDM within this new regulatory environment are unclear. Over time, my plan is to adjust this contract so that my RIA earns a negligible profit on this contract, and nothing more, as necessitated by tax statutes. Offsetting these expenses, my RIA entered into a rental agreement at a rate of USD $5,000 a month as of January 1, 2023 for use of part of the Puerto Rican office building owned by MGG. MGG believes that this is a market rate of revenue.

I want to assure you that we've tried to make this square peg fit into a round hole for the better part of a year now, and we've hit a level of exhaustion with the topic that only those of us who have been working on this, can truly appreciate. Unfortunately, this is the only path forward that can preserve the value of KEDM for shareholders.

Once again, I wanted to be as forward as possible with you as related party transactions, particularly large ones, should be avoided. Unfortunately, some simply cannot be avoided.

Conclusion

In summary, the fiscal year 2022 continued upon the past few years of progress. We have now incubated and launched KEDM with great success. KEDM has passed through the first renewal period and has proven that subscribers find dramatic value in it. Our public equity investments have succeeded beyond our wildest ambitions, and we are in the best financial position we have been in since we started this adventure. Gen and I very much want to continue this adventure. We have big plans and even bigger ambitions for this company, as noted by our continued and aggressive insider purchases over the years. Unfortunately, various regulatory and tax authorities have put a roadblock in our way and despite speaking with multiple consultants and spending a veritable treasure chest of money on this problem, we cannot find a way forward. We haven't given up hope yet, but are also realists, hence we are making you aware of the likely return of a substantial portion of this company's capital.

During the quarter, the company repurchased 302,600 shares under its Normal Course Issuer Bid. At quarter end, our share count was 27,710,499 or 23% fewer than during our peak share-count in 2016. To date, the company has repurchased a total of 8,224,800 shares.

Sincerely,

Harris Kupperman
CEO