WSG

INVESTMENT RESEARCH

FG Group Holdings (FGH)

Multiple Ways to Win

FG GROUP HOLDINGS INC.

NYSE American: FGH

At the time of this writing, WSG does own FGH shares

Table of Contents

Analysis

I wrote the following in Ballantyne Strong update on May of 2022 on the Strong Global IPO:

"This IPO is going to give BTN an inflow of cash through the sale of ownership. I hope leadership wouldn't go out and sell a portion of the company we own for less than its intrinsic value which ***I would conservatively ballpark at $32 to $45 million.***"

A year later Ballantyne has been renamed to FG Holdings (FGH) and Strong Global Entertainment (SGE) completed the IPO process when 14.3% of SGE was sold to the public at $4 a share giving the entire company a value of ~$27.9M. The valuation was a 9x multiple of the trailing 12-month EBIDTA and given the recent market environment for small-cap companies, I am not surprised the IPO came in below expectations. However, I think the price was close enough to intrinsic value that shareholders didn't get a bad deal.

From a strategic standpoint, getting on the public market now offers the flexibility to respond quickly to a better environment where they could sell more of their stake faster than trying to IPO a larger piece of equity. The price to pay for gaining this flexibility was a smaller IPO that wasn't the highest dollar. Time will tell if it was worth paying.

During the past 12 months, the company continues to act with two goals in mind. 1) Position the enterprise for the future and 2) get some recognition for the value underneath the hood. This can be seen by the increased investment in FGF, the growth plan for SGE, and the partial IPO of the segment.

The current value of the investments, cash, and real estate can be ballparked between ~$80.7M-$90.7M, the book value sits at ~$42.7M and the market cap is $34M. Sum-of-the-parts story has been the stable thesis for the better part of a year and a half now and hasn't worked yet. **So, the question begs, will it ever?**

The Person Who Draws the Line

SOTP has always been an investing topic that lends itself to critics. When you have your feet planted in the idea of buying stocks for less than they are worth SOTP situations are simple to understand. You add up the values of each segment and if the total is worth more than the market cap you might be onto something.

But, having a SOTP value greater than the market cap doesn't always equate to an increase in share price. For a SOTP thesis to work you must 1) be accurate on your forecast of value and 2) need capital allocation help from management to unlock the value.

When you invest in situations like these you need someone on the inside who is willing to go in and do the work to unlock the value. The memory of when Warren Buffett sent in Henry Bottle to draw a line on the warehouse comes to mind. **For a value situation to play out, the vision and desires of the people on the inside must match those on the outside.**

Kyle Cerminara is the man on the inside for FGH and since taking control of the company in 2015 has taken multiple steps to unlock value. He has traded taxi tops for equity, turned a cash shell into one of the largest lumber mills in Canada, purchased 60% of a financial business that has shown the potential to be a serious value creation flywheel, and sold 14.7% of their only operating division to the public so the entire value was no longer hidden.

Actions speak.

On a podcast with Bobby Kraft, Kyle was asked why he goes through the effort. His answer was, "To make the share price go up"

If this answer was given by someone who had a sliver of equity, I would roll my eyes but Fundamental Global, the investment partnership behind the controlling stakes founded by Kyle and industry veteran Joe Moglia, owns a lion's share and their track record is on the line. Their reputation is on the line. If large insider ownership doesn't solve the agency problem, then I struggle to find a better way to align shareholders with management.

Ways to Win

FGH is one of the simpler holding companies to size up because three out of the four major components are public entities. The remaining one is a private investment to which the value can only be derived from an educated guess based on the carrying cost on the balance sheet and any new information we get from the company.

With the company currently trading for ~80% of book value and ~50% of investments and cash the implied expectations of these investments are negative. This is where the market and I differ in opinion.

FGH Investments

~85.7% of Strong Global Entertainment (SGE) valued at ~$20M

In 2022 SGE earned ~$3M in EBITDA. The company is the sole provider of IMAX screens and has exclusive contracts with large movie theater operators. They have grown their technical service offerings over the past 3 years and are capitalizing on the upgrade cycle inside theaters to laser projection systems. In addition, they have launched a content creation division titled Strong Studios where they can earn short- and long-term revenues from production fees and long-term licensing royalties on produced content sold to streaming platforms.

The industry is still recovering from a COVID environment with box office numbers on an upward trend and could retest prior levels within the next two years. Given the upgrade cycle, the growth drivers of curvilinear screens, and content creation, over the next 3-4 years we could see EBITDA grow to ~$4-5M. A 9x multiple on that gives a total market cap of around $36-45M which would translate to ~$30-38M in value for FGH.

~60% of FG Financial (FGF) valued at ~$12.6M

FG Financial was born out of 1347 Property Holdings and was renamed in 2020 to "better reflect the future of the company". Right now, FGF has a book value of $38M and a market cap of $21M.

The company runs on a flywheel of writing loss-capped reinsurance, making investments by sponsoring SPACs and through their merchant banking division, which then leads to more capital under management, leading to more loss-capped reinsurance writing ability.

This flywheel has been spinning for two years and as of the most recent quarter they have written 7 reinsurance contracts, have had 4 successful SPAC combinations, and 2 merchant banking investments.

The game of SPAC investments and merchant banking is about slugging percentage and the people swinging the bat, Larry Swets, Kyle, and Joe have decades of industry experience. This network and know-how has led to deal flow and the more deals they do, the better a chance of hitting a home run. There will be plenty of strikeouts and singles but with enough time the flowers will make up for the weeds.

If this company trades at its current book value FGH's share will be worth ~$22.8M, if the book value of the company grows and gets a 1x BV multiple, it's icing for FGH.

~8.4% of GreenFirst (GFP / ICLTF) valued at ~ $13.7M

GreenFirst is a collection of sawmills with 510M board feet of annual production based in Ontario. Over the past year, the company has been making moves to divest non-core assets and sell some more valuable ones for the right price. During the last quarter of 2022, they did two large transactions selling 2 Quebec Sawmills for CAD 90M and sold 203K acres of forest for $49M.

For those keeping score, the acquisition was done with an all-in price of ~$300M, and in two transactions they got ~$140M back.

After selling off those assets the company is made up of the following:

- 4 Sawmills with 510M board feet of annual capacity with cut rights held on the balance sheet well below replacement cost.
- 4,000 acres of property, with key developable lots in Kenora, Kapuskasing, and Timmins
- An overfunded pension
- ~$82M in deposited duties which are being held until August when the rate is reset and will likely result in a check sent back to the company, I have seen estimates as high as 80%.
- $128M in tax loss carryforwards.

Right now, FGH and Fundamental Global hold ~16.6% of the outstanding shares in GreenFirst and during the 4Q call for FGH of 2022 Kyle said, "We do expect GreenFirst Forest Products to be monetized at some point in 2023. That's our thesis."

Now even if it takes longer than 2023, the signal here is the move to monetization. The continuing operations at GFP produced ~$49M in EBITDA in 2022 with the backdrop of a harsh environment. I won't get into the entire lumber thesis here but it's important to know 2 things in regards to GreenFirst.

1) If the lumber market does trend higher, the cash from operations will drown the $150M of capital left in the investment.
2) Management is looking to monetize. This could mean a sale of the entire company or even a capital return program that would prove lucrative for owners.

In either scenario, GFP should prove to be worth more, if we see a double in the share price FGH's share would be worth ~$30M.

$13M Private Investment in FireFly.

This investment is one where the underlying value is masked by the lack of disclosure due to the private nature of the business. I frame it by thinking about the carrying amount on the books and then using any new information after the investment to give either a plus or minus. In 2021 they added 10,000 new taxi tops in an acquisition and due to the network effects of this business, it's a plus in my mind. Since then, they have touted their data platform and the ability to better target customers making campaigns more effective.

If the result here is to have an exit for this company in the form of an IPO or maybe they get acquired, should this happen I bet the result is a larger number than the $13M. Again, if we see a double, that's $26M.

~$15-24M Real Estate Portfolio

In addition to its business investments, FGH owns 2 commercial properties.

1) Joliette Plant in Québec- 80,000 square foot building with twin 90FT coating towers. FGH leases the building to SGE on a 15-year triple net lease. Rent for the first 5 years is $415,000 and then increases by 1.5% a year for the remainder of the lease. Using a cap rate ranging from 4-8% we can conservatively value the building between **~$5.18M-$10.3M.**
2) Digital Ignition Building in Alpharetta, Georgia- Located 15 minutes from Atlanta, this 43,000 SGFT space on 11 acres of land was purchased by FG in May of 2022 for $8.2M and financed $5M of the purchase price with debt. Today the building is listed for $11M here: https://rb.gy/v8kes
   I estimate the building is worth somewhere in the range of **$10-14M** based on the location, growth in the area, and the listing price above. **Using this range values FGH's equity in the building between $5-9M.**

Digital Ignition

Digital Ignition is a co-working space that is specialized to serve those who are starting new businesses in the technology space. Within the building, they host Venture Summits and offer startup accelerators where 10 companies are selected to go through a 12-week hands-on program with mentors in the start-up space. This type of incubation lends well to the other offerings at Fundamental Global like merchant banking from FGF.

Digital Ignition is a call option for FGH. It could prove to be a spawning ground where FG can cultivate, mentor, and shepherd small startups into much larger enterprises that would be both a win-win for the entrepreneur and FG.

The Overarching Theme

The picture I am trying to make clear here is the simple thought experiment that shows the possible upsides to the current investment portfolio. With the market cap trading where it is, there doesn't need to be any huge steps taken for the overall portfolio value to dwarf the current market cap of the company.

FGH is trading below book value with multiple engines pushing forward they only need 1 to go somewhat okay. When you size up each investment with a potential success rate, I like those odds.

Trust or Sell

In a recent conversation with a fellow investor, we both concluded with FGH.

Either we are going to make money, or we are getting conned.

So far, evidence points to the former instead of the latter.

With a holding company like this, it all comes down to the trust you have in management. With this name, it seems to be a topic that comes up again and again, so I began to think, how does a team build the trust of public opinion in the market?

The answer? Track record and execution.

I think book value per share is the best way to gauge the track record as most of the assets are now public and their growth or decline will be directly translated into the net worth of the company. This is where I want their focus.

I don't want them thinking about how their judgments will be perceived by others. They could spend hours on end crafting articles and doing podcasts about their experience and why you should trust them, or they can spend time working on creating value. I think the right choice is obvious. If one has reservations, the team is on quarterly calls to answer questions and they have an annual meeting every year where you can go and ask more if you like.

FGH isn't for everyone. They do funky things. They started an independent film studio from scratch, put together a lumber mill acquisition in the heat of COVID, and traded operating assets for a slug of equity in a startup but the theme is all the same; **They are out seeking asymmetric risk to reward payoffs and only need a few to go right over a long enough time frame to drive outperformance.**

I believe there has been enough evidence so far to draw your own conclusion. They have massive skin in the game and if you are not willing to trust them with patience, there are plenty of other opportunities to look at.

In Closing

Over the next 12 months, I will be watching how SGE continues to fare in the upgrade cycle for theaters and watch any of the films Strong Studios publishes. It will be interesting to see how these new growth arenas translate into numbers. It's easy to track the theater environment by looking at the box office and releases statistics here: https://www.boxofficemojo.com

FGF just announced the recent combination of their two SPACs so those will be de-SPACing over the next couple of months, and we will see how those fare. Plus, the new merchant banking division will likely continue to make deals. I expect to see maybe a few more reinsurance contracts written showing the growth of the flywheel.

GFP and ICLTF are in a challenging lumber market but should the tied turn the mill will drown in cash and could be lucrative to a potential buyer. I wouldn't be surprised if we see a sale of the company or a capital return program in the next few years but if lumber sucks for the next decade though, it won't be pretty.

I don't think anything big will happen with FireFly anytime soon as they are continuing to chase scale.

All in all, FGH has transformed into an interesting little special situations / SOTP name with capital allocators at the helm. Actions so far point to a positive trend going into the next decade so all one can do is sit back and see how it plays out.

If it isn't obvious by now, I own shares of FGH and plan to hold them for the foreseeable future. I trust that Kyle, Larry, Mike, Joe, and Mark are working in the interest of shareholders. They have large amounts of personal capital at risk, so I am positive as a shareholder we are aligned in our desires.

Overview

The roots of FG Holdings were sown back in 2015 when Kyle Cerminara and Fundamental Global took a large stake in Ballantyne Strong and closely after taking the stake was named Chairman and CEO of the company.

Since taking control, Kyle has orchestrated several capital allocation decisions which have transformed the company from a business with only one operating segment to one that now has an operating segment on top of an investment portfolio which has thus diversified the company as a whole. As of the most recent quarter here are the assets they own, a discussion of each will follow.

1) ~85% of Strong Global Entertainment (SGE)
2) 8.4% ownership of Green First Forrest Products (TSX: GFP, OTCM: ICLTF)
3) ~60% ownership of FG Financial (FGF)
4) $13M private investment in Firefly
5) Real Estate Portfolio
6) Cash

Strong Global Entertainment

SGE is the only operating company underneath the FGH banner. During 2022 FGH disclosed they were going to pursue an IPO for part of SGE. The IPO commenced on May 15th with the final offering being 1M shares priced at $4 each. These 1M shares represented a ~15% stake in SGE which would mean the total value of the business is in the ballpark of ~$25M to $30M depending on the stock price for the day.

SGE operates under two segments.

1) The Screens and Systems Segment
2) Strong Studios

The Screens and Systems

This segment is the largest manufacturer and distributor of premium large-format projection screens in the U.S. They are the sole screen manufacturer/provider of IMAX screens and have exclusive provider agreements with Cinemark, AMC Theaters, and Marcus Theaters. Their customer list also includes most of the names in the movie theater industry such as Regal, Cinemark, and Cineopolis.

In addition to movie screens the company also manufactures their "eclipse" screens which are curved. These curved screens give an immersive experience and are currently being used in theme parks, military simulations, and museums. The introduction of this new type of projection screen has been a smaller growth driver for the company as they have been able to expand its addressable market beyond movie theaters.

SGE also has a technical services segment where they are responsible for the maintenance and servicing of screens and projection equipment for the theaters. Since COVID we have seen much more demand from operators for an outsourced service solution to keep costs low in-house. This type of operation where you sell the big equipment and the service contracts that go with it reminds me of the blade and razor business.

VALUED PARTNER OF WORLDWIDE LEADERS

Circuits	Country / Countries	Screens	Sites	Customer	Exclusive
AMC Entertainment Holdings, Inc. [1]	US	7,712	591	✓	✓ [3]
Regal Cinemas (Cineworld Group PLC) [1]	US	6,474	478	✓	
Cinemark Holdings, Inc. [1]	US	4,392	318	✓	✓ [3]
Cinepolis [2]	US & Mexico	4,271	509	✓	
Cineplex Entertainment LP [1]	Canada	1,641	158	✓	
Marcus Theaters Corp. [1]	US	1,053	84	✓	✓ [4]

[1] *The Cinema Foundation - State of the Cinema Industry*, March 2023.
[2] *Cinepolis*, February 2023.
[3] Customer is exclusive for screen products in the United States.
[4] Customer is exclusive for screen products and technical services in the United States.

7

Source: SGE Spring 2023 Presentation

One of the tailwinds is the current upgrade cycle for theaters as they begin to switch over from xenon projection to laser projection, this upgrade in laser projection would also lead to an increase in demand for upgrading screens as well. We have seen large commitments from AMC to upgrade their 3,500 screens in the US to Barco laser projectors through 2026.

Here is what Chairman Kyle Cerminara said about the laser upgrade cycle on the 3Q2022 earnings call on (date)

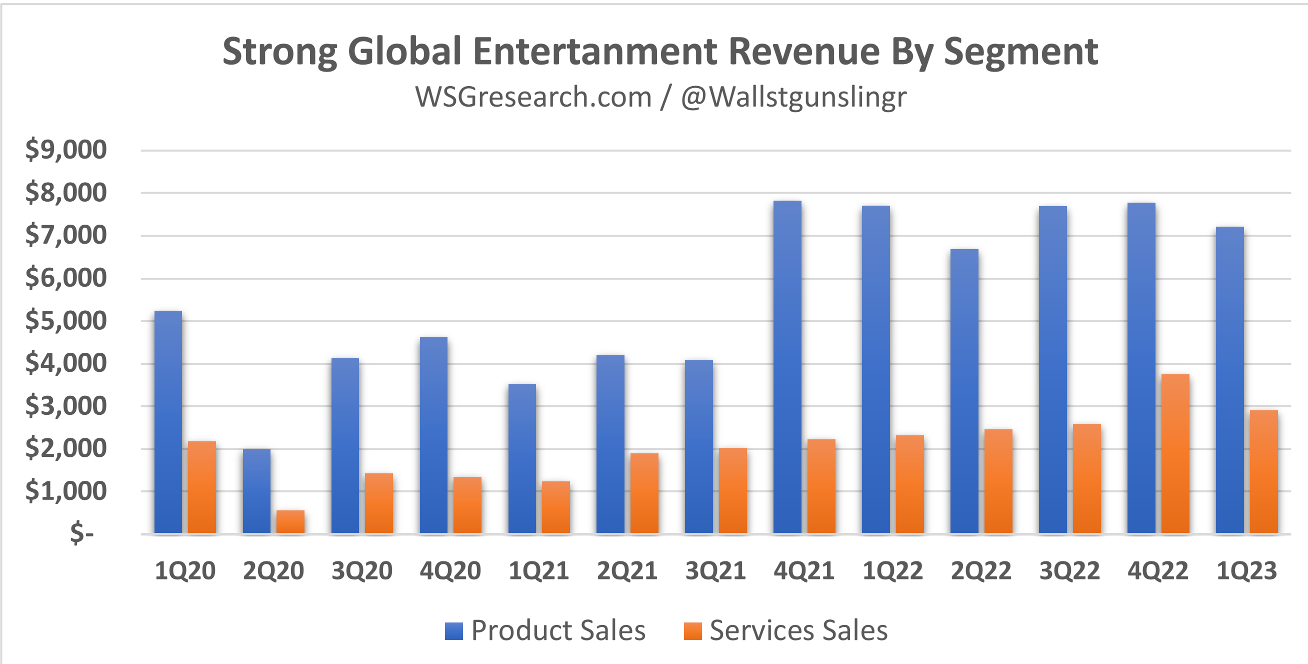
"The laser upgrade cycle is -- it's a really big event for the industry.

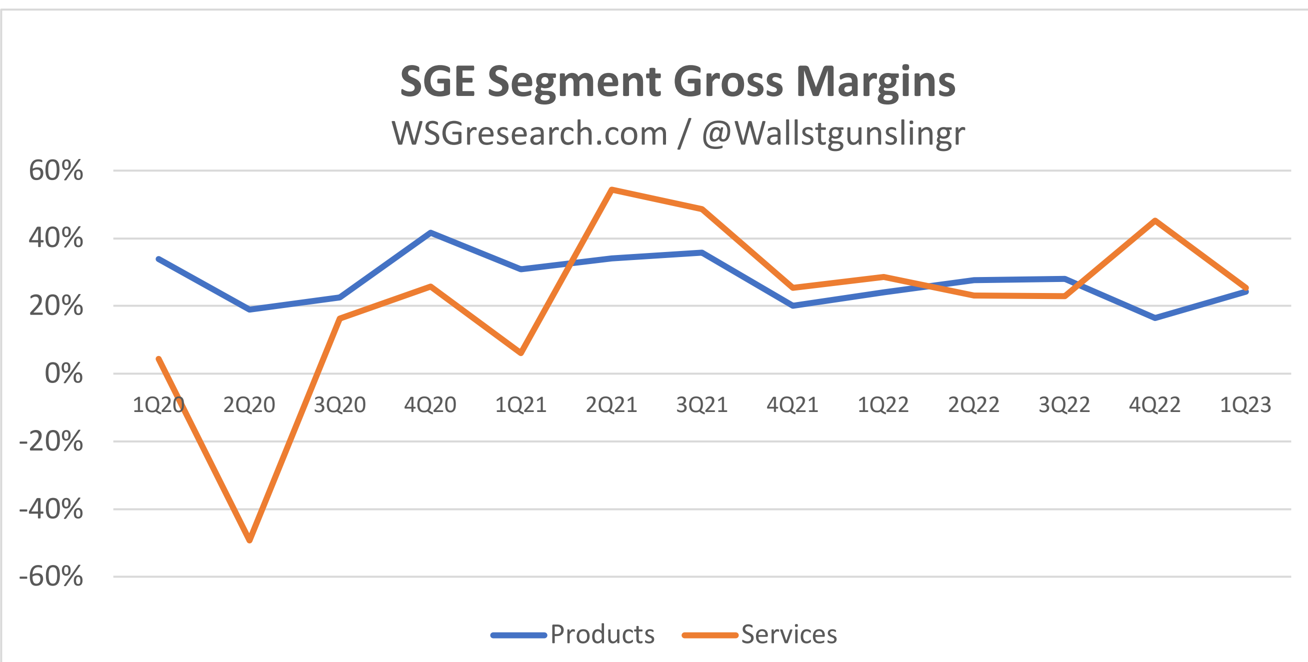
It's probably the biggest technology upgrade and refresh that the industry has had in the past decade or so. The last big technology cycle occurred with the industry upgraded from analog to digital. And the upgrade from Xenon projection to laser projection is an equally large event for the industry.

It's probably going to be spread out over quite a few years, probably the next 5-plus years, really as all the exhibitors begin to upgrade. We're seeing the largest exhibitors like AMC and Cinemark primarily starting the upgrades. Now AMC started theirs and publicly announced their intent to do about half their circuit in the first wave, which will take over the next couple of years.

Out of their 8,000 screens, we've probably worked with them to upgrade a couple of hundred so far by the end of this year. So it's early stage, going with the world series of analogy, I'd say it's the first inning. It's probably really the first few pitches of the first inning. "

During the First Quarter of 2023, the company reported $7.2M in product sales and ~$2M in service sales and we have seen the services side of the company continue to grow since the COVID reopening.



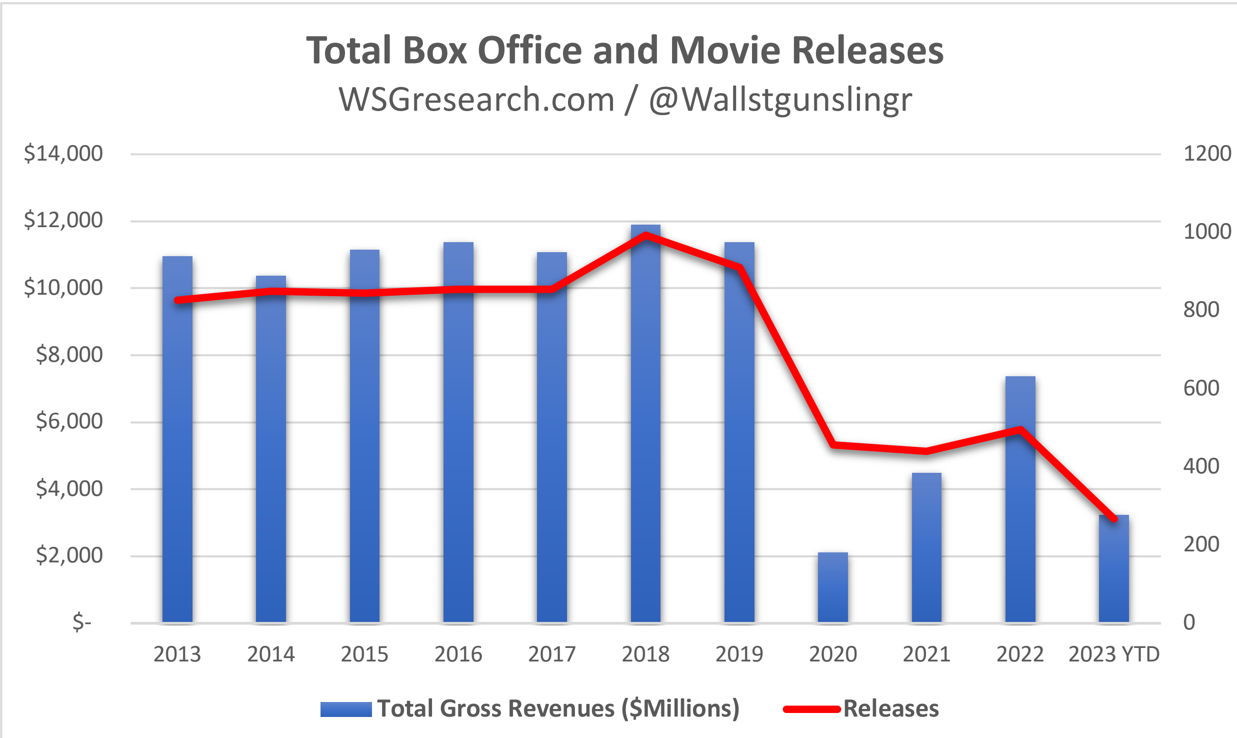


Source: Company Filings

The biggest growth driver for the screen systems segment right now is the upgrading cycle and the diversification into screens made for environments that are not movie theaters like theme parks, military simulators, and museums.

Check out what they did at the Van Gogh, The Immersive Experience traveling exhibit. These are SGE screens: https://vangoghexpo.com

Also at their backs is the pent-up box-office demand that was sidelined during the pandemic. We are still working our way back to the levels reached pre-Covid with box office receipts above $11B and releases above 800.



Source: https://www.boxofficemojo.com/year/

Strong Studios

Strong Studios launched on March 7th, 2022 when David Ozer, formerly the CEO of Landmark Studio Group, was made president of the new division. Strong Studios produces and develops feature films and television series as well as acquires the rights to content for platform distribution.

When they brought on Ozer he came with a portfolio of film assets that were currently in production and right now we are coming to the end of post-production for their first film *Safehaven.*

Strong Studios can make money in multiple ways:

- Production revenues
- Producer fees

- Backend profits
- IP licensing and merchandising

During my study of Netflix, Reed Hastings spoke about how there wasn't going to be enough room for all of the players to have their streaming platform. Thus, he mentioned some of the names are going to turn into arms dealers. Which meant, ditching the streaming platform and beginning to license their content to others. Strong Studios isn't even attempting to get into the streaming game and is going straight for the "arms dealer" mode.

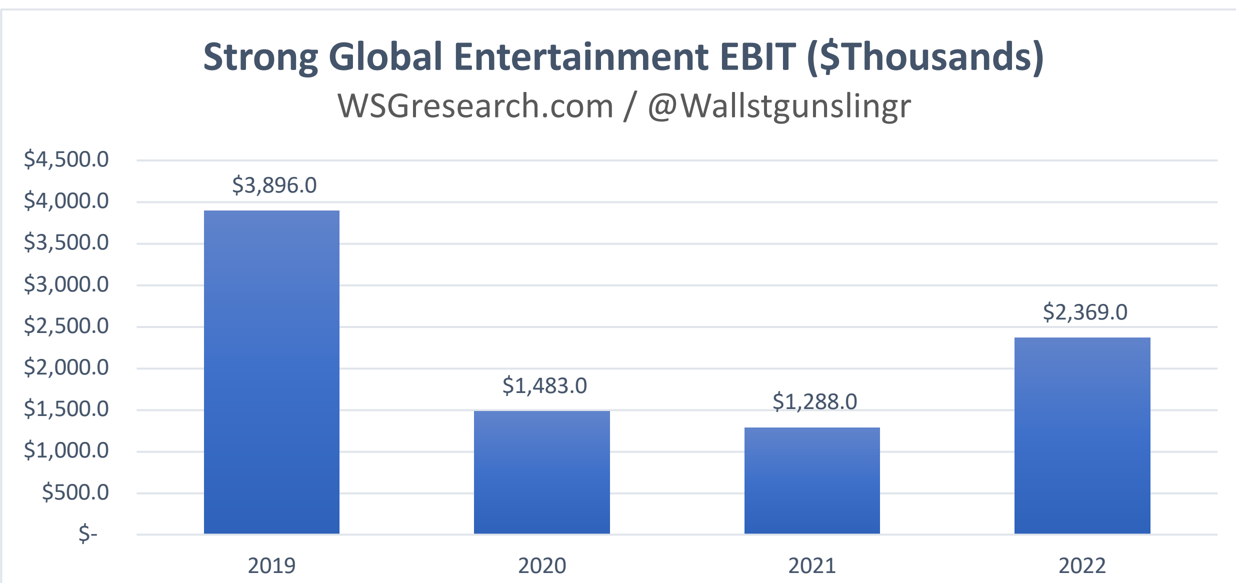
I find the business model of investing in content fascinating. On one hand, you can invest in a forest of content, own part of the trees, and thus the fruit they bare. Plus, Strong Studios gets paid to do the labor of planting trees in the ground.

This revenue upfront brings down the risk of losing money on a project as the risk shifts from the production company to the streamer who made the commitment. The ability to take risk off the table and still participate in the back end is a situation I find attractive.

It is still early days for this company so there isn't any material revenue yet but as the projects continue to move from postproduction and onto the platforms, we will be able to see how they fare.

SGE Financials and Moat

With the separation of SGE from FGH complete, we can get a better look into the specific financial results of the company over the last few years. In their S/1 the company listed their EBITDA numbers for the last 4 years which we can see an average earning power of ~$3m a year. It's hard to compare the results of the recent past to the earning power today due to the pandemic so we haven't seen what the company can do during a "normal" operating environment. I think $2.5M is a good gauge for where they stand on an average annualized basis going forward.



Source: SGE S-1

They disclose the EBITDA numbers, but I like to be more conservative and look at EBIT. I understand the arguments why not too but right now SGE is predominantly a projection screen manufacturer and I bet the maintenance on the facility is roughly in line with the D&A expense, if anything I don't think the variance is large enough to consider it.

SGE does have a strong competitive position and they seem to be only getting stronger as they sign exclusive contracts with major theater operators.

In the S/1 they list the following companies as their competitors:

- Harkness Screens International
- Severtson Screens
- Galalite

The biggest notable difference for SGE is its exclusive position as the only manufacturer of IMAX screens in the world. If someone wanted to compete with them, they would have to get over the biggest hurdle of building a space large enough to manufacture screens this large. Then when you layer on the already entrenched competitive position and customer relationships, they currently have it makes it hard to justify the investment to go in and try to compete.

GreenFirst Forest Products

The investment began in 2015 when Kyle used some of the Ballantyne Strong's (The name of FGH before the change) to purchase a stake in Itasca Capital, which at the time was nothing but a shell company and a pile of cash. Larry Swets Jr (Also a large shareholder and CEO of FG Financial) approached Paul Rivett, a retired president of Fairfax Financial, and was curious if there were any deals, he was aware of that Itasca could participate in. In 2020 Rick Domain (Board Member at GFP, was the previous CEO) approached Mr. Rivett (Interim- CEO), with who he had done prior business, to discuss the potential opportunities in the forestry space. **There was interest from both parties and Mr. Domain began to search for an opportunity.**

In late August 2020, Mr. Domain presented Mr. Rivett with a potential investment in assets located in Kenora (Kenora Assets) and Mr. Rivett called Mr. Swets Jr to see if the company could be interested. They were, but the price was too large and Itasca didn't have enough funds to cover the purchase. After a few months, Mr. Rivett and Mr. Domain concluded that a public vehicle would be the best method to finance the acquisition of the Kenora Assets, as well as potentially other assets. They both decided to invest in the entity through a private placement, giving them exposure on the platform they desired.

On August 13, 2020, the company was selected as the winning bidder for the Kenora Assets and closed on October 6 of the same year. For the all-in purchase price of $11.5 million. Soon thereafter this minnow of a company went after a whale and began to look further into another acquisition presented by Mr. Domain but this one would require outside financing due to the sheer size of the deal.

Having put alternative financing in place and negotiations taken care of, the company announced on April 12, 2021, the execution of the acquisition of the additional sawmills and newsprint mills for a purchase price of $214 million.

What started as a small shell company with some cash on the balance sheet, named Itasca Capital, transformed into one of the top 10 lumber producers in Canada after the initial deal was closed.

Today FGH owns ~8.4% of GFP

As the company moved into 2022 the focus shifted from getting the operation together to running it efficiently and maximizing the value acquired from the purchase of the assets. The company came into possession of some non-core assets that would bring in value if divested which they proceeded to do near the end of 2022.

The first was the sale of ~203K acres of private land to Perimeter Forest LP for $49.2 Mil in cash on November 9th, 2022. Then on December 21, 2022, GFP announced the sale of their two Quebec Mills to Chanters Chibougamau for $90 Mil in cash also.

When the dust settled the original cost of putting together GFP was ~$300m and in two sales they made ~$140M back. (All of these numbers are in CAD)

As of right now, GFP is made up of:

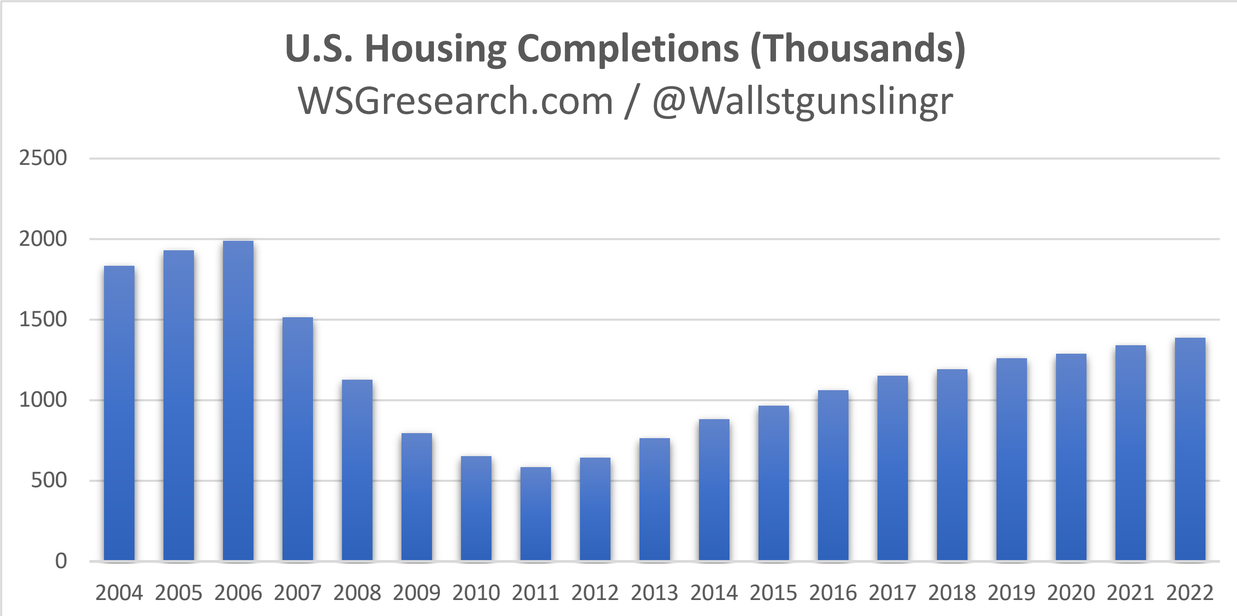
- **4 sawmills with 510M board feet of capacity located within proximity to forests with annual allowable cut rights,**
- **An overfunded pension,**
- **4,000 acres of property,**
- **~$85M of duties on deposit**
- **~$128M of tax loss carryforwards.**

At the heart of it, is the reality that GFP is a commodity-linked product. The ability for them to succeed is directly linked to the price of lumber and the management team at GFP seems to be bullish on this going forward. If they weren't this deal would have never happened in the first place and the price of lumber itself can be correlated to the underlying supply and demand for it.

A Simple Lumber Supply and Demand Outlook

Now, before I get into the nuances of all this, I need to make it clear to you as a reader, I am not a lumber expert. Nor do I hold myself out as one. But I do follow the original thesis laid out by management as to why this could prove to be a real winner of an investment.

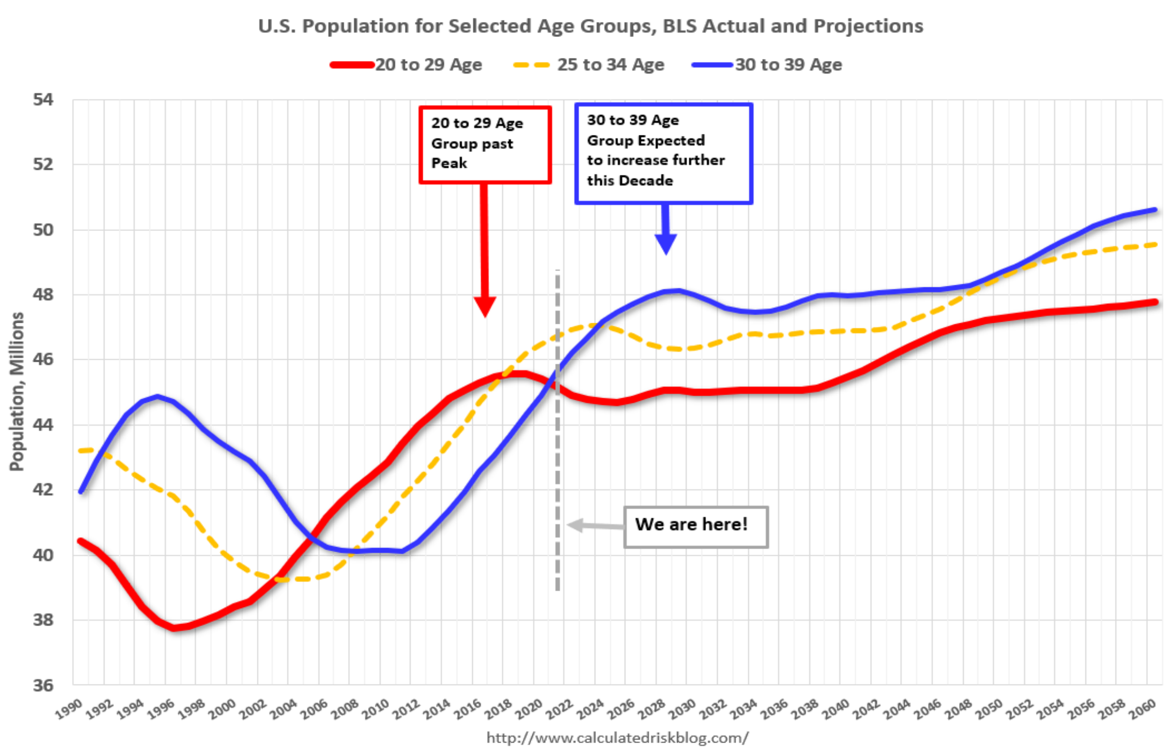
The foundation that the lumber thesis stands on is the underlying lack of supply of houses in the US. This lack of supply came from the underbuilding that has occurred in the industry since the GFC in 2008-2009 and in terms of housing completions we have still not reached the levels seems since before the GFC.



Source: https://fred.stlouisfed.org/series/COMPUTSA

When we compare the recent activity to the long-term trend, there have been a few years that have been below average. This is where the housing bulls jump in and point when defending their thesis and although it's a strong point, in my opinion, it doesn't tell the entire story.

Housing demand is strongly correlated to house creation and population growth. Right now, we have seen a shift in the demographic make-up of the younger adults in our country as you can see by the chart below.

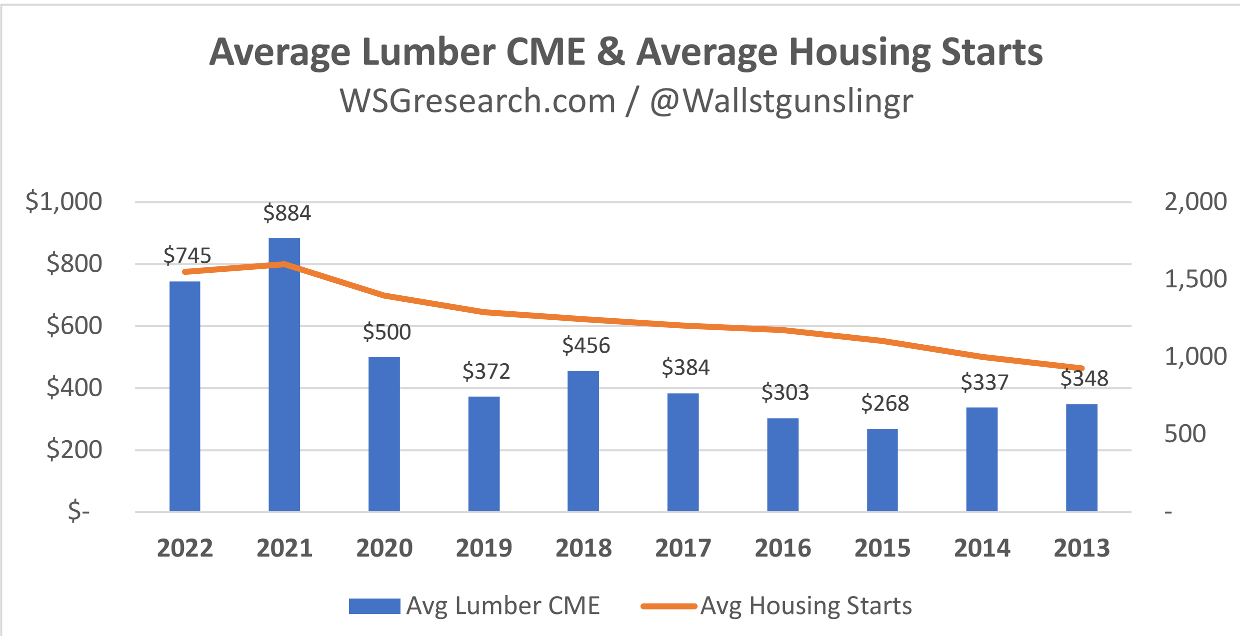


Source: https://twebs.substack.com/p/gfpv-a-rivetting-opportunity

This new switch introduces a larger set of individuals who are now entering the time in their life when family planning and home purchases are more likely. If you believe we have been underbuilding in the recent past, the meeting of these variables points to higher demand for houses with a lack of supply.

When this happens home prices increase and when they get to a point, capitalism begins to work as builders go out and build houses to chase the profits. There is way more incentive to build when prices are high than vice versa.

Based on recent data we have seen that there is a bit of a correlation between the number of housing starts and the average price of lumber.



Source: Yahoo Finance and FRED

The demand for lumber comes down to two variables, the demand for houses and the renovation and remodel space. Right now, housing isn't bad but R&R has cooled down from where it was during the pandemic. I judge the R&R market by looking at the results from big box stores like Home Depot and Lowes. Right now, inventories at these companies are high.

At the time of this writing the trading range for lumber over the past year has been between $700-$345. Right now, we sit at the bottom of that range and at these prices, not many are making money GFP included.

We have a long-term demographic trend that is being fought by the short-term spike in interest rates. By how much? I am not 100% sure, all I know is that there are still more than 15 offers on each starter home I am looking to purchase. This is much less than 2 years ago when there were about 50 offers per house. Although the demand seems a little less, the previous high was such an outlier that the current environment is still above long-term averages.

If demand being higher than average continues, I see no reason why lumber prices won't follow a similar path, and if we see prices above >$450 per thousand board feet, GFP will gush cash.

Should we see an environment where lumber prices stay elevated above the long-term average, GFP will make back multiples of the capital they currently have tied up in the investment accounting for the recent sales for cash which has essentially taken about 50% of the overall price down.

That is the overlay of the outlook for the sawmill prospects, but this doesn't consider the other idea that could turn the GFP investment into a home run.

Enticing a Buyer

When speaking about the GFP assets during an earnings call (March 7th, 2023), FGH Chairman, Kyle Cerminara had this to say:

"*We obviously have a very significant stake in GreenFirst Forest Products. They reported today as well.*

It looks like the stock didn't react that well to it. But we do expect GreenFirst Forest Products to be monetized at some point in 2023. That's our thesis.

That's not me speaking with any information relative to that. But I do think that now that they've sold their Quebec mills, they should be in a position to be a very attractive Ontario Mills sale. And we would think that that's something that could be explored in the near term.

As a shareholder of GreenFirst Forest Products, we would expect the Board of GreenFirst to be exploring all options like that. And we would think that there should be some liquidity that GreenFirst in 2023 is our hope and our not just hope, we don't invest on hope. So that's where we think we'll see some significant liquidity at some point."

The reality is if the environment capitulates like the thesis above, bigger companies will be scrambling to add capacity as lumber prices stay elevated, meaning higher profits for those who own the capacity. If I am someone looking to add more to my portfolio, GFP could be a wonderful addition. Plus, the added benefits like the overfunded pension and the tax loss carryforwards are just cherries on top. Those incentives don't come from building a new mill. Plus, the current replacement cost of the GFP capacity is much more than the market value of GFP itself.

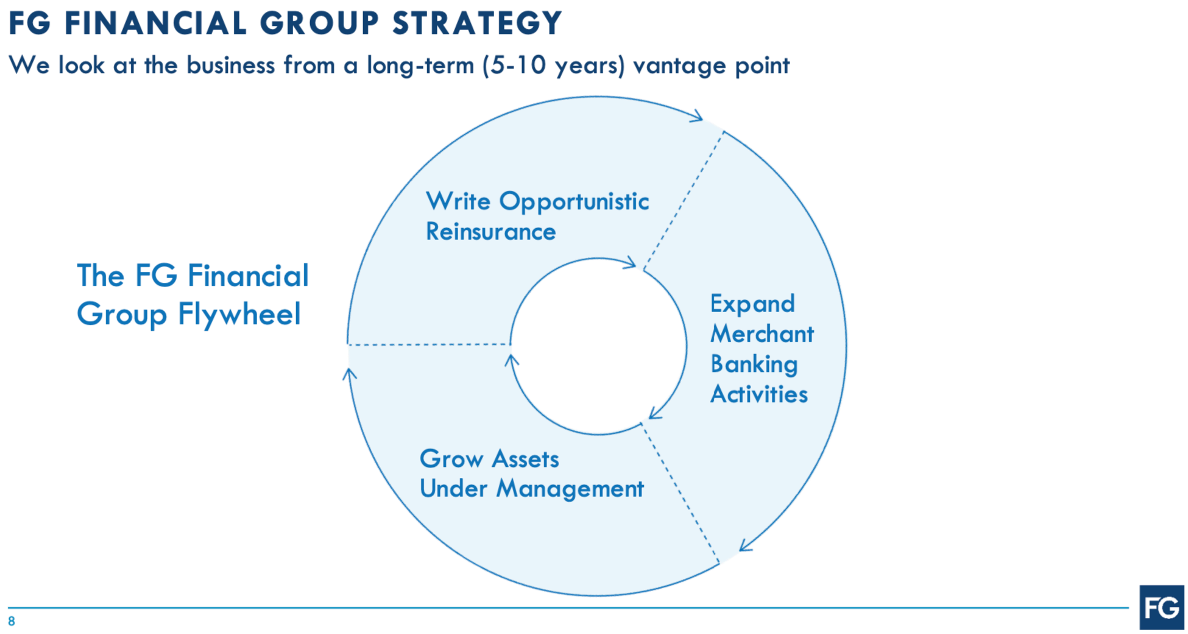
I think there is a large probability that over the next two years, we have an exit event for GFP. If there isn't, I wouldn't be surprised if they begin a capital return program that will show the initial purchase price of these assets to be bargains.

FG Financial

FGH owns about 60% of FG Financial and this too is an investment made at the beginning of Kyles's tenure as leader of this company. In the beginning, the name was 1347 Property Insurance Holdings which was a property and casualty insurance provider in Louisiana, Texas, and Florida. Today the company is much different, it changed its name to FG Financial in December 2020 to "better align with a future business plan".

The company's mission statement is: *"**Grow intrinsic value*** per share with a ***long-term focus*** using ***fundamental research***, allocating capital to ***asymmetric risk/reward*** opportunities."

To make this mission statement a reality they focus on the execution of a flywheel they put in all their presentations that revolves around writing loss-capped reinsurance, taking in the premiums, and then making business investments with those premiums either through their SPAC sponsor program or their merchant banking division.



Source: FG Financial January 2023 Presentation

I wouldn't say FGF is an insurance company, but I also wouldn't classify it as an investment company. The word financial describes it best. The strategy they are pursuing is conservative underwriting with loss-capped reinsurance contracts combined with more aggressive style investments like merchant banking deals and sponsoring SPACs.

Loss-Capped Collateralized Reinsurance

Loss-capped reinsurance is a more conservative approach to underwriting. Party B approaches Party A with a simple proposition, we will give you X premium a year for a Y amount of risk based on a certain event. If Party A likes the risk-to-reward ratio the money is deposited into an account and then the premiums are sent to the company for bearing the risk.

In this type of situation, the loss that could show up for the company to bear is known and capped they can only lose the money that was deposited into the account and no more. This type of underwriting is on the more conservative end of the spectrum and thus, the premiums are likely not the biggest, but the risk-to-reward ratio is heavily skewed in favor of reward.

Currently, the company is involved in 7 reinsurance contracts.

Asset Management, Merchant Banking, and SPACs

The team at FGF is led by Larry Swets Jr, who has decades of experience when it comes to doing business deals and FGF has turned this specialist knowledge into a commercial product that can be useful to other entrepreneurs. The investments division of FGF makes investments in two ways, they sponsor SPACs and do a multitude of financial services in their merchant banking division.

All of their SPAC Sponsorships have either combined or are currently in combination with an operating company. Here is a list of the deals with their sponsor shares.

- **FG New America combined with OppFi on 7.20.21**
    - FGF received 861,690 common shared and 358,419 warrants convertible at $11.50 – currently, OppFi is trading at ~$2.50 and the warrants are priced the same.
- **Adel Financial combined with Hagerty on 12.2.2021**
    - FGF received 533,000 shares and 321,000 $15 Warrants – HGTY is currently priced at ~$9.50 and the warrants $2.50 (These shares are no longer earned by FGF)
- **FG Merger Corp which recently combined with iCoreConnect on 1.09.23**
    - FGF before the combination owned 820K shares, 989K $11.50 warrants with a 5-year expiration, and 85K $15 warrants with a 10-year expiration.
    - Once the deal combination was announced there were some new developments regarding the deal terms. Upon closing the deal all common shares of equity in FGMC before the deal will be converted to a preferred equity post close. This preferred share will have a 12% coupon payable in either cash or paid in kind for the first 2 years after the close of the transaction and then cash thereafter. Then there will be a reset on the preferred shares.
    - The initial conversion from common to preferred will occur at a $10 price point and a reset in price will occur 12 months after the close of the transaction, the reset price will either be $10 or 20% above the simple average weighted volume price. The price can be no greater than $10 and no less than $2.
    - Here is an overview of the iCoreConnect combination: Transcript of the business combination
- **FG Acquisitions, which recently combined with ThinkMarkets on 5.22.23**
    - Going into the transaction FGF owns 819K common shares, 1.4M $11.50 Warrants with an expiration of 5 years, 440K $15 warrants with a 10-year expiration, and either 1.6M $11.50 warrants or $2M in cash or a combination of the two.
    - This deal seems simple with no added clauses like the one described above.

In total, FGF invested $2.6M into FG Merger Corp and $3.4M into FG Acquisitions. Upon the closing of these transactions, the new common equity stakes will be worth much more than the invested sum.

On top of the SPAC investments, in September of 2022, FGF announced the expansion of their merchant banking division which was described as a natural extension of their reinsurance and SPAC business. In the simplest view, merchant banking is a financial pattern for companies that are not large enough to use an investment bank to raise money and such. Merchant banking is a niche type of banking that is not available to the public out focuses on providing financing needs to a select group of customers.

Within this division, they have done two deals so far, a $2M investment into FG Communities, which is a portfolio of manufactured housing communities that they are looking to continue expanding.

The second deal was partnering with Gregg Majewski to launch Craveworthy, a restaurant brand platform that is seeking to create new restaurant brands, develop midsize brands, and revitalized established legacy brands. From the wording in the press release, it seems that FGF is currently playing a partnership role and heading up the financing of the operation. This example of partnering with a growing brand is what merchant banking looks like.

Here is a link to the Craveworthy memorandum for external investors. It gives you a much better idea of what the company is trying to do:

The FGF Flywheel

When you are a financial company there isn't much to differentiate you from your competition. The biggest advantage FGF has going for it is the network of the executives and the deal flow they see daily. Kyle and Larry have spent both of their entire careers in the investment arena in a multitude of situations. Larry has started and sold a financial firm and Kyle has been doing deals for quite some time now. Then you bring in a finance industry veteran like Joe Moglia and his legacy of what he did with TD Ameritrade only strengthens the offering they are trying to provide, which is a partnership and the best way to deserve good partners is to embody the characteristics of one yourself. There is little doubt in my mind they are not trying to do that every day.

This flywheel of writing conservative insurance contracts and then combing this with investments that might fall on the more aggressive side but can offer a large upside will continue to turn as the company constantly is evaluating the potential for capital allocation.

In terms of what this means for FGH the 60% ownership puts these two companies' hand in hand with each other. It's not a huge surprise, Kyle and Larry have been doing work together for a long time and this new structure puts them both under one roof. I wouldn't be surprised if, in 5 years, the assets on the FGF balance sheet far outweigh the FGH balance sheet. I also don't see how these two companies become more intertwined as time goes on. This type of business is right down the middle for both Larry and Kyle.

Firefly

On top of all the public market investments of FGH, on the balance sheet lays a private investment in Firefly. Firefly defines itself on its website, fireflyon.com, as an Internet-connected, high-res smart screen on taxis and rideshares in the most impactful markets in the US, including LA, San Fran, Chicago, Miami, and New York. It is a first-of-its-kind street-level media company. Companies can target their audience more effectively and drivers can earn more by employing the screens on top of their cars, around $300-400 more per month.

Before signs on Taxis were static but with the internet connection and the digital make-up of the FireFly signs ads can be focused on given locations and can change if the vehicle moves from one "zone" to another. This can help the effectiveness of an advertising campaign.

For example, if you are Nike you might want to drive traffic to your store, before you would buy space on a static sign, and wherever the car goes, so does the sign but now if you're Nike you can set up a marketing campaign to run only around 2 square miles of your store thus making the campaign more productive if the car moves out of the desired location, it changes to another campaign.

These dynamic campaign types give the creator much more control over the entire campaign. Companies want to make sure each dollar is being spent to achieve maximum value.

This idea of maximizing every dollar is only capable because, on top of being a digital sign company, there is an arm of Firefly called, StreetIQ which is where they take all the data produced from the signs like latitude and longitude and leverage it to make the campaigns even stronger for their clients. This ability to watch the campaign's effectiveness in real-time and tweak them as they go to make them stronger is a huge advantage over older ways of taxi top advertising.

An example of FireFly using a Hologram for the new Ghostbusters Movie:

This idea of maximizing every dollar is only capable because, on top of being a digital sign company, there is an arm of Firefly called, StreetIQ which is where they take all the data produced from the signs like latitude and longitude and leverage it to make the campaigns even stronger for their clients. This ability to watch the campaign's effectiveness in real-time and tweak them as they go to make them stronger is a huge advantage over older ways of taxi top advertising.

The way this investment came about is an interesting case study in capital allocation.

A few years ago, there was another business within FGH called Strong Digital Media (SDM). This arm provided advertising services and experiential marketing services. Some of the business was conducted through advertising on top of Taxicabs in major metropolitan areas and other off-the-beaten-path advertising ideas like using glass trucks at music festivals. But on May 21, 2019, the company entered into a collaboration agreement and a unit purchase agreement with Firefly Systems, where SDM made 300 digital tops on taxi cabs viable to Firefly.

Instead of getting cash for the assets, Kyle elected to receive shares in Firefly instead. Then in August 2020, SDM entered into an asset purchase agreement with Firefly to sell certain assets to them from their strong outdoor unit in addition to the 300 taxi tops they were already operating under the other agreements.

The future of this investment remains uncertain. Kyle still sits on the board of the company, and they have gone on to do additional fundraising rounds. FGH is one of the largest private shareholders along with Google Ventures and NFX. The investment currently sits on the balance sheet with a value of $12.89M and hasn't been updated since making the initial investments a few years ago.

Due to the private nature of the business, there were no financials disclosed but in 2021 the company made a large acquisition of 10,000 taxi tops from Curb Taxi Media and they have been a first mover in the digital taxi top advertising space giving them the first mover advantage.

I wouldn't be surprised if this company goes public at some point, or an event occurs that causes the investment to be marked to a more recent valuation. Which, if I had to make my best guess, would be larger than it is currently sitting on the books.

Real Estate Portfolio

The FGH real estate portfolio is made up of 2 main buildings the Joliette Plant in Quebec used by SGE where they manufacture all the screens and the Digital Ignition building in Alpharetta, Georgia.

Joliette Plant

The manufacturing plant is 80,000 square feet and is home to two twin 90ft screen coating towers. This building is specialized for screen manufacturing and coating. This specificity gives SGE a competitive advantage. If someone wanted to compete, they would need to replicate this plant first.

During the SGE IPO, the transaction left the building in the ownership of FGH which then in turn leased it to SGE on a triple net 15-year lease. The lease terms are $415,000 of rent a year for the first 5 years and then a 1.5% increase every year thereafter. To determine the full value one can use a range of cap rates between 4-8%, given how specialized it is, the tenant quality is high and thus the cap rate might be at the lower end of that range.

Using the above cap rates, the value of this property can be ballparked between $5.18M-$10.3M.

Digital Ignition Building

Photo Source: https://www.loopnet.com/Listing/190-Bluegrass-Valley-Pky-Alpharetta-GA/28137107/

On May 18th, 2022, FGH acquired the land and building where it held the Digital Ignition subsidy. Digital Ignition is a co-working space that is specialized to serve those who are starting new businesses in the technology space. Within the building, they host Venture Summits and offer startup accelerators where 10 companies are selected to go through a 12-week hands-on program with mentors in the start-up space. This type of incubation lends well to the other offerings at Fundamental Global like merchant banking from FGF.

Digital Ignition is a call option for FGH. It could prove to be a spawning ground where FG can cultivate, mentor, and shepherd small startups into much larger enterprises that would be both a win-win for the entrepreneur and FG.

The building itself was bought for $8.2M and financed with $5M of debt. It has 43,000 square feet of working space and sits on 11 acres of land. Based on the most recent listing the company is valued at ~$11M, which can be found here: https://www.loopnet.com/Listing/190-Bluegrass-Valley-Pky-Alpharetta-GA/28137107/

Based on a conservative value range between $10M-$14M, FGH's equity in the building currently sits around $5M-$9M.

Management, Incentives, and Capital Allocation

The outcome of FGH will be closely tied to the capital allocation of management. This is a cliché line thrown around a bunch in investing circles but for this situation, it holds more weight.

FGH, at its most basic level, is a collection of equity holdings in a multitude of different companies. Based on the current market values, the stake in GFP is almost as large as the 85% ownership in SGE. In terms of this company, it has morphed into a grab bag for Kyle Cerminara and the team at fundamental global.

This makes the situation both simple and complex to understand. On the surface, this company doesn't screen well. When you layer this with the size of the company it quickly becomes eliminated from many buyers in the market, thus only the people who want to expel the effort to look under the hood are the ones who can be counted on to give an informed opinion on the value of the company.

Bobby Kraft asked Kyle Cerminara why he goes through all of the trouble of taking an activist role in the microcap space to which he replied, "I do it to make the share price go up"

Fundamental Global is a private investment partnership founded by Kyle Cerminara and Joe Moglia and the name has somewhat spread across multiple different tickers as the investment partnership influences the moves of the companies in which it holds big stakes.

In terms of incentives, there seems to be no need to go into detail on the compensation of each of the respective companies because the result for FGH will be driven by the increase or decrease in the public market value of each of their holdings and each of the companies under the fundamental global banner come with significant skin in the game. There is no better alignment than that.

Chuck Akre has spoken about before if there was only one question you could ask management, what would it be and his answer was: "How do you define success?" Simple on the surface but it will tell you all you need to know about the focus and aim of management.

We already know how Kyle defines success and why does it matter to him? Because he has a huge amount of money at stake along with his shareholders.

Here is the amount of insider ownership for each of the public companies:

- FGH: 32.4% owned by Management and Directors
- FGF: 61.9%
- GFP: 28%
- SGE: 85.7% owned by FGH

The ownership speaks for itself.

Now, the question should be asked, what if the increase in share price doesn't motivate them? What if money isn't the motivation?

I find this to be a valid argument and question. However, the actions taken by the companies so far do not suggest to me that they are complacent with the share price.

For example, GFP selling off assets to raise cash and then promoting their hidden assets on the most recent earnings slide doesn't tell me they don't care about the stock price. And the commentary from Kyle on the FGH earnings call from last year about how he expects a monetization of the company during 2023 wouldn't have been made if he didn't care.

If we walk a bit further into the actions done within FGH with the recent IPO of SGE, there wouldn't have been a reason to go through all the trouble to try and unlock the value if there was no desire to increase the share price.

To me, there doesn't seem to be enough supporting evidence that points to a lack of care.

Now, there could be a question raised about the investments Kyle has made thus far and about their quality. Back when Kyle took control of Ballantyne in 2015 the company looked much different than it does today. On March 3, 2016, the company had ~$20.6M in cash and $5.6M in investments on its balance sheet. Here is the value of their investments, real estate, and cash today:

- SGE: $20.1M
- GFP ICLTF: USD 13.7M
- FGF: $12.6M
- Firefly (At Cost): $13M
- Real Estate Portfolio: ~$15-$24M (Includes $5M of debt)
- Cash: $4.3M plus the additional funds from SGE IPO which will likely be ~$3M if I had to guess

In total: ~$81.7-$90.7M
This range includes the $5M of debt on the Real Estate

The judgment is still out on whether the investments made within FGH are good ones or duds. It helps that this writer has a firm grasp on the complexity of resulting investment decisions on a timeline. To me, we haven't given the moves enough time to mature. Ask me again in 5 years and I think we will have a better answer but for now, I think there is still patience needed.

Headwinds, Tailwinds, and Big Variables

Here is a breakdown for each segment.

Strong Global Entertainment

Headwinds

- Movie theaters are still recovering from COVID
- There has been a large shift to streaming which could hurt future demand.
- Some chains need to begin an upgrade cycle to stay competitive and some might choose not to lay out the capital.
- Strong Studios is a content creation company and there is huge competition in the space.
- The recent IPO came in under expectations which wasn't a great sign.

Tailwinds

- We are in an upgrade cycle of theaters and SGE will be a beneficiary of the upgrades by those who are going to do them.
- Although still under pre-covid numbers, there has been resilience in the box office and the pent-up demand from COVID seems to be working through the system with an upward trend.
- Strong Studios provides a nice compliment to their manufacturing-heavy company and the diversification in revenue will be able to hopefully offset the slowdown in sales after the upgrade cycle slows down.
- The growth in both the technical services and the immersive screens gives the company a differentiated product from its competition and only makes its market position stronger.

Big Variables

- Box office spend and number of releases (link to box-office mojo)
- Growth in service revenue as more and more operators transition away from in-house technical knowledge.
- Revenue from Strong Studios. This could represent a significant upside for the company being able to monetize in the short term from production revenues and the long term from licensing rights.

GreenFirst Forrest Products

Headwinds

- A harsh macro environment with higher interest rates, high home prices, and a cooled R&R market.
- Lumber is a commodity and has been extremely volatile in the recent past.
- For this thesis to play out there has been a large emphasis on the housing deficit, which has been an estimation and could prove to be wrong. The jury is still out.
- We have been in a steep lumber decline since the peak of 1,500 in January 2021.

Tailwinds

- Housing starts have been above the 1.2M number in the past two years and if they stay there it could be bullish for the industry
- We are seeing a bit of a supply squeeze when it comes to cutting rights and the natural wood baskets. This means any company with a large amount of cutting rights and the forests to support those rights could be in a position of strength should we see a surge in demand.
- GFP has sold off some noncore assets and now only owns the lowest-cost operations out of the reaming sawmills. This lean and mean operational structure could throw off a bunch of cash if we see lumber prices trend back up into the $500-600 range.

Big Variables

  - Interest rates, housing starts, and lumber prices. All of these are big-picture macro numbers that could be hard to predict but are of importance to this company.

- Shareholder capital allocation, the company has shown a willingness to make the moves necessary to unlock value from the company. Which could mean a sale and monetization of the assets.

FG Financial

Headwinds

- SPACs have gotten crushed and the demand for them has fallen off a cliff
- Reinsurance could prove to be costly if a few bad events happen in one given year.
- A provider of capital has no differentiation other than the network and relationships of the people running the place.

Tailwinds

- Kyle, Larry, and Joe are industry veterans who have shown the ability to get deals done and work with people to help with their financial needs. Now, if you just look at the SPACs they have done in the last year, the record looks poor, but the fullness of time will show whether they were right or wrong in their investment decision.
- The flywheel of value creation has been spinning for 2 full years now with 7 reinsurance contracts, 4 business combination SPACs, and 2 merchant banking deals.
- This is a slugging percentage game. The companies they are working with all are on the smaller side and have a runway of growth ahead. With a venture capital-like approach they will only need a few big wins to drive shareholder returns in the long run. We will be able to see the investment ability in 5 years after these investments have had time to mature.

Big Variables

- Deal flow.
- The number of reinsurance contracts they can write.
- Success with their 2 newest SPACs

Firefly

The private nature of this company makes it a little harder to come up with a full list of headwinds and tailwinds. This is a small company and is still considered a startup by many so the risks here are those that come with the usual start-up. However, they have been able to do larger deals like the one with Kyle, trading taxi tops for equity, and with Curb Taxi Media. This ability to get deals done shows the team is chasing scale and if they can get there I wouldn't be surprised if this turns into a solid investment.

The biggest variable for this company is the network effect. As they continue to expand into more and more cities they will be able to offer a large and much more valuable product to their customers. Each new network node in the overall system makes the company that much more valuable and right now chasing scale is priority one. We saw this grow with acquisitions last year and I am willing to bet over 2022 the number of nodes increased.

At the time of this writing, WSG does own FGH shares

Please be advised*, Wall St Gunslinger is not an investment adviser and does not give personal investment advice.* ***All content is for educational and entertainment purposes only and should not be interpreted as anything other than such****. Investing entails a lot of risks and should be managed appropriately. Please do your own research and consult with an investment professional before making any investment decisions. Thank you.*