Dear Fellow Shareholders:

Our past fiscal year was rather eventful. Apart from achieving record shareholders' equity, a number of strategic actions were completed:

A. FRMO increased its interest in Horizon Kinetics LLC ("Horizon Kinetics") from 0.86% to 4.95% by dint of an exchange of stock.
B. FRMO exchanged its revenue specific interests in Horizon Kinetics for a 4.199% participation in the gross revenue of Horizon Kinetics.
C. FRMO completed a private placement, raising almost $5 million of additional capital.

In this letter, the first order of business is to discuss the importance of the strategic actions. The next order of business is to take note of various relevant points regarding our investment portfolio. Finally, all of this will be placed within the context of the current investment climate.

Horizon Kinetics Investment

In order to understand the increase in the Horizon Kinetics ownership interest to 4.95%, it is perhaps helpful to recount one of the stories of the wise men of Chelm:

One day a man was walking along the side of the road carrying a very heavy package on his back. He grew more and more fatigued. Fortunately, he encountered a farmer on his way to market with a big, partially empty wagon, who invited him along. However, he kept the package on his back.

The farmer was, of course, astounded. He asked the man why he did not put the heavy package down.

The man replied as follows, "You were nice enough to give me a ride. I don't wish to add any unnecessary burden to the horse."

It should be recalled that your management is not solely the Chairman and President of FRMO, but also the Chairman and President of Horizon Kinetics. In the past several years, our burdens in the money management field have been made much easier by the global implementation of mass indexation. So, why not put the package down?

It is worthy of note in this connection that, according to the World Federation of Exchanges, on May 31, 2013 the market value of all equities on the planet was $58.6 trillion. The value of trading in just exchange traded funds ("ETFs") (a subset of the general trend in indexation) was

$1.082 trillion. This trend, if continued for a year, would become 22.16% of all trading. However, it far understates the phenomenon. First, ETFs obviously trade equities, so that the participation rate is higher than merely the trading volume of the ETF shares themselves. More importantly, most institutional investors index without using ETFs, since the direct approach to indexation is cheaper. There is no reliable statistic as to how much of the global equity market is represented by the index form; yet, it seems safe to assert that it is far more than merely the ETF world.

Horizon Kinetics is part of the seemingly ever diminishing breed of active managers. According to the Investment Company Institute, as of June 30, 2013, the number of equity mutual funds was 4,509. This figure represents a decline of 1.57% from the level of June 2012.

As a firm, Horizon Kinetics has had the same investment team in place essentially since its inception 19 years ago. If one were to take the leap of faith that the firm has demonstrated some investment skill, and if one were to take the much more precarious leap of faith that the firm will demonstrate such skill in the future, it will be a rare asset. It was possible to purchase this asset at a private market value in April 2013.

Insofar as investment results are concerned, these are available to the public at www.horizonkinetics.com and www.kineticsfunds.com. It is perhaps ironic that Horizon Kinetics as an active manager is now in the index business. However, our approach is to apply elements of active management strategies to indexation strategies. This runs counter to the accepted wisdom of modern portfolio theory. In any case, the strategic role of indexation as it pertains to our business initiatives will be more fully elaborated upon in the sections to follow.

Horizon Kinetics Revenue Interest

As noted previously, FRMO exchanged its specific Horizon Kinetics revenue interests for a 4.199% interest in the gross revenue of Horizon Kinetics.

A revenue interest in and of itself has value inasmuch as it is a direct shareholder asset. In ordinary corporations, the shareholders can only own revenue less expenses. The employees, and particularly the management, share in the revenue in the form of salaries and bonuses. In addition, in the FRMO instance, if the various Horizon Kinetics products are successful, it is obvious that more revenue will be generated. FRMO will be paid 4.199% of that entire increased sum rather than the previous arrangement in which FRMO was dependent upon the success of specific products. This is a far superior alignment of interests.

Horizon Kinetics has launched two passive products in the past year. The first is the Virtus Wealth Masters Fund, which endeavors to profit from what is referred to as the owner/operator phenomenon. This fund had $6.8 million of assets under management ("AUM") in late July 2013. The AUM has more or less doubled in the past 90 to 100 days.

In early June 2013, Horizon Kinetics launched the Japan Founders Fund in the nation of Japan in partnership with a Japanese institution. As of late July 2013, this fund had roughly $24.1 million of AUM. This fund is also organized around the owner/operator concept.

The operating leverage aspects of such products are obvious inasmuch as the operating expenses, while not fixed, will exhibit in success mode a far smaller coefficient of expansion than the revenue. Consequently, the FRMO/Horizon Kinetics revenue exchange is a very significant strategic action. Horizon Kinetics is also about to launch a third index in the swap platform arena.

Apart from revenue considerations, the three indexes are marketed in three different areas. These are the U.S. mutual fund marketplace, the Japanese mutual fund marketplace, and the swap/derivatives marketplace. These open new distribution vistas in which we have not hitherto participated.

Among other features of the effort that are worthy of note are that our indexes are not merely offerings of exposure; they are portfolios of shares based upon a common attribute associated with superior return. It should also be noted that the products carry a premium fee for indexation products. Also, noteworthy is that for the Japanese index fund, as well as the soon to be created swap market product, Horizon Kinetics acts as the intellectual capital originator and does not assume the daily orchestration risk.

Limitations of space prevent a full discussion of the owner/operator concept. The modern approach to risk control is to identify the risks of the various investments in a portfolio and diversify as much as possible, as in an index. The larger systemic risks that are not easily controlled by diversification are then "hedged." This involves some form of payment to a third party for risk assumption, as via an option or swap. In the owner/operator approach, the idea is to make investments in which the management has placed a significant amount of its own wealth. In principle, as a matter of personal interest, such individuals are disinclined to accept egregious risk in the first instance.

More colloquially, let us, in the interest of space, express the concept in the following anecdote. A wealthy woman was once shopping at an elegant fur boutique for a mink coat. She was quite properly concerned with risk, given the expense of the coat. Therefore, she inquired what would happen if she were caught in the rain. The owner immediately replied: "Lady, did you ever see a mink with an umbrella?"

FRMO Investment Portfolio

The most obvious feature of our investment portfolio is the cash position, which exceeds $26 million as of May 31, 2013. Years have been required to build the cash balance to this level and not disrupt normal investing activities. For instance, on February 28, 2009, at the end of that auspicious fiscal year, FRMO had roughly $17.7 million of cash on the balance sheet and our investment portfolio totaled roughly $5.3 million.

Our current investment portfolio now exceeds $29 million, the great preponderance of which is in bond securities, as well as $17.8 million of investments in partnerships at fair value, in addition to a $2.3 million short sale portfolio at market (‘cost’ or proceeds of $4.5 million, which is to say that the short-sale portfolio has an unrealized gain of $2.2 million). We would like to be in a position to make an acquisition in the $15 million range without accepting any material degree of financial leverage. Of course, we could simply have continued to accumulate cash. Yet, if such were the case, we would have avoided many smaller, but nevertheless profitable, investment opportunities.

It could be persuasively argued that we could continue with our investment opportunities as deemed appropriate and liquidate investments as needed if and when funds were needed for an acquisition. The disadvantage of this course of action is twofold. It forces management to realize taxable gains and pay taxes which, as long as our investments remain attractive, represent essentially a tax-free loan from the government. In our case, it will be observed that there were just over $10 million of deferred tax liabilities on the balance sheet at May 31, 2013. Moreover, it forces us to choose between two possibly equivalent investments. There is no reason to place the company in this potential situation.

The investment portfolio in securities, which is to say exclusive of the partnerships, contains $17 million of closed-end fixed income funds. Recently, fixed income as an investment has become questionable, given increases in interest rates. We have no views as to the likely direction of monetary policy. Yet, the closed-end fund market is one of the least efficiently priced areas of securities markets. It is frequently possible to purchase funds at not insubstantial discounts to net asset value that are managed by genuinely talented individuals. In other words, we can buy the same bonds that they buy except, in our case, they are cheaper since we take advantage of the discount. Most recently, it has become possible to purchase mortgage funds at discounts to net asset value. These funds hold mortgages of 2005 vintage with high loan to value ratios, since that was accepted practice in 2005. However, the mortgages are current and there is a strong incentive against default because of the self-amortizing nature of a mortgage when existing for 8-9 years. The mortgages trade at discounts to par. The funds yield between 8-9% with yields to maturity of meaningfully higher levels. Our investments are not very substantial. However, that is the general direction of our fixed income investing.

In terms of equities, well managed firms with substantial management ownership are of necessity underweighted in indexes. This is because all indexes are calculated on the market capitalization weighted, float-adjusted system, which means that, for the purposes of determining the position of a company within an index, the important consideration is how many shares are in the hands of the public versus how many shares are in the hands of management. If the management, ceteris paribus, were to increase the number of shares held by purchasing for their own accounts, the float would be reduced and the weighting of the company in the index in question would be reduced as well.

An even greater problem is the manner in which companies are categorized for index purposes. For instance, Nestle is categorized as a Swiss company, British Petroleum as British, Samsung as Korean, and so on, even though the bulk of the business of these firms is done outside of their nations of origin. This is a significant problem, since global equity risk control is based upon calculated correlation coefficients between indexes designed around country codes that are highly misleading in terms of the business risks encountered by the companies.

This is an example of Simpson's Paradox, a phenomenon of statistics that instructs us that data categorization must be used with extreme caution. To illustrate the point simplistically, let us assume the existence of two universities, each with a graduating class of 1,000 students. In the case of University A, 90% or 900 students are gainfully employed 12 months subsequent to graduation. In the case of University B, 80% of the graduating class is gainfully employed subsequent to graduation. One might naturally conclude that University A is preferable to University B in terms of achieving employment.

Yet, let us suppose that the average salary post-graduation at A were $30,000 per annum and let us assume that the post-graduation salary were $60,000 per annum at University B. Clearly, from the point of view of expected annual income, University A = 0.90 x 30,000 or $27,000 per annum. In contrast, at University B, the post-graduation expected annual income would be calculated as 0.80 x 60,000 or $48,000 per year. In the sense of expected annual income, University B would be deemed to be superior. This is an example of a confounding variable.

If the reader is not yet convinced, let us introduce yet another confounding variable. Let us assume that, at A, 1% of the student body is independently wealthy by way of inheritance. In the case of University B, the similar figure is 20%, or 200 students. Ergo, in the case of University A, 10 students had no need to seek employment. Hence, 900 out of a population of 990 (1,000 less 10) achieved employment, or 90.0%. In the case of University B, 200 students had no need to seek employment, which leaves a population desirous of employment of 800, and all 800 achieved employment 12 months subsequent to graduation. Viewed in this light, University B is far superior to University A.

It should be obvious at this point that proper categorization of variables is a critical aspect of any statistical undertaking. Indexation, as it is currently practiced, and risk control in equities, to the degree that it is practiced, is to a very great extent a statistical undertaking. Nevertheless, the object of the exercise is not the maximization of return; it is simply to obtain exposure in the most liquid manner possible. One might legitimately wonder what type of exposure is ultimately achieved.

The answer, by definition, can only be that the exposure will be based upon those firms with the largest market capitalizations with the minimum of insider ownership. In other words, it is a form of capitalism designed to be practiced without the capitalists. There will be statisticians to build the indexes. There will be paid executives to manage the large firms. Yet, there will be no entrepreneurs. That is to say that there will be no, or perhaps very few, who organize and operate a business and assume a large financial risk in the process. This form of investing essentially rejects implicitly the work of three centuries of economists ranging from Richard Cantillon to Adam Smith, Jean Baptiste Say, Joseph Schumpeter, and Peter Drucker. Indeed, acceptance of these indexation principles, already quite widespread, is growing.

At this point, the reader should see the connection between the revenue interest in Horizon Kinetics and the increased equity interest. Horizon Kinetics owns Horizon Research, which is the wellspring of our investment approach. If successfully applied to indexation, the revenues of Horizon Kinetics increase and the revenue interest in the aforementioned will also increase, with no commensurate expense, to the benefit of shareholders. The cash flow is used to fund our investments. Theoretically, the dislocation caused by indexation should create investment opportunities that ordinarily are not created.

Of course, in closing, we invite readers to study our own economic interest in this firm, which is quite substantial. This shareholder letter is more a strategic overview of our business interests than a statistical review of our investments. Yet, it is such thoughts that ultimately animate our investment approach and we hope that you find it illuminating.

As always, we thank our shareholders for their long-term support of our endeavors.

August 8, 2013

Murray Stahl
Chairman and Chief Executive Officer