Blue Tower Asset Management, LLC
311 RANCH ROAD 620 SOUTH
SUITE 111
AUSTIN, TX 78734

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The Blue Tower Global Value strategy composite had a relatively weak Q2 with a loss of -5.89% (-5.63% gross) despite broad market indices having a gain. Sanctions have frozen our Russian investments, leading to high levels of dispersion among accounts in the composite, so please rely on your account statements for your individual investment performance. Our portfolio was affected by declines in small-cap and value stocks and also a decline in the Georgian stock market.

Small-cap and value stocks have had an overall flat performance this year to the end of Q2. However, things have improved in the first two weeks of Q3. Reports from the Federal Reserve this week showed that inflation is slowing which caused an improvement in investor sentiment and a rally in stocks, especially value stocks. As a result, in the first two weeks of Q3, we recouped most of the Q2 loss.

There are huge volumes of investor money flowing into the 7 mega-cap tech stocks which have been driving up the S&P 500 index: Meta Platforms, Amazon, Apple, Tesla, Alphabet, Microsoft and Nvidia ended Q2 with a total combined market cap of $16 trillion and make up over 32% of the index! These 7 stocks ended the quarter with an average trailing P/E of 45.3, compared to 20.7 for the other 493 stocks in the S&P 500. Additionally, these 7 companies are responsible for more growth within the index for the first half of 2024 than the other 493 combined! This type of extreme concentration is highly unusual and is part of the AI euphoria that has gripped tech stocks. While we believe that AI technologies will create large economic value over the next 10 years, emotions may have overtaken fundamentals here and the index may pull back in the future as a result.

We have made several trades this quarter to rebalance the portfolio in response to economic changes and valuation fluctuations. Post-covid changes in healthcare spending affected MASI and RGEN more than we originally forecast, leading us to exit those positions. We rebalanced our Japanese stocks and sold over a third of our Meta shares. We used the capital from these liquidations to invest in four new companies (ACDVF, BELFB, CMT, TFII) which I will discuss in detail in future letters. I believe that our current portfolio contains many great businesses with strong fundamentals trading at bargain prices and is well positioned for success over the long-term.

Russia updates

In Q2, our TCS Group portfolio holding became further sanctioned and was segregated to the OFAC escrow accounts which had been previously set up for our Sberbank shares. In addition to the escalating sanctions regime involving Russia-connected businesses, there were two major corporate changes that contributed to TCS specifically coming under stricter sanctions. Like many foreign-registered companies with a majority of their operations in Russia, the holding company is redomiciling from Cyprus to Russia[1]. The new company name is IPJSC TCS Holding and the name of the consumer brand for the bank is changing from Tinkoff Bank to T-Bank in order to further distance itself from the founder who was pressured to sell his ownership in 2022. The second major change is the company merging with Rosbank through a stock-for-stock transaction. Vladimir Potanin, who purchased Oleg Tinkov's shares in 2022, is also majority owner of Rosbank (through his majority ownership of Interros). This new combined bank will be majority owned by Potanin or institutions controlled by him. As the wealthiest man in Russia, Potanin has been placed under direct sanctions by the EU and USA which also extends to corporations which are majority-owned by him.

Our two Russian holdings continue to achieve success in the current chaotic environment and have gained significant market share within Russia since 2022. However, the risk of expropriation of shares owned by Western investors increases the longer the war drags on. Per our client agreements and policies, we defer to our custodian on the valuation of these shares.

Georgia Capital

By far the biggest impact on the portfolio this quarter has been from one stock, Georgia Capital, CGEO. Georgia Capital, in the Republic of Georgia, is one of our biggest holdings and fell -26% in Q2 despite posting strong numbers at their recent earnings call, corresponding to a -3.7% contribution to the strategy composite. We previously discussed them in our Q1 2021 deep dive into the company and also in the Q4 2021 letter. However, after the end of the quarter, Georgia Capital stock recovered from the crash to a large degree and is now at a higher price than at the start of the year.

The reason why CGEO is falling is due to an overall decline in all Georgian stocks in reaction to the recent protests against a law that was recently passed, "Law on Transparency of Foreign Influence". This would require media groups and NGOs that receive over 20% of their funding from foreign sources to disclose the source of their funding and register with the government. The stated goal of the law is to bring more transparency to the activity of foreign influence operations on Georgian politics. Critics of the law claim that the true reason for the law is to make it easier for the government to use extrajudicial methods of intimidation on opposition figures. They also claim it resembles restrictive Russian legislation used to suppress dissent and could undermine Georgia's democratic reforms and aspirations to join the European Union. The governments of the EU countries and the US have harshly criticized the law. I believe investors were scarred by the recent sanctions against Russia and are now reflexively dumping Georgian stocks due to a recency bias as they fear US/EU sanctions against Georgia. I expect any sanctions will be narrowly targeted against political figures and won't affect Georgia Capital or the broader economy. I will be closely following their national election in October.

Assuming the political situation there remains stable, Georgia Capital is definitely the biggest bargain in our portfolio right now. Our estimate is that the conglomerate is trading at around 3x of the normalized annual operating cash flow of their underlying businesses. Most of this cash flow comes from the company's 19.7% ownership of the Bank of Georgia (LSE:BGEO) which itself has a market cap of $2.6 billion. Georgia Capital has a market cap of $588 million, so their

[1] TCS redomiciled to Russky Island in the Far East of Russia which has preferential tax treatment within Russia

partial ownership of the Bank of Georgia is alone worth almost as much as their own market cap! Georgia Capital is trading at 41% of the company's valuation of their NAV. The management of the company is using the cash flow from their subsidiary businesses to rapidly buyback stock and plans to repurchase around US$110M of stock between this quarter and the end of 2026 which is about 19% of outstanding shares at current prices. In the end, this price decline will have been a great thing for investors as it allows the company to buy back stock at lower prices.

I appreciate the continued support of Blue Tower's investors. Please contact me with any questions you have.

Best regards,

Andrew Oskoui, CFA

Portfolio Manager