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The Blue Tower Global Value strategy composite slightly underperformed the ACWI this quarter, ending a sequential 4-quarter streak of outperformance. Our Q3 net return was 6.02% (6.30% gross) bringing our net return for the first nine months of 2025 to 35.31% (36.39% gross). Please refer to your individual account statements as they will differ slightly from the composite.

The largest contributor to this quarter's performance once again, was our investment in Georgia Capital (London:CGEO). In spite of the gain in the company's share price so far this year, the shares still trade at a significant discount to the company's NAV calculation. As a result of the gain, Georgia Capital is now the largest position in the strategy.

The past few years have seen an evolution towards a global trade system that is less dependent on the US dollar and more decentralized. Sanctions, tariffs, and a large federal deficit have weakened the appeal for the USD as a global reserve asset. USD reserves, as a percentage of total global reserves, are down to the levels where they were in the mid-1990s and gold is increasing as a reserve asset. Despite this, the US stock market remains valued at extremely high multiples.

Dollar deficits likely leading to weakness in the future

In North America and Europe, developed Western countries are facing an addiction to deficit spending as well as an impending pension crisis from an aging population. In the United States, the debt has reached $38 trillion with a projected deficit of $1.78 trillion for 2025. France has experienced political turmoil in passing every annual budget since 2022. President Macron has tried and failed to get a pension reform increasing the retirement age to 64 from 62, which is necessary to keep their retirement system solvent.

There is simply a lack of political will in Western countries to either increase taxes or cut government spending. In the short term, the deficit spending acts as a fiscal stimulus and will reduce the risk of a recession and boost returns for investors in public equities. Over the longer term, this deficit spending will lead to several negative consequences for Western countries. An unsustainable debt may force crudely targeted spending cuts which reduce state capacity. Critical government functions such as maintenance of needed infrastructure may see their investment level cut. The growing debt will lead to a loss of foreign investor confidence. Foreign investors fear that Western governments may voluntarily refuse to pay back loans or monetize the debt through inflation. This loss of confidence will shorten the runway that Western governments have to correct these fiscal problems and increase borrowing costs. Investor confidence has already been dented by the freezing of Russian central bank reserves.

When a government spends more than it collects in taxes, it borrows the difference by selling Treasury securities. These treasuries compete with other forms of debt in the economy, causing the equilibrium interest rates to rise. Higher interest rates make financing more expensive for households and businesses, suppressing consumer spending and business investment. Additionally, beyond just debt markets, the government's increased demand for goods, labor, and materials can reallocate real economic resources away from the private sector. This growth reduction effect at high debt levels is called "crowding out."

While most empirical studies find evidence that high debt reduces real economic growth, the threshold where this occurs varies by study and the countries included within it. The upper limit is generally found to be between 60-100% of GDP, with a mean threshold of 75% of GDP for developed countries[1]. According to the most recent FRED data, the US is currently at 119%. Other developed Western economies aren't much better on that front. According to 2024 IMF data, the UK is at 101%, France is at 113%, and Italy is at 135%. Germany is at a comparatively healthy 64%. Japan has a much higher debt at 237% of GDP, but around 45% of their debt is owned by the BoJ which is majority owned by the government of Japan. Foreign nations and investors own only about 12% of Japan's debt.

The current amount of US deficit spending is raising real interest rates, diverting capital from private investments, and reducing future growth potential.

De-dollarization

One possible strategy that countries may pursue to reduce their dependance on the US dollar by settling trades through their local currencies, with gold serving as the ultimate settling instrument. Russia and China now conduct much of their trade in rubles and yuan, while India and Brazil are building local-currency settlement mechanisms for trade in energy and agricultural products. These arrangements keep much of the settlement within participating central banks and local payment systems.

As countries trade, bilateral trade faces an inherent imbalance as one country almost always imports more than it exports to the other. In the face of this imbalance, the currency of the importer would fall against the currency of the exporter, eroding the stability of the settlement. This problem can be solved by using gold as a neutral settlement medium. Instead of holding large amounts of foreign fiat currency, countries can use gold as their reserve asset. They can periodically settle trade imbalances with gold transfers between their reserve accounts. Additionally, these gold transfers do not need to be physical. They could be digital transfers of tokenized gold reserves on international clearing platforms.

According to J.P. Morgan "the share of gold in FX reserves in [emerging market] is still low at 9%, the figure is more than double the 4% seen a decade ago; the corresponding share for [developed market] countries is much larger at 20%[2]." So far in 2025, the price of gold has already risen by 55%. While the US dollar is still the primary reserve asset globally, recent increases in the price of gold and the rising proportion of gold in reserves indicate that some

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[1] *The impact of public debt on economic growth: What the empirical literature tells us*. Mercatus Center. https://www.mercatus.org/research/policy-briefs/impact-public-debt-economic-growth-what-empirical-literature-tells-us

[2] J.P. Morgan. *De-dollarization: The end of dollar dominance?:* https://www.jpmorgan.com/insights/global-research/currencies/de-dollarization

countries are beginning to look at it as a tool for de-dollarization and trade settlement diversification.

High valuations of US vs international

The US stock market has dramatically outperformed the rest of the world since 2009. While US companies have had slightly faster EPS growth than their international counterparts[3], this outperformance has been primarily due to multiple expansion (stocks becoming more expensive relative to their earnings).

This US outperformance trend is beginning to reverse and now international stocks have outperformed the US market by about 11% so far in 2025. Despite this year's underperformance against international stocks, the US market remains very expensive relative to the rest of the world, nearing the peaks seen during the 1990s dot com bubble.

One argument made is that the US is justified in having a higher valuation than foreign countries due to the composition of the US stock market. Some industry sectors trade at lower multiples than other sectors due to perceptions of a lower projected future growth and higher risk. As countries have different proportions of sectors in their national stock markets, the aggregate appropriate valuation multiples for their markets will differ. One could imagine that a hypothetical country whose stock market consisted solely of coal mines should have its stock market trade at a lower multiple compared to a hypothetical country whose stock market is dominated by technology companies. As the US is home to many huge technology giants, perhaps the US market is justified in trading at a higher multiple. However, as we can see in the chart below, the over-valuation of the US market is observed even when one controls for industry sectors.

Index	Forward PE as of September 30, 2025
MSCI USA	23.25
MSCI ACWI ex USA	14.95
MSCI AC Europe	14.42
MSCI AC Asia Pacific	15.74
Consumer Staples	
MSCI USA Consumer Staples	21.29
MSCI Europe Consumer Staples	15.10
MSCI Emerging Markets Consumer Staples	19.01
Technology	
MSCI USA IMI Information Technology	30.55
MSCI Europe Information Technology	26.95
MSCI Emerging Markets Information Technology	17.57

[3] Exceptional Expectations: US vs. Non-US Equities. AQR Capital Management. May 9 2025 https://www.aqr.com/Insights/Research/White-Papers/Exceptional-Expectations-US-vs-Non-US-Equities

While there are still many great opportunities for individual companies within the US market, at these elevated valuations, it is unlikely that investors in US stock indices will experience future gains similar to what they experienced in 2009-2025. However, the average financial advisor still allocates 77.5% of their equity portfolio to the US! [4]

Volatility Ahead

The political, economic, and technological changes occurring around the world will create heightened volatility in global markets. AI investments, in particular, are having a large impact in capital expenditures and stock valuations. Generally, this is good for active managers as the changes are likely to create dislocations and opportunities that we can act upon. However, this volatility can also mean drawdowns in our performance or underperformance relative to market indices on shorter time periods.

We will not outperform the market during every hour of trading, or every day, week, month, or even year. Our aim is to outperform the market over the long-term[5] by investing in high-quality businesses at bargain valuations.

Thank you for your continued trust in Blue Tower. Please contact me with any questions you have.

Best regards,

Andrew Oskoui, CFA

Portfolio Manager

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[4] BlackRock Investment Institute. 2025 Fall Investment Directions: Rethinking Diversification. August 25, 2025 https://www.blackrock.com/us/financial-professionals/insights/investment-directions-fall-2025

[5] I consider a rolling 7-year time period to be long term