

Private Companies: Primary Capital is Purposeful Capital

Tom Slater, Lawrence Burns & Claire Shaw
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Capital at risk. Past performance is not a guide to future returns.

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Claire Shaw (CS): Good afternoon, and welcome to the session on private companies. My name is Claire Shaw and I'm the portfolio director on Scottish Mortgage.

Private companies is a topic that is always of huge interest to our shareholders, so Tom, Lawrence and I wanted to dedicate some time in our conference to share with you the exciting progress and developments that are being made here.

However, for those that are new to Scottish Mortgage and are less familiar with the makeup of the portfolio, Scottish Mortgage has the ability to invest up to 30 per cent of the Trust into private companies. As of today, we have 40 companies which are still private, which equates to about 23 per cent of the portfolio, with our ten largest private companies accounting for two thirds of our exposure to this asset class.

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Now our rationale for investing in private companies is simple. Companies are staying private for longer. And the implications of that is that more value is being created prior to companies entering the public markets.

But gaining exposure to private companies often involves paying high fees. The difference with Scottish Mortgage is that we want to give our shareholders access to all that value being accrued in the private space, but doing so in a low-cost way.

Also, we can offer shareholders liquid access to private companies which are typically deemed illiquid by a function of us being a daily traded company of the FTSE 100.

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Now our history in this field goes back to 2012, when we invested in our first private company, which was Alibaba. Since then, we have gone on to deploy £4.6bn of capital into this area. And in the 12 years since then, we have supported 46 companies on their journey from private to public. And we still hold 14 of them today, one of which is the money transfer company, Wise, who you'll hear from in the final session.

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Scottish Mortgage is unique. Public and private companies owned together in one fund. And our proposition is straightforward. We own companies uninterrupted in their journey from being private, through an initial public offering and into the public markets, so that shareholders have the opportunity to benefit from long-term compounded returns.

Thank you to everyone who submitted questions, which we've included within our discussion today. Joining me now are our two managers, Tom and Lawrence.

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Afternoon, both. To kick off, before we get into the companies themselves, we had a number of questions come in, asking could we please provide a quick beginner's guide, an overview to the types of private company investing and where Scottish Mortgage typically gets involved?

Lawrence, why don't you kick us off with that?

00:03:00

Lawrence Burns (LB): Sure. In some ways, the term private companies can at first seem really very broad, because that's every company that isn't listed on the stock exchange. That's everything from a start-up founded last week in a garage in Silicon Valley, all the way to a mature company that's been around for 75 years that we've known for generations, like Ikea, for example.

And Scottish Mortgage really sits somewhere in between those two extremes. We're doing in many ways what we do in the public space. We're looking for private growth companies. So not the most mature companies, but those that we think have the potential to, again, be a multiple of their size over our investment horizon. It's very similar to what we're doing in the public space, but in the private space.

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The other element to it is that we're not going for the most earliest companies, that garage in Silicon Valley that was founded last week. Companies such as that may have a bright future, but at that point they

probably aren't even generating revenues, let alone profits. And they're better supported by seed investors and venture capitalists. High reward, high uncertainty there. And that's really where, in some ways, the term venture capital comes from, it's adventure capital.

What is Scottish Mortgage doing? I think what we're doing is deploying the vast majority of our private capital into private growth companies that I would say are really in the scaling phase. What I mean by that is that they've shown some clear signs of traction of their business model, it's working. Our role there is to come in and provide capital that's a catalyst to that growth, to help it continue and accelerate it.

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As an example, in 2015, when we invested in Spotify, they were growing very strongly. That was about accelerating their growth, so they could expand into new markets. That's really one large part of it.

Now, I would say at the same time, we do tend to invest in earlier stage companies, very occasionally, but at much smaller holding sizes. An example there might be Upside Foods in the US. Upside Foods, they cultivate meat from cells. So no animal slaughter, better environmental footprint. Earlier than our average investment, but huge opportunity and an awful lot for us to learn.

But the vast majority of capital is invested in these businesses that have that scaling opportunity.

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CS: Perfect, Lawrence, that's very helpful. I think the natural place to start with giving an optic on our actual private companies is our largest private company, currently just over 4 per cent of Scottish Mortgage, which is SpaceX. A shareholder is saying 'Ask Tom Slater how SpaceX has already changed the world and how he anticipates it will further change the world?'

Tom, could you maybe give us an update on the progress the company's making, both in the launch market, but also on their satellite business, Starlink?

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Tom Slater (TS): Yes, sure. The launch business has already had a massive impact. We in the West had got ourselves in the position of being completely dependent on Russia for access to space, and we've seen the challenges that that presents. You've seen a private company become the gateway to space for the Western world. They've been able to do that at an

enormous scale. They did close to 100 launches last year, and basically have more than doubled the size of the launch market in the space of 18 months. They're going to do a significantly larger share than that this year.

It's already had a really transformational impact. You saw just this week that SpaceX was going to the International Space Station to bring back astronauts that really nobody else could've done.

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And that's before you start to think about the new platform, Starship, which is a huge vessel, the size of a skyscraper, capable of taking 150 tonnes into orbit. Which will enable a whole new set of capabilities that I don't think people have even started to get their heads around. I maybe won't go into that in too much detail right now.

Then, as you say, they also have launched their satellite internet business. I think the last time they updated us, they had more than 3 million subscribers to their internet business. It's in 100 countries. That's really exciting as an investors because telecoms is a huge market. And so, to be a global provider, able to provide service in areas that others can't is also transformational.

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I think you'll see them going from satellite to satellite dish, to satellite to mobile device. And that will eliminate coverage dead spots. A quarter of the US landmass has no cell phone coverage today. Again, a big extension it the size of the market. I think both of those businesses have huge potential and they also fit very well together because it's access to that launch capacity that gives Starlink its huge competitive advantage over everyone else.

CS: Tom, can we stay on SpaceX? Because we did have quite a few questions come in about how do we actually value SpaceX? We're comfortable with your valuation process, but we want to understand what variables are used to value this business? Can you maybe just walk us through, how do we actually go about valuing this company?

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TS: Sure. Three inputs. The first is transactions between third parties. That's really valuable because it gives you a clear view on what two completely independent players are prepared to transact at. The company's been pretty good at providing those regular access to transactions, either by bringing in new capital or allowing insiders to monetise some small part of their position. That's the first one.

The second one is as you're looking at the operational metrics, is the company hitting its targets? Both from a financial standpoint, whether that's revenue generation, profitability. Profitability is an important one here. People think about private companies and think pre-profits. No, this is a really profitable business in the satellite side.

You've got third party transactions, you've got operational metrics, and then the third one is looking at, I hesitate to say the word peers, but similar listed businesses, to see how market perceptions of these type of companies are changing. Those are the three inputs.

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CS: Super, Tom, that's really helpful. Maybe just shifting tact a little bit. We called our session today primary capital's got purposeful capital. I think there are a number of companies within our private companies that are at, I would call, the forefront think of innovation and driving the energy transition. I think it's well known in order to achieve decarbonisation, we need to find some breakthrough innovations and technology that can really reform some carbon-intensive sectors.

But we know that scaling these companies is going to need patient support from investors, like yourselves, because these companies are tackling incredibly complex and difficult problems to which there is no playbook, there's no peer group, there's no comparisons. But if they work, the implications, both financially and for society, are huge.

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Lawrence, on the theme of the energy transition, can you maybe pick out a couple of companies within our private company portfolio that's helpful to use as case studies here, who are really tackling some of these complex problems? And what progress are they making?

LB: Sure. I think I'd start off by saying I think the term purposeful capital is an interesting one. Most of the time when you go and buy shares on the stock market, you're buying those shares off another financial market participant. Off another retail investor, off a financial institution. I think what makes capital purposeful is really when it's primary. When that capital is going directly to the company and the company are using it to do something, to accelerate progress or make the business better.

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And that's the case of our energy transition company. You've asked for two examples. I'll choose, I think firstly, Redwood, because they're visiting actually one week ago today.

Redwood was founded by JB Straubel, who's one of the co-founders of Tesla. Their opportunity set is that most people expect there's going to be soaring demand for batteries because there's going to be a lot of greater need for electric vehicles, for batteries for storage for renewables.

And you can address that need by going out and buying lithium, nickel, cobalt and making a battery. Redwood's approach, though, is that actually, we have a lot of those materials already in our countries, in our economies, you just need to recycle them. From old batteries, from old electronics, and that's how you can get those materials. And there's a few advantages that come from that.

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The first is you get batteries that are potentially cheaper. You get batteries that are more sustainable. And the third is that you get less dependence on global supply chains. You're not needing to get those resources from other countries, you've got them within your own national borders.

Redwood, our capital has gone in and funded construction of a facility in Nevada, a facility in South Carolina. I think I'm right in saying that as of last year, they had a capacity to process about 40,000 tonnes of material. That's enough to build batteries for about 100,000 cars. They've signed deals with major auto makers, like BMW and Toyota. They're supported by the US Government with a loan, Department of Energy, so progress there is going very well.

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You asked for two examples, so I'll give you Climeworks as the other one. We are facing a climate crisis. We need to reduce the amount of carbon dioxide that we're pumping into the atmosphere. But to really tackle climate, I think we need to go further. We need to actually take out the carbon emissions that are already in the atmosphere, and that's where Climeworks comes in.

Its facility is quite literally suck carbon dioxide out of the atmosphere and store it underground in rocks for about 10,000 years. They have two facilities, both of them in Iceland, that we've helped fund. They have a range of paying customers, everyone from Microsoft in the US to here in the UK, British Airways.

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One thing we noticed when we first invested was actually, that a lot of their customers were actually holdings of ours, Shopify, Stripe and Ocado. I would say that Climeworks is again at the earlier end of what we do, but there is that potential that if they are successful, they are the pioneers of

a new multi-billion-dollar industry. Where the founder talks about in the future, for future generations, these carbon removal plants will be as common as wind farms are today.

That could potentially have a really material impact, we hope financially for shareholders, but also it is possible if they succeed, that they will quite literally change the world.

CS: Amazing. And then, Tom, I'm going to stick on this theme of the energy transition, because there has been a bit in the press recently on our of our holdings, Northvolt. Could you perhaps give us an update on what has been happening here?

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TS: Northvolt, the investment case there is that batteries will become much more prevalent and that regions of the world, countries in the world will want domestic supply chains. Northvolt has a European champion in this technology, which is capable of delivering batteries that had a very strong green supply chain and would be a reliable source for local manufacturing.

They are having some challenges. Partly, you've seen very strong competition from Asia, partly that you've seen the rate of demand growth for EVs start to cool a little. And in particular, the Western European manufacturers have not been having great success in this market. That's a challenging backdrop.

At the same time, a bit like Chris Miller was talking about earlier in semiconductors, making batteries is hard. Actually scaling those facilities and getting the cost efficiencies of getting to scale has been really challenging for them. You've seen some announcements about restructuring and reducing the scale of their ambition to focus on getting the early facilities producing at the rate that they need to, to be competitive.

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CS: Perfect. And Tom, I'm going to stay with you because I think the question I've had more than any other this year, and it comes as no surprise, there was a huge volume of questions submitted on this topic. When do we think the IPO market is going to fully open again? Can you perhaps give us an update on what is your outlook for private companies coming to markets? Are there any IPOs on the horizon?

TS: We've come through a big cycle in this, where in 2021 we were seeing a lot of IPOs and then it probably turned out to be the case that 2023 was a

trough year with very, very few companies moving from being private to listing on the stock market.

Things have improved a bit in 2024, but it's still nothing like the pace you might expect. We had one of our holdings, Tempus AI, list. This is a company that does testing for cancer patients to help determine the genetic basis of their disease, help recommend treatment pathways. On your theme of purposeful capital, I think we put about a quarter of all of the primary capital that went into Tempus. And you now have this service that exists that is really helping to improve outcomes for patients. I think that really is very purposeful capital.

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But back to this question, I think there are various macro variables that determine the pace at which companies come to the market. I think confidence is an important one. I think interest rates is an important one. I think, as well, meeting what the market wants and whereas there was huge appetite for companies that were growing very quickly, but weren't profitable three or five years ago. I think as a company, either being profitable or having a clear path to profitability has become a really important variable.

I think 2024 is an improvement on 23. I feel more optimistic as I look into next year. And in part because there is just this huge pipeline of companies that have effectively been trapped for the past three years, where the pressure is building and building to actually move, make that transition to a public company.

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CS: Thanks, Tom. I mentioned in the intro about Scottish Mortgage being unique in many ways. And actually because of our structure, we're a closed-end fund, which is evergreen in nature, so we have that ability to own companies throughout their entire growth cycle, from private to public.

Lawrence, you mentioned Spotify earlier. It's probably a really good company we can use to illustrate this. Can you perhaps talk us through that journey from our initial investment back in, what, 2015, I think it was, to today and the importance of having that long-standing relationship with the company as well?

LB: In some ways, that seems shocking that was almost a decade ago. Me and Tom both went to go down in London for our first meeting with them. I remember getting up excruciatingly early and flying down to London to see them.

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I said earlier that our ideal is when we're investing in companies that are showing traction, and at that point, Spotify was showing superb traction. They were outcompeting free music in Sweden, their home market. They'd reached about 75 per cent of total music consumption.

We invested in 2015 for around \$56 a share. We did a follow-on round, which we invested in in 2017. And then they had their direct listing in New York in 2018, and we again put more money in at that point, I think at around \$130 a share. We pretty much didn't sell any until only a few months ago, earlier this year, at around \$300. That's an example of a company that has bridged that private/public divide.

There's a couple of advantages, I think, that come with that. The first is the obvious one, that we're able to create value for shareholders, not just as a public company, but also when it was a private company.

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The second I think in some ways is a bit more interesting. What really, really mattered, I think, was that those few years allowed us to really get to understand the company better and to build a really genuine relationship with the people that were running and building it. If you compare that to when you meet people in an IPO situation for the first time, where they're coached by investment bankers of what to say and what not to say, and they're trying to give you the most positive story possible, that's a very different environment.

And so, today I think our access is actually better because we're private holders. They actually emailed on Friday, offering to introduce us to the CFO, who's new and just started last week. We get to meet Daniel Ek regularly now. And I think we might be, if not the only, then certainly one of the very few people in the world that get to meet him on a one-on-one basis these days.

In many ways, our advantages didn't stop when it became a public company from being private. It carried on in terms of the understanding that we'd built up and in terms of the relationship that had been built.

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CS: Thank you, Lawrence. As a final question, we put a poll out in our social media, which private company did our shareholders most want to hear about. Thank you to all those that voted. The standout winners were quantum computing company, PsiQuantum, and Blockchain.com, which is the platform that enables the transaction of cryptocurrencies.

To finish, Lawrence, I'll give you the incredibly easy job of explaining quantum computing and PsiQuantum. And maybe, Tom, you can take Blockchain.com. Lawrence, over to you.

LB: PsiQuantum is a company that is developing quantum computers. Every computer we use today, whether that's a smart phone, a tablet or a computer in the cloud, works on classical computing. Quantum computing would be something very different.

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The best quick analogy to try and explain how quantum computing works would be if you think of a really complex problem to solve and analogue that to the most complex maze that you can imagine. A classical computer would try and solve that maze by going through one pathway at a time to try and find the exit. That would take a while, but it would do it eventually.

A quantum computer, because of superposition and because of entanglement, is able to explore every single pathway of that maze simultaneously, and will therefore find the exit a lot quicker. The result of that is that you've had studies that have shown that a classical supercomputer might take half a century to solve a problem that a quantum computer could solve in seconds.

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That leads into really interesting areas, cryptography, weather forecasting, high fidelity molecular simulation. It could give us everything from faster drugs to better fertilisers, superior battery chemistries.

The opportunity there is immense. In terms of progress, they've signed just in July a deal with the State of Illinois to build the first utility-scale quantum computer in the US, in Chicago. It's again at the earlier end, and we shouldn't be under any pretence that what they're doing is incredibly difficult and it will take time, but this does have the potential if they're successful to really be a pioneer in a new industry.

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CS: Thanks, Lawrence. Tom, over to you on cryptocurrencies.

TS: I think I get the easy job.

CS: You've definitely got the easy job there, I think.

TS: What Blockchain.com is doing is providing access to cryptocurrency, providing the services that a bank might provide in traditional fiat currencies. They are benefiting because they're one of the survivors of the

severe downturn that we saw in crypto markets over the past three or four years. As you've seen life return to that area, they're benefiting from a much-enhanced competitive position.

Link it to, here's an obscure example for you, why this is a purposeful company. One deployment of mining for cryptocurrency we've seen has happened in Sub-Saharan Africa. Where, as a company now, it's economical to install a solar facility to provide energy for a village. Use it to run a crypto mining machine that produced cryptocurrency, which is valuable, and then the village gets to benefit from the rest of the power that's generated by that installation. You can pay for the installation using the crypto mining.

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It's a nice combination of Starlink, which is providing the internet connection that makes that possible, and a company in the crypto space that enables that sort of transaction.

CS: Super. Two pretty exciting companies to finish on. As a final comment, I think as a team we have made a real deliberate effort over the last couple of years, to really try and increase our transparency and disclosure on our private companies. We have to strike the balance between respecting private companies' desire for discretion and the NDAs we sign. But we've strived to share as much as we can, to not only give shareholders comfort on areas such as evaluation process, but to also keep you up to date on the amazing and exciting progress these companies are making.

All this information can be found on our website, at scottishmortgage.com. Tom, Lawrence, thank you very much. And I hope everyone watching found this session useful. Next up we have Lawrence in conversation with CEO and co-founder of Wise, Kristo Käärmann. We'll see you in a few minutes.

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Scottish Mortgage Annual Past Performance To 30 June each year (net %)

	2021	2022	2023	2024	2025
Share Price	62.8	-46.1	-6.3	33.4	17.5
NAV	70.1	-38.8	1.9	15.1	19.3
Benchmark*	25.0	-3.6	11.7	20.4	7.8

Performance figures appear in GBP. NAV (Net Asset Value) is calculated with borrowings deducted at fair value for 1, 3 and 5 years and par value for 10 years. *FTSE All World Index (GBP) TR. Performance source: Morningstar and relevant underlying index provider, total return.

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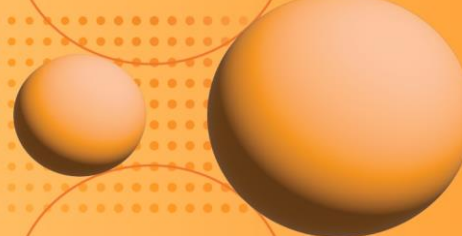
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