

# International Smaller Companies Q3 investment update

October 2024

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Investment manager Brian Lum and investment specialist Eoin Anderson give an update on the International Smaller Companies Strategy covering Q3 2024.

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**Your capital is at risk. Past performance is not a guide to future returns.**

**Eoin Anderson (EA):** Hello, and welcome to the Q3, 2024 update for the International Smaller Companies Strategy. My name is Eoin Anderson and I'm a specialist on the strategy, and I'm joined today by Brian Lum, who's the lead portfolio manager. Today, we hope to talk about team activity, portfolio activity, performance and outlook.

But first, as a quick reminder, International Smaller Companies is a small cap strategy looking to invest in small, exciting, and most importantly, growing businesses from within the international equity universe.

So, Brian, we're well past the halfway point of the year, we're coming towards the end. How is the team progressing against its goals, its objectives, hopes for the year?

**Brian Lum (BL):** Thank you. Our objective is really very simple. It is about finding a diverse range of great growth companies in the small cap universe. We invest in them with a long-term mindset, and we deepen our understanding in these companies over time.

And we have been very busy. Each year, we aim to engage with the vast majority of our holdings in the portfolio, and we're on track to achieve that. And overall, we are broadly reassured by what we've heard in these meetings and in calls.

**EA:** It sounds like there've been quite a few face-to-face interactions with companies. Maybe you could share a little bit more detail?

**BL:** Yes, face-to-face interactions is a hugely important part of our research process. For example, I visited Taiwan earlier this year, where I met some of the largest positions in the portfolio. Praveen, who's our Japan specialist, he spent five weeks in Japan over the summer and met over 60 companies, again, including many of our holdings. Remya, together with our analyst David, they just came back from Sweden, having met 20 or so companies. And Tom Fenton, who's also on our team, he met dozens of companies in Southeast Asia. That trip is more about new buys, potential buys, than existing holdings.

And on top of that, we have our usual Zoom calls, and also smaller trips to Europe. So, we have been covering our major markets on a systematic basis. On top of that, there's the usual input from our colleagues from around the investment floor as well.

**EA:** So has all of this led to any portfolio activity or changes?

**BL:** Absolutely. So, the research from the trips have contributed new buys as well as some changes. Let me just give you two examples when it comes to new buys.

One is Andes Technology. It is a Taiwanese company that focuses on silicon IP (Intellectual Property). They build RISC-V (Reduced Instruction Set Computing - five) based CPU (Central Processing Unit) cores, and in layman's terms, think of RISC-V as an alternative way to build computer brains to what Intel and Arm offer. We have been doing some work on the RISC-V ecosystem. It is fast-growing and has lots of potential, and Andes is an exciting one. It falls under our transformational growth bucket.

Then we've got Philippine 7, which is far easier to describe for my own benefit. Philippine 7 is the 7-Eleven franchise in the Philippines. It is the leading convenience store brand in the country and still a very long growth runway left. But what really caught our eye is the parent's backing here. The parent is President Chain Stores, which is a company that we've long admired as a high-quality operator in Taiwan running [the] 7-Eleven franchise there as well.

Another recent new buy would be Xtep. This is a sportswear brand in China, very focused on running. Increasingly you see Xtep very well represented in marathons and so on. Now, running is an activity that is gaining in popularity and very much supported by the government as well. We've been following the company for some time, with multiple reports on our research history, and we think it has excellent potential. And it also brings some direct exposure to Chinese consumers, which we don't have in the portfolio.

The other new names would be ViTrox, which is a Malaysian testing equipment company, and also Fugro, which is a geo-data specialist. But I think we covered those in previous occasions.

**EA:** So quite a few new ideas. How have you been making room for these within the portfolio?

**BL:** We exited quite a few names so far this year, and there are two broad themes here. One is some of the names exited because of acquisitions. Recent examples there would include Keyword Studios, which is an Irish video game company. They were acquired by a private equity firm, EQT. Another one is New Work. It's a long-standing holding. You can think of that as Germany's LinkedIn, if you will. It was taken private by its existing lead shareholder.

The other theme would be we exited a number of smaller Japanese holdings. It is very much a conscious effort on our part to express our views in Japan in a clearer way. So, some of the proceeds that we got from these exits were reinvested into higher conviction names, such as Sansan, GMO Financial Gate.

**EA:** So, mentioning Japan there, mentioning China slightly earlier on, it feels perhaps like some of the macroeconomic headwinds have been clearing slightly. How has this impacted performance?

**BL:** Yes, those macroeconomic headwinds that you mentioned have been incredibly tough for us over the past two or three years. I'd say that the market conditions remained difficult and volatile for most of the year so far. But very recently, we are seeing some positive signs.

For one, the yen has strengthened. As a reminder, the yen has depreciated massively over the past four or five years. It got to 160 yen per dollar at one point earlier this year. It bounced back to 146 today, I think, and that has certainly helped our Japanese holdings. It has been one of our strong contributors to performance this quarter.

The other one would be that Fed (the Federal Reserve) has cut interest rates. That always helps growth investing, in particular sentiments on small caps, which are often seen as a riskier asset class.

Our absolute returns recently have been good. In relative terms, we are marginally behind this quarter. And this gap is in so much explained by one stock, Global UniChip. Global UniChip has been a solid long-term performer for us. But in the short term, share price can be all over the place. For example, ramp-up schedules for its latest AI projects and so on can be subject to change. Global UniChip is one of the companies that we have in the portfolio exposed to AI, which is a powerful theme for us, but in the short term, there can be sharp ups and downs.

**EA:** Okay, so as we look into not just the final quarter, but obviously as long-term investors, way beyond as well, any reflections to share?

**BL:** We are very excited by the opportunities that we see. Despite a recent bounce in small caps, I would say that, as an asset class, it remains deeply out of favour. Looking at [the] valuation gap between small caps and large caps, it remains clear, the gap remains at historic highs.

In the meantime, we are broadly encouraged by the fundamental performance of our holdings, and we do have a strong pipeline of new ideas waiting in the wings.

As for ourselves, we would recognise that our performance has been disappointing in recent years. We are working on a number of evolutionary process improvements, as ever, and we are confident that we will turn this around. But what won't change is our commitment to investing for the long term and to growth investing.

**EA:** Thanks very much, Brian. If you have any further questions, please don't hesitate to get in touch with us here at Baillie Gifford. Otherwise, we look forward to talking to you next quarter.

## International Smaller Companies

### Annual past performance to 30 September each year (net%)

	2020	2021	2022	2023	2024
International Smaller Companies Composite	40.6	23.6	-45.5	16.5	19.7
MSCI ACWI ex US Small Cap Index	7.4	33.5	-28.6	19.6	23.8

### Annualised returns to 30 September 2024 (net%)

	1 year	5 years	Since inception*
International Smaller Companies Composite	19.7	5.7	5.3
MSCI ACWI ex US Small Cap Index	23.8	8.7	7.8

\*Inception date: 28 February 2019.

Source: Revolution, MSCI. US dollars. Returns have been calculated by reducing the gross return by the highest annual management fee for the composite. 1 year figures are not annualised.

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