SAINTS MANAGER INSIGHTS

Approaching its half-century of dividend growth, co-manager James Dow provides the SAINTS managers' annual update

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James Dow: Hello, and welcome to this annual update on SAINTS, the Scottish American Investment Company. I'm James Dow, I'm the head of the Global Income Growth team at Baillie Gifford, and one of the managers of SAINTS.

A simple solution for two types of investor

SAINTS is managed with two types of investor in mind. The first is the investor who is looking for capital growth together with a resilient income, an income which can be relied on year in and year out, and which over time grows ahead of inflation.

As the managers, we invest most of SAINTS' portfolio in equities to achieve these goals. At the heart of SAINTS is a portfolio of around 60 different companies from around the world, all of which we believe have excellent long-term prospects for real growth, ahead of inflation, in profits and dividends. Names such as Apple, L'Oréal and Novo Nordisk.

Because of our focus on steady long-term compounding in profits and dividends, year after year, SAINTS also appeals to a second type of investor. That's the type of investor who doesn't necessarily need the income that SAINTS pays out every quarter, but who is attracted by the style of our investment approach.

Our approach has, over time, delivered steady capital growth. And so alongside income investors, we also serve shareholders who are simply looking for long-term steady growth in their capital.

SAINTS 150th anniversary

This year, SAINTS reaches the one hundred and fiftieth anniversary of its formation in 1873.

To mark the 150th anniversary, and to help provide the benefit of perspective, the board and Baillie Gifford have commissioned a short history of SAINTS, in book form, which will be available by early June. You can request a copy at bailliegifford.com/SAINTS150.

A lot has happened over the past 150 years, but a key point you will find illustrated in the book is that, throughout its history, SAINTS has been able to take advantage of opportunities to invest globally, and by doing so, support and benefit from the economic and technological progress that drives capital and dividend growth.

It has also been very resilient, weathering many storms and setbacks that have arisen over the years, from the railroad boom and bust in the US in the 1870s, two world wars, and several periods of high inflation, right up to the present day.

It has always had an engaged and active board, seeking shareholders' best interests, and making sure SAINTS stays on course.

We are optimistic that SAINTS' 150th anniversary year will also be its 50th consecutive year of dividend growth.

A review of 2022

In a challenging year for the global economy and financial markets, the net asset value of the company fell 3.7 per cent last year. Although a positive return would have been preferable, we believe this is a reasonable result in the circumstances.

The net asset value return of SAINTS once again exceeded the return from our global equity benchmark, which fell 7.3 per cent in 2022. And the performance of the equity, property, infrastructure, and fixed income investments all compared favourably with benchmarks in their respective asset classes.

SAINTS has outperformed equities as measured by its equity benchmark over the past one, three, five and ten years. We believe this is a testament to the special companies in which SAINTS invests, with their good growth opportunities, good returns on capital, and good management teams.

The equity portfolio represents about 85 per cent of the Company's gross asset value. But what about the other asset classes?

Well, our infrastructure and emerging markets sovereign bond investments delivered the best-performance of any asset class last year, both delivering positive total returns. Both of them are good diversifiers for SAINTS, and they did well as other assets struggled.

The property portfolio faced a more challenging environment, as rising interest rates adversely affected valuations. But the underlying performance remained good, with the portfolio fully let and, crucially, the portfolio retains its strong focus on inflation-linked and increasing rents.

SAINTS recently announced its final dividend for 2022, and this marked the 49th consecutive year that the Company has raised its dividend.

The board decided to increase the dividend by just over 9 per cent over the full year, which was broadly in line with UK CPI inflation. And that dividend was fully covered by the Company's earnings.

The bottom line is that SAINTS' shareholders own a portfolio that proved its resilience once again in 2022, and we believe it is well-positioned for the future.

The outlook for the global economy is showing tentative signs of improvement, and we're optimistic about delivering steady growth in earnings and dividends in 2023 and beyond.

Changes in the portfolio

We are big believers in investing for the long term and have low turnover in our portfolio from year to year. Still, it was a little surprising to us that during the course of 2022 we made only three new equity investments.

We are not short of ideas. Growth stocks have fallen out of favour, and we might have expected to acquire, opportunistically, more stocks whose price/earnings multiples have been de-rated.

But we tried hard to remain disciplined in the face of last year's market turmoil, and we only bought new holdings where we see an excellent fit, and where we believe the long-term returns are firmly skewed in SAINTS shareholders' favour.

Our three new equity holdings, Intuit, L'Oréal and Cognex, all fall into that category.

L'Oréal, the French-listed beauty products company, is a firm which we believe still has many years of growth ahead of it, with resilient dividends along the way.

Cognex, which is a world leader in machine vision, is likely to be a bit more cyclical, but we believe it has very attractive long-term growth prospects and the company is committed to paying a progressive dividend.

Lastly, Intuit, the software company, also has great growth potential and again we expect its dividend to be resilient.

On the other side of the ledger we made four dis-investments last year: Kimberly-Clark de México, Hiscox, Haleon and CH Robinson. You can read more about all of these investment decisions in the Managers' section of the latest annual report.

Our evolving approach to environmental, social and governance (ESG)

There is much debate around ESG and the importance it should have for asset managers. We are very much of the same view as SAINTS board on this matter.

Our shared belief is that sustainability analysis is absolutely vital to meeting the Company's investment objectives over the long term. This is why, for every SAINTS holding, as managers we complete a deep analysis of ESG opportunities and risks.

The board has adopted and published a clear ESG policy for us to follow. And as managers we engage proactively with all our holdings on numerous topics to ensure the long-term compounding that we seek on behalf of shareholders has every chance of being delivered.

SAINTS' latest Stewardship Report contains many examples of our engagements over the course of the past year. For example, we have encouraged our software holdings such as Apple and Microsoft to continue pushing towards best practice in data privacy and supply chain management.

And we have voiced our desire for UPS, the package company, to lean into electrification and emissions reduction from its transport fleet.

Companies that do not respect and benefit wider stakeholders are less likely to deliver the long-term compounding in profits and dividends that is core to achieving SAINTS' financial objectives. So ESG analysis will remain central to our work as managers.

Debt refinancing: a watershed year

One of the advantages that investment trusts have over open-ended funds is their ability to borrow long-term debt, as long as it is done prudently, and then invest those borrowings in assets which should deliver a higher level of income and return than the cost of borrowing. We can then pay out that surplus income to SAINTS shareholders.

During the course of 2022, the larger part of the Company's borrowings were refinanced at a rate agreed in 2020, before inflation started shooting up. So, in an environment when interest rates have been rising substantially, the cost of the SAINTS borrowings has actually fallen very significantly.

The debenture maturing in April 2022 had a coupon of 8 per cent and the new borrowings replacing it have an average cost just below 3 per cent per annum.

The refinancing of the long-term debt appears to have been well timed and the Company is now well placed to use its borrowings to enhance returns and support the dividend.

Outlook for 2023

As we begin 2023, we remain humble about our ability to foresee what is just around the corner. If we look back at forecasts from the start of 2022, or 2020, we see that very few people predicted the major events that subsequently transpired, such as the war in Ukraine or Covid-19.

As 2023 gets underway, there are tentative signs of hope triggered by lower energy prices and reduced interest rate expectations. But we shall see what transpires.

What we can say with confidence is that SAINTS owns a portfolio of assets that have proved resilient to some extreme tests over the past few years.

Earnings have grown steadily, and despite the shock of a global pandemic, which caused many income-generating investments to stop or slash their distributions, SAINTS has extended its track record of dividend increases to 49 consecutive years. In 2022, the Company's earnings and dividend broadly kept pace with inflation, with the dividend increasing 9 per cent, fully covered by earnings.

Whatever happens in the world at large, as managers we will continue our search for steady long-term compounding in earnings and dividends.

We made a number of new investments in 2022 which we believe upgraded the resilience and growth potential of the Company. And we have lots of good ideas in the pipeline.

There are no certainties in investing. But we do believe that, whatever winds may blow, and as far as we are able to ensure as managers, the odds remain skewed strongly in favour of long-term capital appreciation and dividend growth in the years ahead for SAINTS shareholders

Share Price Performance to 31 December each year (Net %)

	2018	2019	2020	2021	2022
Scottish American Investment Company P.L.C	-1.6	25.1	12.0	19.5	-3.5
FTSE All-World Index	-3.4	22.3	13.0	20.0	-7.3

Source: Morningstar and underlying index provider, total return sterling.

Dividend Performance to 31 December each year

	2018	2019	2020	2021	2022
Total dividend per ordinary share (net) – (pence per share)	11.50	11.875	12.00	12.675	13.82

Source: Baillie Gifford & Co.

Past performance is not a guide to future returns.

The views expressed should not be taken as fact and no reliance should be placed upon these when making investment decisions. They should not be considered as advice or a recommendation to buy, sell or hold a particular investment. If you are unsure whether an investment is right for you, please contact an authorised intermediary for advice.

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SAINTS invests in overseas securities and changes in the rates of exchange may also cause the value of your investment (and any income it may pay) to go down or up.

The Trust invests in emerging markets, which includes China, where difficulties with trading, liquidity, regulation and taxation could arise, resulting in a negative impact on the value of your investment.

SAINTS has some direct property investments, which may be difficult to sell. Valuations of property are only estimates based on the valuer's opinion. These estimates may not be achieved when the property is sold.

The trust can borrow money to make further investments (sometimes known as “gearing” or “leverage”). The risk is that when this money is repaid by the trust, the value of the investments may not be enough to cover the borrowing and interest costs, and the trust will make a loss. If the trust's investments fall in value, any invested borrowings will increase the amount of this loss.

FTSE