

International Growth Q4 investment update

January 2024

Client relationship director Nick Thomas and investment specialist Hamish Maxwell give an update on the International Growth Strategy for Q4 2023.

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

Hamish Maxwell (HM): Hello, I'm Hamish Maxwell, an investment specialist on Baillie Gifford's International Growth Strategy. And I'm joined by Nick Thomas, who's been a member of the strategy's Portfolio Construction Group since inception 20 years ago.

Thanks for joining the video. We're going to touch on recent performance and our reasons for optimism about the future.

International growth is a long-term, active, growth investment strategy. 50+ of what we see as the most exceptional growth companies in international markets. These are businesses with rapid or robust growth potential, that we can own for at least 5 to 10 years, allowing competitive advantage to become financial success.

Nick, experience tells us that our style of investing can be really valuable when it allows us to capture the most extreme winners, but it can also be volatile in the short term. Is that fair to say?

Nick Thomas (NT): Yeah, that's right, Hamish. I think we've just experienced that, haven't we? After a very strong decade of growth investing, the last three years have been a lot more difficult for us. Our portfolio was not very well positioned for the end of the pandemic and our more highly valued growth stocks proved very sensitive to the inflation and interest rate cycle that we've been going through.

Now the market's view of the inflation outlook moved around a lot during 2023, and I think that contributed to quite an inconsistent year of performance for us. But it was good to end the year on a positive note. So, the portfolio was up around 12 per cent in the fourth quarter, which is around 2

per cent ahead of the benchmark, and it rose by about 15 per cent for the whole of 2023. So good result in absolute terms, although that was slightly behind the benchmark over the year.

HM: So how did our holdings contribute to these returns?

NT: Okay. So, in the fourth quarter, at the sector level, I.T, industrials and financial stocks led the way. So an interesting blend there. In financials, Adyen enjoyed a very sharp rebound after a pretty large profit warning in the third quarter, and in the fourth quarter it reassured investors about its long-term profitability, and the stock regained a lot of the lost ground. So, a slightly unusual episode with Adyen. In the IT sector, ASML again, which we talk about a lot, reported good results with global demand for its lithography systems still outstripping supply. And alongside Elastic, I think ASML also benefited from its status as a beneficiary of the AI boom that we're all getting to grips with.

Two of our large industrial holdings, Vestas Wind Systems and Atlas Copco both reported good results as well. Strong revenue growth [and] rising margins were quite a theme in the portfolio and they performed well.

And two of our e-commerce platforms, so MercadoLibre and Pinduoduo also contributed during the fourth quarter. MercadoLibre beat expectations, continuing to grow with record margins. And Pinduoduo's revenue was up nearly 100 per cent - good progress domestically in China and some spectacular growth from its international marketplace app Temu, that quite a few of us are probably getting to grips with ourselves.

On the negative side in the fourth quarter, our health care stocks had a pretty tough time. So, in biotech, Genmab and Argenx both released some disappointing pipeline updates. They've both got really successful initial drugs in the market, but some follow-on products have had mixed data from trials and they both fell back. And also our contract research and manufacturing player, Wuxi Biologics, which has a very broad exposure across the industry, they reduced their revenue guidance - biotech funding has declined and there's a knock-on effect on Wuxi. And I think there have also been some approval delays at the FDA. So that's it sector by sector and by the stocks.

But I think more broadly, the valuations of many of our holdings had a boost in the fourth quarter as the market decided that the interest rate cycle had definitely turned this time.

HM: So, looking forward, I know the team is feeling optimistic. Can you give us a sense of where that's coming from?

NT: Yeah for sure. We do maintain an optimistic mindset. I think perhaps we have to as growth investors. Where's it coming from? Well, as always, we take our strongest signal from what we hear from our companies. They are continuing to invest heavily for the future. They're innovating to solve important problems. And that's where our long-term value creation is going to come from. So that's our source of optimism really.

In terms of staying optimistic ourselves, we've been reflecting on the importance of morale in investing. So Tom Coutts who chairs our portfolio construction group has drawn attention to some writings by Field Marshal Slim, who wrote about the challenges of maintaining morale and getting an army through tough periods. This could also be relevant to us in investing when we're not performing very well. Maintaining our morale helps us to stay focused on the future, which we're definitely trying to do, and to stick to our philosophy and our approach despite some setbacks.

So, morale remains strong.

And in the quarterly letter he wrote to our clients, Tom also wrote about the importance of remaining credulous, which is a word you don't often see in investment where credibility and confidence are so important. But being credulous, means remaining open minded and literally being willing to believe in things. So, we try to be credulous and willing to believe in some uncertain opportunities.

That's what we need to do to find the great growth stocks for the next decade.

HM: And so, you've touched on performance a couple of times. It has been a torrid couple of years for us in performance terms as there were rapid rate rises and extreme risk aversion, [which] have brought growth valuations down from the highs they reached. People are understandably asking questions - can growth provide attractive returns from here?

NT: Yes, we believe the answer is yes. Valuations were very high, now they're not. I would say they're in the middle of a long-term range in terms of growth stocks against the general market. And whilst that's the case, our growth companies, are executing really, really well. And some of the themes that they are exposed to are, if anything, accelerating.

So we think these are very, very important businesses for clients to have in their portfolios. In terms of the areas of enthusiasm and themes that we are excited about, we continue to focus on digital infrastructure, the energy transition and health innovation and we're finding great businesses in those areas that we think will provide fantastic returns in future. We've talked about China quite a

lot in our updates and our awareness of the risks in China has definitely increased due to domestic regulation and geopolitical tension.

But there are still opportunities in China. We've reduced our Chinese weight a little bit during the course of 2023. It's now more concentrated in the areas of energy transition and consumer internet companies - in both of those fields where China is a real global leader.

HM: And so in terms of transactions then, turnover remains low. It's about 10 per cent, which is very much in line with our 5 to 10 year horizon. But our analysis did lead to some transactions in Q4. Would you like to touch on those please?

NT: Yes, for sure, Hamish, it did. We sold two small holdings we had in a couple of Norwegian companies, Adevinta and Schibsted, which both came out of the same media group a few years ago. Essentially, we think they're quite mature and we see some better opportunities elsewhere. We've also reduced several of our smaller holdings that have been performing well. So we've trimmed Spotify, Ferrari, Wix and ASML. And we've also reduced our holding in the luxury goods company Kering. Now we've held Kering for a very long time. We've now got a little bit more cautious about the strength of some of its brands in its portfolio. So we've been trimming that holding back a little bit.

And realizing those sales have allowed us to take a new holding. So we've bought Atlassian, which is an Australian software company working on collaboration software, which is increasingly important to all businesses. We've also put money into Shopify, the platform that allows small businesses to sell competitively online. And finally we've bought the French business Soitech, which makes engineered substrates for the semiconductor industry.

HM: Well thanks for joining the conversation Nick. And in summary, on the outlook, there are signs that some macro pressures on growth are starting to ease. And when this combines with our long-term exposure to growth trends and our holdings' operational progress, this can lead to really good long-term returns. We hope you find this a useful update on the International Growth Strategy and if you have any further questions, please reach out to your client contact.

Goodbye from Edinburgh.

International Growth

Annual past performance to 31 December each year (net%)

	2019	2020	2021	2022	2023
International Growth Composite	36.7	64.6	-10.1	-36.3	15.0
MSCI ACWI ex US Index*	22.1	11.1	8.3	-15.6	16.2

Annualised returns to 31 December 2023 (net%)

	1 year	5 years	10 years
International Growth Composite	15.0	8.2	5.1
MSCI ACWI ex US Index*	16.2	7.6	4.4

*MSCI EAFE prior to 30 September 2018.

Source: Baillie Gifford & Co and MSCI. USD. Returns have been calculated by reducing the gross return by the highest annual management fee for the composite.

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