Baillie Gifford™

UK Core
Q1 investment update

April 2025

Investment manager Iain McCombie and investment specialist Chloe Darling-Stewart give an update on the UK Core Strategy covering Q1 2025.

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Chloe Darling-Stewart (CDS): Hello, and welcome to this Baillie Gifford UK Equity Core Strategy update. My name is Chloe Darling-Stewart, I'm an investment specialist with the team, and I'm delighted to be joined today by Ian McCombie, who is head of the UK Team and lead portfolio manager on the strategy. Welcome, Ian.

Iain McCombie (IM): Hi, Chloe.

CDS: As a brief reminder, our UK Core Strategy is looking to find the very best of British businesses and invest in a portfolio of 45 to 65 companies for the long term. Over the next 10 minutes or so, Ian and I will discuss what's been going on in the market, some of the key drivers behind recent performance, portfolio activity, and then finally on why we remain confident about the prospects for your portfolio going forward.

So to kick off, Ian, it's been a particularly volatile quarter. Given your three decades of experience, how would you say this quarter compares to other turbulent periods that you've navigated? And what lessons can we learn from that?

IM: I mean, Chloe, you're right that it has been a volatile quarter, particularly for our performance relative to the index. But in terms of that experience point, I think it's a really useful context, because when I look at my career and the core strategy, in terms of 3 per cent outperformance or underperformance after fees, this is only the ninth time this has happened. So it has happened before. So, this is not unprecedented.

So, although in some respects what was happening over in the US with President Trump and what he's talking about, we've had volatility before. And what's really important for us is to stick to our knitting in the sense that we're looking at bottom-up opportunities for that.

We're cognizant of what's going on in the top-down or the macroeconomic backdrop, but we are very much bottom-up investors and we're trying to focus on that.

CDS: And as you say, it's been quite a challenging period for performance. It was flat over the quarter and lagged the index. Could you perhaps walk us through some of the key themes or some of the specific holdings that were driving that?

IM: Yeah, I mean, I think one of the things about, as you said, what the volatility has done is caused a lot of uncertainty because people are not quite sure what does this mean for the global economy or let alone the UK economy.

And what you've seen in the UK in particular in the stock market is a kind of flight to safety. So some of the big defensive companies have done very well, that you might expect. But also the other area that's done very well, which we haven't owned, are some of the big defence companies, such as BAE and Rolls-Royce. We actually have owned another company, which I'm sure we'll come back to, which has helped us. But those are some of the big themes that have gone against us.

Now, the other factor that I think is worth talking about is the short-term volatility. I think in my colleagues' words as well as mine, I don't think we've ever seen as volatile an earnings season as we've ever seen in my career here.

And what I mean by that is when you had results on the day of a company, you're getting very big share price movements, positive or negative, depending on what they're talking about the outlook. And that is very unusual.

I mean, normally you get – if it's something particularly bad or good, you expect a big share price movement. But what we've seen is very much the market doesn't like disappointment, doesn't like short-term disappointments. And companies are just saying, look, the economy is tough out there at the moment. The market hasn't reacted well to that.

Now, we think that is very much an overreaction, but it's something that is certainly notable and probably not helped us in the short run.

CDS: And in terms of the portfolio itself, have there been any stock-specific issues or concerns?

IM: Yeah, I mean, as I said, if you talked about any disappointments, then that's hurt you. So, for example, Greggs, the food to go retailer, was one of the big negatives in the quarter. Now, what they had said was that actually profits were in line with expectations.

But some people were worried about the fact that their like-for-like sales, which is kind of the sales on their existing stores, had started to decelerate a little bit. But what they also said was that they're putting in some very big investment in new plant capacity over the next few years, and that's going to have an impact on their margins or basically their profits.

And the market doesn't like that, and it's punished the business for that. But actually, when you think about it, it's the right thing to do for this business, because what they're trying to do is to allow this business to have the capacity to keep growing over the medium to long term. And they have to build these facilities.

And what they're really saying is it's the real world, that you build a brand new facility and you're incurring all the costs of that. It will take time for that volume to build up in those facilities until you make those very attractive returns, but the market's short-term focus.

But in the long-term, that makes perfect sense. So again, that's what we're trying to work with, is that the market is very much focused on one thing. But we think the really important thing is that long-term ability for that company to grow. And that's why we're sticking with it.

CDS: And then amongst that, there have been some bright spots of performance. I'm thinking of Babcock, as you mentioned earlier, or some of the financials like St. James' Place. Could you talk us through what's going on at these companies and the long-term prospects?

IM: Yeah. Well, in the case of Babcock, that's the defence company I was referring to earlier. It is actually very well-positioned. It's one of the leading kind of defence companies in the UK. Interestingly, it has virtually no exposure to the US.

So what was seen as perhaps as a weakness in the past is now seen as a strength, because with this talk about Europe having to spend a lot more money on defence, they are really well positioned. They've got a huge exposure to the UK as one of the prime submarine maintenance companies in the UK, but also the fact that they're building ships and so on.

And I think they have some very important strategic assets for the UK. Devonport, which is one of the main bases for the submarines, but also Rosyth and a lot of other things. And importantly, they keep winning new contracts. And they had a renewal of a very important contract to maintain a lot of the Army's vehicles, which has been extended for another five years, which, again, is great news for the business. So that's really well positioned.

St James' Place is a totally different story here. But I think it's really about a new management team steadying the ship. And actually, despite all the– you remember all the negative news last year about fees and so on and changing their fees, actually they still saw very strong inflows into their business, which together with the market going up meant that their assets were up very significantly over the year. And actually that's good news for the business.

And the fact that there's really been no new news or any negative news in terms of what's been happening with fees or any of the kind of other issues that the management are dealing I think it's giving people more reassurance that this business is on the way to be back on track, which is very encouraging and the share price responded to that.

CDS: And turning to portfolio activity, periods of volatility often throw up some opportunities. Have you used this period to make any changes to the portfolio?

IM: Yes, but no. Now, what I mean by that is we have, but not to a huge extent. I mean, by and large, we've stuck with the portfolio because we're very much, ‘if it ain't broke, don't fix it’. And that's been very much our attitude.

But we have looked at a few things. And one thing I could talk about is we've been adding to a company called Shaftesbury Capital, which you may recall we bought earlier this year. Now, this is a London property company. It owns a number of estates in the centre of London.

A very interesting bit of news came out near the end of the quarter, which kind of made us want to add to the position. And that was when they announced that they were selling 25 per cent of their Covent Garden portfolio to the Norwegian Sovereign Wealth Fund.

And what was really interesting was that they're selling it at the net asset value of it. So the same value that the company's valued at on its balance sheet. But the share price is at a 35 per cent discount to that.

Now, that is a very interesting discrepancy, if you want to put it like that. Because here's a very sophisticated buyer coming in, willing to buy one of the prime assets in their portfolio in the centre of London for the net asset value. And yet the share price is saying, no, it's not worth that. That doesn't make sense to us.

But what's also important is that it allows the management team to have the balance sheet flexibility to invest in the rest of their estate now, because they're going to get that money coming in. And as I say, the shares are trading at a big discount. So, we've added to our position.

CDS: The last question I wanted to ask you about, Ian, was looking at the overall health of the portfolio on a fundamental level and some of the operational progress that you see. Could you share your perspectives on where you think the portfolio is at the moment and how confident you feel looking forward?

IM: Yeah. Well, in a funny way, it might sound contradictory. But actually, in tough times, and we clearly are in tough times, that's when the really good companies start to come through. Let me give you an example of that.

Howden's Kitchens, the kitchen company you and I have kind of talked about over the last kind of year or so often. It's had OK numbers recently, but put that in the context of the market backdrop.

The kitchen market in the UK, they reckon, has been down high single digit, which is pretty tough, which is not surprising given the cost of living crisis and the economic growth being very weak. But their own position has been maybe -1. So they've taken significant market share. Which is good news.

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But what's really important is what they're doing at the moment. They're continuing to invest in their product. They're continuing to invest in the logistics. They're continuing to invest in their manufacturing capability.

Now, these things won't impact right away, but over the medium to long term, they're going to have a significant advantage in terms of lowering costs, better service, better choices for the consumer. And I think that's a really important point, is that this is a business that's setting itself up for the future in the tough times.

And because they've got the management, that vision, and they've got the balance sheet to be able to do that, that's really good. Now, that's just one example. I could give you plenty of other ones in exactly the same position. And that's what we're trying to keep looking at. Is the long-term potential of our businesses still intact? We think they are. And that's why we're still very upbeat about the future.

CDS: Well, I think that's a positive, a really positive place to leave things. Thank you, Ian. I hope that's given you a good sense of what's been going on in the portfolio this quarter and why we remain confident about the prospects for your portfolio going forward.

Thank you very much for tuning in and please do get in touch if you have any questions.

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UK Core

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

	2021	2022	2023	2024	2025
UK Equity Core Composite	52.6	-4.7	-7.9	8.2	9.1
FTSE All Share Index	41.0	7.9	-3.3	10.8	12.9

Annualised returns to 31 March 2025 (net%)

	1 year	5 years	10 years
UK Equity Core Composite	9.1	9.6	3.5
FTSE All Share Index	12.9	12.9	4.7

Source: Revolution, FTSE. 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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