

Portfolio Update

Q3 2024

Hamish Maxwell, Investment Specialist

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

Hamish Maxwell: Hello, I'm Hamish Maxwell, an investment specialist with Scottish Mortgage. Thanks for watching this update, to the 3rd quarter of 2024.

I'll bring you up to speed on how we've been navigating choppy markets, a bit about positioning, including our China and private companies exposure and some repositioning, and I'll end on returns drivers and upside potential.

Our purpose at Scottish Mortgage is simple - to maximise total returns over the long term. To do that, we aim to own the world's most exceptional public & private growth companies.

The businesses we want to own address large and growing opportunities they have strong competitive advantages, disrupting their industries or even creating new ones. Many are founder-led and have a cultural advantage.

Exceptional businesses don't change industries, or create new ones, overnight. It takes 5-10 years, or more, and will involve mistakes along the way. That's why our end of the bargain when we find the best growth companies is to be patient and supportive shareholders.

An Optimist's Perspective in Navigating Choppy Waters

What everyone is talking about short term – **macro**



What matters long term – **structural trends**



Navigating choppy waters is further helped by our access to company leaders. This year we have met with 34 of our holdings.

Investors have been navigating a complex backdrop with the market focussed on a number of short-term uncertainties, notably:

1. The interest rate environment
2. And political and geopolitical risk from the US election, to armed conflict and tensions over Taiwan.

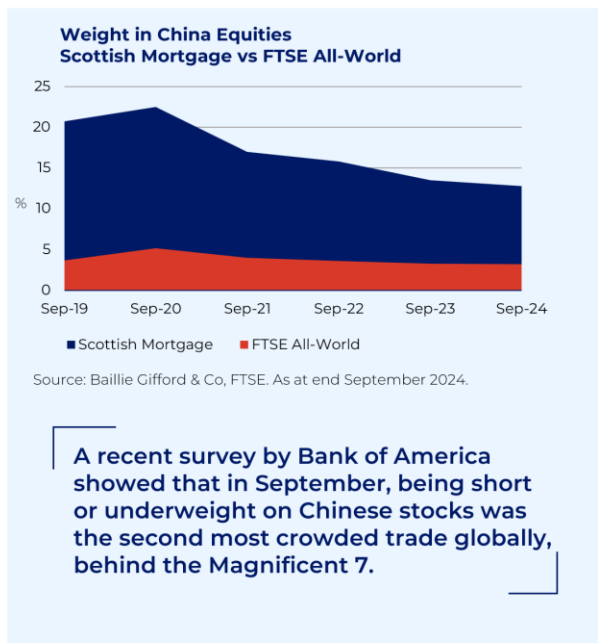
However, as my colleague Claire Shaw mentioned last time, what matters more to us are the long-term structural trends driving growth in the global economy. Mega forces like AI, the energy transition, the digitalisation of the economy, and advances in healthcare.

Growth doesn't move in a straight line. But these transformational forces are creating massive investment in the economy, with enormous upside potential, and we find that really exciting.

Our China exposure, is a little over 10% of the portfolio. It's come down in recent years, as regulatory and geopolitical risks have increased.

China

Against the Herd



But



It's perhaps typical of China's market volatility, that in the last Q alone, we saw a rapid market rise after signs of monetary stimulus from the Chinese government, then a decline when the fiscal detail was somewhat limited.

But our focus is on few companies in China that continue to drive change, and grow their businesses, regardless of market sentiment.

Companies, like electric vehicle maker BYD online content company ByteDance and ecommerce leaders Meituan and PDD. We think these companies offer attractive returns potential.

And during the recent anti-China sentiment which has weighed on share prices these companies have shown lots of operational progress. BYD made 3mn electric and hybrid cars in 2023. Meituan recently delivered more meals in one day than there are people in the UK. And PDD has generated rapid growth in China and overseas, which is a combination that many companies have tried but failed.

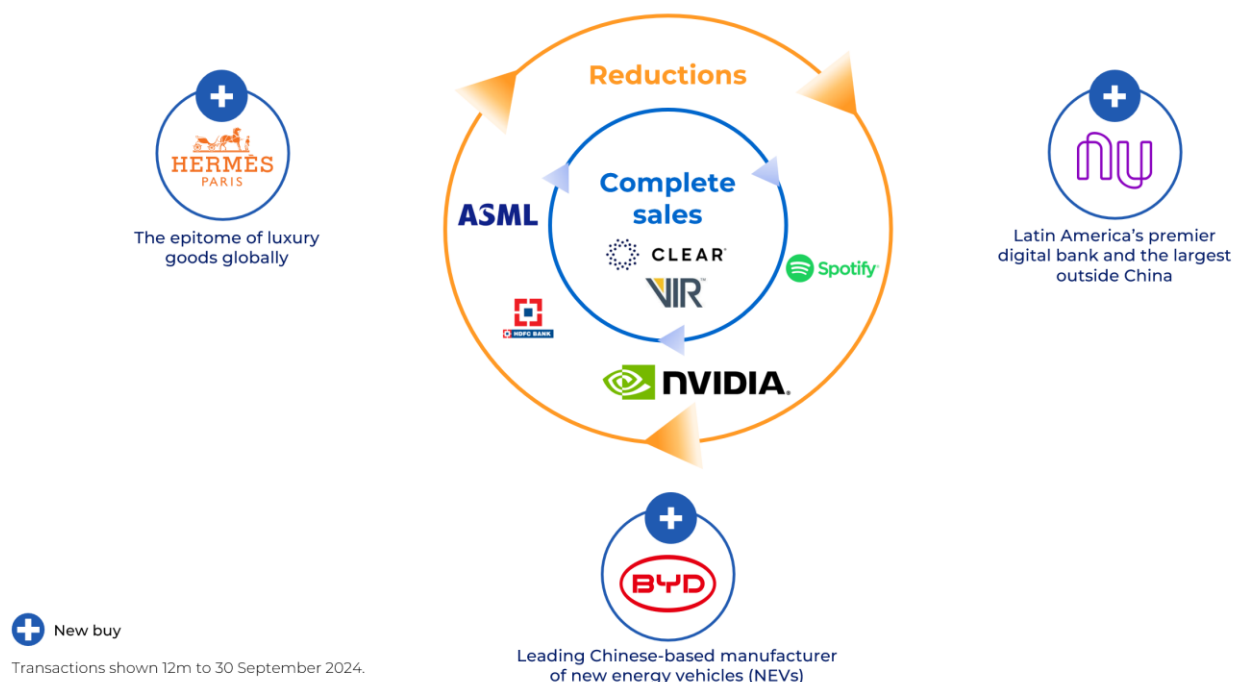
Our view is that China is a place for stock pickers. And though our allocation has come down, we are excited by what a few companies can offer.

Portfolio turnover remains low, and in line with our 5–10-year horizon. But we have been busy with research and engagement. This year we have had dozens of meetings with company management, and lots of written research alongside it.

This has led to some recycling of capital.

Recycling Capital

Competition for Capital Remains as Fierce as Ever



We reduced our holding in chip designer NVIDIA. Given the amazing progress it's made with artificial intelligence, it's become one of the world's largest companies. But as we look out over the next five years, there's a bit more of a symmetric returns potential for NVIDIA, than the asymmetry we look for. We still think AI will have huge application, but to do so it will have to be low-cost. So what does that mean for NVIDIA's rapid revenue growth?

We also reduced ASML, the leading lithography equipment maker used to produce semiconductors. It's got a monopoly in the latest *Extreme Ultraviolet* technology. But as the industry is evolving we've redeployed some capital into leading semiconductor foundry TSMC, whose competitive position has improved recently.

If you're interested in learning more about these companies and the semiconductor industry, please see our insights web page for our interview with Chip War author Chris Miller.

We completely sold our position in VIR biotech, which works to treat and prevent serious infectious diseases, after a strategic pivot by VIR shows perhaps less confidence in its insights and drug pipeline.

We also sold Clear Secure, the biometric identity company which helps customers save time at airports, simply as we found more attractive growth elsewhere.

And we have been finding new and interesting ideas. We bought Nubank, Latin America's leading digital bank, indeed the largest digital bank outside of China. Nubank is working to help hundreds of millions of under banked people in the region.

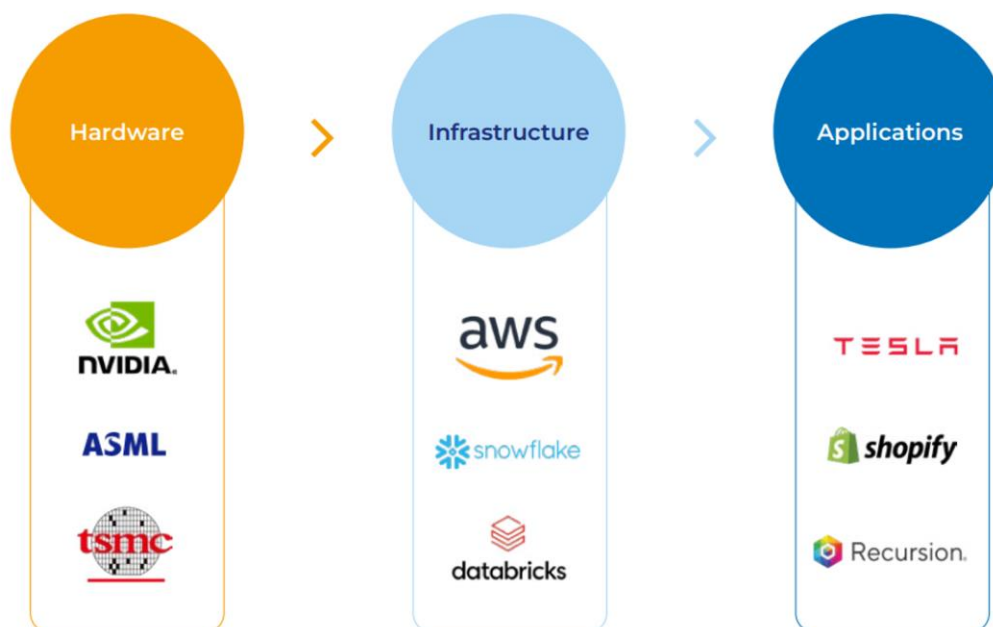
We took a holding in Hermes, the French luxury goods company that's finding new markets for its ultra-high-end products. A 180-year-old company may not seem an obvious Scottish Mortgage purchase, but the market often fails to recognise the power of compounding. Hermes' brand allure and pricing power shows no sign of abating, and there's room for its *exceptional* quality goods in new markets.

We also bought BYD, China's leading electric vehicle maker. BYD is one of the reasons that China has come to dominate the new and growing EV industry, thanks to its vertical integration and virtuous cycle of cost and scale.

After decades of science fiction, artificial intelligence (AI) is finally here and it is changing the world. Innovation drives profits. And the rise of AI has been a primary contributor to market performance recently.

Artificial Intelligence

What happens next as AI enthusiasm broadens to involve more companies?



Phase 1 has been the hardware that makes AI possible, and this is the microchips, or semiconductors. At the heart of this supply chain, you find our holdings NVIDIA, TSMC, ASML. As a threesome, they each do something unique and vital.

- NVIDIA designs the best chips for AI
- TSMC makes the chips for companies like NVIDIA
- It does so using ASML's machinery

Next in the AI supply chain is infrastructure. Companies using chips to create huge AI models. These include cloud providers, network infrastructure, data analytics, and security software. Scottish Mortgage has a range of investments in this phase, including Amazon, Meta, Snowflake, Databricks, and Cloudflare.

Then we have companies incorporating AI into their business model, to grow revenue and improving productivity. In our portfolio, examples include:

- Adyen using AI to detect payment fraud
- Ocado using it to control its robot hives, for food delivery
- And Meituan using AI to personalize recommendations and optimize delivery routes.

Coming back to what we're trying to do for our investors. The long-term returns from Scottish Mortgage have been strong, and driven by a few big winners.

Inevitably, we experience some losses in individual holdings. Recently Northvolt, one of our private companies in the battery industry, has experienced lower than expected demand meaning and has to consolidate its finances and operations.

And Moderna, the biotech company, is experiencing lower revenues in the period between its covid vaccine success, and the future roll out of its newer pipeline, such as RSV and cancer vaccines.

But in both of these cases, the upside could still be profound, so we are engaging with management and monitoring the situation.

However, the maximum you can lose in one company is the original investment, but the returns from the biggest winners can be unbounded. This asymmetry which has been crucial for our good long-term returns

For instance, NVIDIA, which we bought in 2016, has returned 85x our original investment Tesla bought in 2013 has returned 18x, and ASML and Ferrari have returned 10x.

So what about extreme returns from here?

It comes back to my opening remarks, about structural changes in the economy - AI, energy, health, logistics, digitisation. We believe our holdings are driving this sort of valuable change.

So notwithstanding near-term macro volatility, we are excited about the potential of Scottish Mortgage to deliver extreme long-term returns.

Thanks for listening.

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

2020	2021	2022	2023	2024
97.8	44.5	-45.0	-13.9	25.6

Source: Morningstar, share price, total return, sterling.
Past performance is not a guide to future returns.

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