Baillie Gifford

Long Term Global Growth Q1 investment update

April 2024

Investment manager John MacDougall and investment specialist Stewart Hogg give an update on the Long Term Global Growth Strategy covering Q1 2024.

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Stewart Hogg (SH): Welcome to the Long Term Global Growth quarterly update for Q1 2024. My name is Stewart Hogg, a client director in the team. And today I have John MacDougall with me, decision maker and portfolio manager. Welcome John.

John MacDougall (JM): Hi Stewart.

SH: Now, as a reminder, Long Term Global Growth is a concentrated portfolio of high growth companies that embraces the asymmetry of equity returns over the very long term.

Now, moving to performance, John, the US chip company NVIDIA has been the standout performer over the last year. And a lot of that performance has continued into the first quarter of 2024. There's clearly been a lot of excitement around those chips being used in artificial intelligence applications.

So, one question I had was, how are you thinking about that current company in terms of portfolio positioning and its future opportunities? But before we do that, could you explain the background to NVIDIA and what first attracted us to the business a number of years ago?

JM: Yeah, sure. Well, we were actually recently just looking back through our internal research library of the progression of our thinking over this business, because I think it's sometimes quite interesting to do that. So, our interest within the LTGG strategy really started picking up over the course of 2015, resulting in the first 10Q report that we wrote on the business in early 2016. And looking back on the discussion minutes from that period, it's quite interesting to reflect on our initial five-times upside case as to why NVIDIA could be an outlier business, really was based around potential within the virtual reality and augmented reality space, which seemed a very natural adjacency for the business, given its historic strong position within high-end gaming graphics processing.

But over the course of the discussion within the team, it became clear that that was just one of many potential shots on goal that NVIDIA had. So, we went back and sort of challenged ourselves again to come up with an even more sunny blue sky thinking upside case, to really see what type of outlier returns might be possible. And when we started to incorporate some revenues over the long run, from perhaps autonomous driving or the deep learning artificial intelligence space, which was really quite nascent at that stage, you could really start to come up with some very big numbers.

So, I think back at that stage, there was the potential at least for a 25-times return, bringing market cap up towards the $500 billion-ish mark. And obviously, sitting where we are today with a $2 trillion-plus market cap, even our most optimistic outcomes have been exceeded since then.

I think there's probably a couple of important learnings that we can take from that. One would be even with our creative imaginative focus and optimistic upside exploration. Even for us, sometimes we fail to fully capture all the potential positive outcomes for a particular business. And also, I think it's important to remind us not to get overly fixated on absolute accuracy. I don't think we ever try to pretend that our five-times upside cases will be absolutely perfect down to the nth degree. It's about being broadly right, exploring the different scenarios as to how you can make a lot of money. And crucially as well, becoming comfortable that a company has the right internal culture to allow these opportunities when they come along to really be acted upon and taken advantage of. And I think that's something that NVIDIA has clearly been fantastic at over the years.

SH: So it shows you just how important that pillar of our philosophy of being optimistic really is. So, to reiterate that point, our blue-sky sunny case was $500 billion and that was out by a factor of four. Just shows you the progress that can happen, so far anyway.

Moving on to how we're thinking about NVIDIA within the portfolio right now, after the recent share price ascent of the past year.

JM: Yeah. So, we've taken a little bit of money out when the position hit the sort of 10 percent stock limit that we have within the strategy. But more recently, we've been more proactive in actually taking a little bit of money out of that name. Reason being, I guess, when you look over the shorter run, the next year or so, it's harder for us to justify our view as differentiated as it is from the market as it might have been a few years back. So, we thought it was prudent to recycle some money from that into newer ideas. But we still absolutely want to maintain it as a decent sized position.

Going back to my previous answer about continuing to think creatively and imaginatively about where the business could be. One thing that we've always admired is the CEO Jensen Huang's amazing ability to focus his research and development efforts on the real long term. He talks about unearthing the next zero-billion-dollar markets, which are markets that don't exist yet, but that he can see as being really significant opportunities for their technology over the long run.

And when you think about all the different areas that intelligence is starting to permeate into, I think we should give him credit for that. And thinking five, 10 years forward, you can see how NVIDIA could be selling a lot more of these chips.

SH: I think that statistic on underestimating where a part of the business could ultimately get to. I remember seeing that the deep learning opportunity in the data center was about zero billion dollars in revenue back in 2016, and it's now nearly 20 billion dollars every quarter at the moment. So, it just shows you what is possible.

Well, maybe moving on, you talked about some of the reductions we've been making at NVIDIA. I know there's been a little bit more of portfolio activity, specifically in the Chinese names. Do you want to maybe talk on those?

JM: Sure. So, Mark and Linda were on a trip to China earlier in the year and met with quite a few of our holdings and the founders of several of those businesses. And as you say, we have made some alterations on the back of that to the portfolio.

So, two that we've decided to move on from would be Alibaba and NIO. In both cases, I guess over the last few years, we've been increasingly concerned about some of the competitive dynamics for both those companies. In NIO's case, we really thought the focus on the higher end of the EV market in China was an attractive strategic feature of that company that would allow them to remain away from the really competitive more mid and mass market area. But the company has really decided to persevere and launch a new sub-brand into that much more competitive area of the market, which we worry about the implications for that, for the company's returns in the long run.

But it's not like we've decided carte blanche to sell down all our Chinese names. We've actually recycled some of that money into Meituan, which was one of the companies that the guys saw on their trip again most recently. We think the story is quite different there, in that their market for local delivery and newer markets, including grocery delivery, are really still at a relatively early stage of penetration. And for all, some market participants that worry occasionally about ByteDance entering into some of those markets. We really think Meituan's competitive position is really quite solid thanks to this network of drivers in local neighbourhoods. So, we've actually decided to increase the weighting within that name.

SH: Okay. Thanks, John. So you mentioned a couple of sales there of Chinese names. I know we've added a number of new holdings to the portfolio this quarter. Maybe give us a summary of those newer ideas.

JM: Yeah. So, on paper, when you look at four new buys in the first quarter, it's pretty unusual for LTGG, that level of activity. But I think it's important to put it in the context of the four new names that have been purchased were names that various members of the team have been working on over the last year or so, getting to know the businesses better, spending even longer with the founders of these businesses to help us get over the line. So it's not some sudden immediate surge within the first quarter.

And just very briefly, to give you a feel for some of the different areas that those new purchases have been made in, one of the names is Nu Holdings or Nu Bank as it used to be known, the Brazilian digital bank. We think this is a really fascinating company that from their core within Brazil, they've been able to secure over half the population of Brazil as customers already. And the majority of those customers, which is really unusual for a digital bank, are actually choosing to use their service as their main current account, their main transacting bank, which is very different to any of the fintechs elsewhere in the world who've really struggled to overcome that hurdle of trust. So we think Nu Holdings are really doing something quite special in that regard.

Some of the other new purchases, Rivian, the American electric vehicle company focused on the pickup truck market. This is a business we got to know over the last several years, really quite admired the founder. I guess looking back on our early days in Tesla, there's some similarities there in that they've had issues really scaling up the manufacturing as they've tried to build their vertical integration themselves, which we think makes sense in the long run. But they have had tough times, but we think they're really starting to get through that. And over the next few years, as we've got new models launches coming, we can see a really nice profit outlook for that business.

And then another business, a new holding, is Moncler. The luxury goods business really focused on winter, extremely warm down jackets. From that core position, the company has really established a really, really strong brand. We think various people have tried to come in and dislodge them from that core and have struggled. We think it's still relatively in the early days of expansion when you look at its revenue scale overall. So, we can see with a bit of geographic expansion, some store footprint expansion, sensible expansion of their lines, revenue lines away from just the core. Plus, as with all these luxury goods companies, very gentle, careful increasing of average selling prices over time. Through those different factors, we again can see a really nice long-term compounding story for a business like that. So that's another new one.

SH: So, thanks for that. And I know there's just one more that you maybe want to touch on. You've been doing quite a bit of work on it. I think it probably goes back to your days in the Japanese equity team, where there was a number of robotics companies that you were interested in back then. Could you talk a little bit about the final new purchase for the portfolio?

JM: Yes. So the last new purchase is a US company called Symbotic, which is actually short for 'Symphony of Robotics'. So that's where the name comes from. So, the problem that this business is trying to solve is initially focused on the slightly older retailers, more traditional retailers, bricks and mortar stores within the US market. Now, these companies have been facing competitive pressures over the last decade and are looking for ways to become more efficient. Now, the warehouse network for these companies to deliver to their stores is one of the most obvious areas in that the vast majority of US warehousing is still very, very manually done. And we're seeing at the moment most of these warehouses struggling with rising wages, shortage of workers, even workers that join up tend to decide it's not really that fulfilling a role and leave three-to-six months down the line. So, these companies are really, really desperate for a more automated solution inside these existing warehouses.

Now, Symbotic had developed a complete system to automate the whole process. That includes robots that move around within the warehouse. It includes the software system, which carefully plans the routes for these robots. So, you can now have a delivery into the warehouse taken from that initial stage, stored, and then retrieved when a local store places an order and it needs a top-up of particular products. And such is the demand for their service that with only a handful of salespeople, Symbotic has already got a backlog of tens-of-billions of dollars of potential new revenues from big retailers such as Walmart. So, we think that's really quite an exciting development within that space. So keen to see how that progresses.

SH: Thanks, John. Well, it'll be good to see how those develop in the coming years. So in summary, John to begin with talked about how we're thinking about NVIDIA and its long-term opportunity, specifically its weighting within the portfolio. We then went on to discuss some of the recent sales specifically in the Chinese equity space, but also highlighted how we're still adding to Chinese equity holdings as well. And then finished off with a flurry of new purchases that we've added to the portfolio, which could be the future outliers of tomorrow. So, I'd like to thank John for his comments today. And thank you, everyone else, for listening.

Calton Square, 1 Greenside Row, Edinburgh EH1 3AN
Telephone +44 (0)131 275 2000 / bailliegifford.com

Long Term Global Growth

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

	2020	2021	2022	2023	2024
Long Term Global Growth Composite	10.7	104.4	-18.1	-18.1	26.2
MSCI ACWI Index	-10.8	55.3	7.7	-7.0	23.8

Annualised returns to 31 March 2024 (net%)

	1 year	5 years	10 years
Long Term Global Growth Composite	26.2	13.9	14.7
MSCI ACWI Index	23.8	11.5	9.2

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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Calton Square, 1 Greenside Row, Edinburgh EH1 3AN
Telephone +44 (0)131 275 2000 / bailliegifford.com