Baillie Gifford

International All Cap Q2 investment update

July 2024

Investment manager Iain Campbell and investment specialist Richard Gall give an update on the ACWI ex US All Cap, EAFE Plus All Cap and Developed EAFE All Cap strategies covering Q2 2024.

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Richard Gall (RG): Hello and welcome everyone to the 2024 second quarterly update on Baillie Gifford's International All Cap strategy. My name is Richard Gall, I'm an investment specialist on the strategy and I'm joined by Iain Campbell who is chair of the Portfolio Construction Group. As a very quick reminder, International All Cap is Baillie Gifford's longest international equity strategy. It's been running for about three decades now and like most of our strategies it's bottom-up, it's long-term, it's active and it's growth in its remit.

So turning to the most recent quarter Iain, I guess overall it was a relatively quiet affair, but what would you pull out as the highlights or indeed the lowlights of it?

Iain Campbell (IC): Yes, well, as usual, the drivers of performance were quite varied. The semiconductor theme, as with the first quarter, was an important driver of the top performers in the second quarter. So ASML, the Dutch lithography business, had a very strong quarter in operational and share price terms. TSMC, which we hold for those clients who allow us to hold emerging market stocks, also had a very good operational and share price performance in the quarter. And that was all driven by the ongoing buzz around AI and semiconductors, for which NVIDIA in the US is the poster child.

Beyond those names, it was largely driven by stock specifics. So, we saw very good share price performance at Hargreaves Lansdown, which is the UK-based online wealth management platform. It was the subject of a takeover bid and its share price responded positively to that. We also saw a positive share price performance at Recruit, which is a Japanese company. It owns Indeed, which is the online jobs board which operates globally, and they issued a positive update for their full year numbers around better-than-expected monetisation of their platform. And that was encouraging to see a business that in a tougher economic and jobs market climate is managing to drive growth through its own efforts.

At the other end of the ledger, we saw weaker performance from a few of our more rapidly growing names. So Adyen, which is a payments company, Wise, which is a money transfer business, and Sartorius, which is a lab products business, all issued slightly disappointing guidance. And as the share prices have been strong in the months running up to this, they saw quite a lot of weakness in this most recent quarter.

RG: Great. Thanks for that, Ian. Now, you're quite recently back from an investment trip to Japan, and I appreciate this is quite a well-trodden path for you, having worked in that area for a long time. But it'd be great to hear any reflections you've come back with.

IC: I suppose the biggest, most noticeable feature was the weakness of the currency. I mean, just to put some numbers around it, in 2021 the yen to the dollar rate was 115. Last week, it was 160. And, you know, operating in Japan, going to restaurants, it really is notable how good value that country now is. And we're seeing that in tourist flows. And I was seeing it as I went around train stations and the centre of big Japanese cities. There's a lot of tourists there. And that's great after what had been really some pretty quiet years immediately after Covid. And we're seeing it in the stats as well. So, in March, Japan saw 3 million, or over 3 million, tourists arrive, and that takes them back up above the pre-Covid level. So that's really encouraging and should be good for some of our consumer-related cosmetics stocks in Japan.

The Japanese currency is also providing a real boost to Japanese exporters and, combined with a trend for corporate governance improvements, that's really been creating a supportive environment for the Japanese market. Now at the moment the companies and the share prices that are benefiting the most are those at the value end of the market, those with the most scope for improvement. So, our holdings in high-quality growth businesses have been slightly left behind, but the overall environment in Japan is supportive. Now as usual, my trips are a combination of checking in with management at existing holdings, and prospecting for new ideas.

And I'd maybe call out a couple of interesting areas. The first would be around semiconductors, which, as I mentioned, is an area of a lot of dynamism at the moment. Japan has a reputation for expertise in precision manufacturing, for consistent reinvestment in R&D. And therefore, I think it's not surprising that this cluster of semiconductor production equipment companies has grown up. Now, the one that's in the portfolio is Tokyo Electron, which is a world leader in etch and deposition. Other ones that we've looked at would be companies like Advantest or Lasertec in inspection or Shin-Etsu in silicon wafers. So, it's an area where there's a lot of interest, there's a lot going on, but it's also critically for us an area where I think the strong gets stronger. You build on your prior year's R&D, it's about reinvesting and incrementally getting better. And I think that means that these strong Japanese businesses are going from strength to strength. The only concern, from my point of view, is valuation. It's not the business fundamentals. So that was one area of encouraging developments.

The other is an area where we've had a bit more of a troubled time in recent years. So, a number of manufacturers in Japan and across the world have really struggled with this post-Covid period of opening up. Now, Covid was obviously a strange time, when demand for some goods increased dramatically, but also transportation – friction in supply chains increased and availability of components and raw materials became a problem. And for a lot of manufacturing companies, their reaction was to stockpile inventories of finished goods, components, and their customers were doing the same. They were stockpiling the products. And it meant that when we came to the end of Covid, and reopening happened and demand normalised, there were these huge inventories throughout the supply chain. And for these manufacturing businesses, clearing those inventories has been a headwind to growth. Now, I visited one company, Shimano, and I think there were really encouraging signs that those inventories are now clearing. Capacity utilisation is improving back to more normal levels, and cash flows and profitability are recovering. So that was encouraging, in an area where we've had a number of more troubled holdings, that this inventory issue seems now to be resolving itself.

RG: Great. That sounds like a useful trip overall. Thanks for sharing. Turning to trading in the portfolio, there has been a slight uptick in that. What would you highlight in terms of the notable new buys and sells?

IC: Yes, well, it's always encouraging to see a flow of new ideas. A few new ones I would just want to talk through quickly. The first would be Greggs, which is a UK-based food takeaway business. It's one we've watched and admired for some years. We think it has a fairly unique advantage based around scale in manufacture and distribution. We also think that it can carry on growing in its addressable market for many years, just by rolling out new stores. And we think it's attractively valued at the moment. So that was one that we added to the portfolio.

A second would be Bunzl which is a B2B outsourcing business. They mainly deliver consumables to businesses. Growth here is different. Growth here is more driven by bolt-on acquisitions, but they have a track record of doing those very effectively. And we think there's scope, given the markets they're in, for them to carry on running that playbook for many more years. And then the third one, the final one I would highlight, is Assa Abloy, which is a Swedish industrial. And you'll know that we've found many attractive companies in that Swedish industrial complex over the years. They tend to be very well-managed businesses. Assa Abloy is a leader in door locks and entry systems. And we think there's a strong edge there because of particular local regulations and preferences

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around how these systems work. So we think it has a strong edge. And growth there is going to be a combination of organic growth from new markets, technology, but also bolt-on acquisitions.

In terms of funding, the one I would highlight would be Cochlear, which has been in the portfolio for a long time. It's an Australian hearing implants business, very well managed, a great business. But for valuation reasons, we've now chosen to move on. There were a number of other transactions also during the quarter, and the full details, of course, are in the quarterly report. But overall, I think it's really encouraging to see that flow of new ideas come and challenge for a place in the portfolio.

RG: Great. Well, that feels like a very positive place to end. So, Ian, thank you very much for joining us and thank you all for listening today.

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International All Cap (including ACWI ex US All Cap, EAFE Plus All Cap and Developed EAFE All Cap strategies)

Annual past performance to 30 June each year (net%)

	2020	2021	2022	2023	2024
ACWI ex US All Cap Composite	12.1	41.3	-36.4	14.0	2.8
MSCI ACWI ex US Index	-4.4	36.3	-19.0	13.3	12.2
EAFE Plus All Cap Composite	8.1	37.1	-35.1	16.1	1.7
Developed EAFE All Cap Composite	9.0	36.8	-35.0	17.0	0.4
MSCI EAFE Index	-4.7	32.9	-17.3	19.4	12.1

Annualised returns to 30 June 2024 (net%)

	1 year	5 years	10 years
ACWI ex US All Cap Composite	2.8	3.4	3.9
MSCI ACWI ex US Index	12.2	6.1	4.3
EAFE Plus All Cap Composite	1.7	2.6	3.4
Developed EAFE All Cap Composite	0.4	2.6	3.4
MSCI EAFE Index	12.1	7.0	4.8

The International All Cap Strategy comprises three distinct variants. Overall, the variants are broadly similar, with the key difference being the degree of exposure to emerging markets listed holdings.

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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