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International All Cap: inflection points

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Join portfolio manager Joe Faraday, investment specialist Katie Muir and host Chris Huckle as they provide an update on the strategy's performance, portfolio activity and why they are upbeat about the prospect for long-term returns.

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

Chris Huckle (CH): Good morning, and thanks very much to all of you for dialling in. We really appreciate your time, your attention and your interest in the International All Cap strategy, and the theme of today's session is inflection points.

Just to start with some introductions, my name is Chris Huckle, and I work in the Clients department at Baillie Gifford. And in a moment, I'll be joined by two colleagues, Joe Faraday, Joe is a decision-maker in the International All Cap Portfolio Construction Group here, and Katie Muir. Katie is one of Joe's colleagues, an investment specialist. And they'll both be covering performance, that's both investment performance and operational performance, touching on transactions, talking about the team, little update on the team, and then some of the areas where they're seeing exciting potential for growth.

And we'll try and keep the whole session to no more than 45 minutes. We'll allow time for some questions within that, so probably 30 minutes for the webinar itself, and then 15 minutes or so for questions at the end. And please, do feel free to submit as many questions as you like, using the chat facility on the screen in front of you.

So, just one further point before I hand over to Joe. All the portfolios are very, very similar, but there are one or two differences between them, and perhaps most obviously, in relation to emerging markets. So, you might hear us mention one or two stocks that aren't in your particular portfolio, but please, don't be surprised about that because the majority of them are very, very much the same. So, with that, I'll hand over to Joe, and we'll come back for questions a little bit later on.

Joe Faraday (JF): Thank you, Chris, and good day, everyone. It's great to be speaking with you all. So, as Chris mentioned, I'm going to talk about investment performance, and then what I think, perhaps, is as, if not potentially more, important operational progress that we're seeing across the portfolio at large, the individual holdings. So, if we step back to start with and think about the last year, 2023, arguably, there was a lot of uncertainty, and there was a lot of headwinds on the macro front. We had that period where inflation has, and continues to, persist.

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There was rate hikes, and that abated towards the end of the year in that shift from peak towards when cuts are being priced in, or how and when that still will pan out. Good levels of unemployment, which arguably, is quite a good sign for many economies around the world. Geopolitical tensions, which continue to expand or change quite strikingly. And I think it's almost fair to say that that persisted for a lot of the year. And it's almost really fair to say also that there's been no real change on that so far this year.

I think, also what is quite interesting if you look across markets, just how differently they behaved over the last year. So, this is generalising a lot, but it felt as if the US market, so not international, but the US, was about the Big 7, or quite simply, artificial intelligence and Nvidia. In international, it felt it was quite a narrow market or, across international things, behaving quite differently. So, Japan was really about the deep value rally and the promise of long-awaited signs of economic progress coming through there.

Europe felt very much about quality. Narrowed it down to a few specific stocks, or you could almost term it as just being the Novo Nordisk market. It felt like that at certain times. A real need to be selective. It actually felt as if top-line growth was quite weak in Europe, but profitability or margins were quite strong, so it was really important to be navigating through that.

And then, lastly, got on the submerging markets, whether that's direct or indirect exposure, some of the more cyclical and tech-focused businesses doing well, so semiconductors, ecommerce platforms and quite striking differences in behaviours across end countries within emerging markets. So, again, direct or indirect exposure into China being a big headwind, and then the tailwinds, or quite promising growth being seen in India, Mexico, Brazil and the like.

So, if I turn that over then and get into the portfolio a little bit, if I try and generalise about 2023, what we would highlight is, there were strong absolute returns, but at the same time, markets were generally really strong across international equities and from the US as well, quite notably. And that led to a period of relative underperformance, and we're very conscious that's been a continuation for some time now.

If I focus in on the last year, I'd cite three main factors behind the degree of underperformance that was seen. The first of those, and I think it's the main one, is Japan. That was a really tough market for us to be navigating through. I touched on the strong performance of value more focused stocks. There was areas within that we have low to no real exposure to. So, financials, cyclicals, the holding companies, they did very notably well.

At the same time, some of the holdings were quite weak. So, some of the exporters, the industrial champions that sell a lot into China, seeing soft demand and strong competition in that market. And a similar backdrop for some of the consumer-focused companies as well.

And another general comment on Japan would be that we didn't see the uplift from governance improvements that you saw at quite a lot of companies, or that potential for change, given the already very high levels of standards that we see across the holdings that there are in the portfolio. So, that was the main notable headwind for the last full calendar year. The two others I would call out would be China, and again, that's direct or indirect exposure. A couple of examples there would be the Asian-focused insurers and also the luxury goods companies.

And then a last comment would be a lack of exposure to certain financials, so banks, which benefitted last year. So, those would be some of the headwinds that were faced over the whole of the last year.

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Now let's turn to the fourth quarter. Performance improved quite markedly, so it's a real welcome sign. And I think what's really important is operational performance showing through across lots of individual holdings and that being very promising and that getting rewarded. I think that's to be celebrated or really needs to be called out. It's what we're really all about, ultimately.

Some of the positive return contributors I would cite would be a number of the online disruptive businesses, so Spotify music streaming, and then where held Mercado Libre, the Latin American ecommerce business, Shopify, the Canadian ecommerce facilitator. A number of the technology holdings, some of the semiconductor businesses, so ASML's a good example there, the lithography business. Nemetschek, which is the Autodesk equivalent in Europe behind computer-aided design for building and construction.

Then you could cite some of the industrial companies, Atlas Copco, one of our longest-standing holdings, with its strong presence in compressors and vacuum technologies, and IMCD in speciality chemicals. And perhaps it would be remis to miss it off actually, but some of the Japanese names did quite well in the latter parts of the year. Recruit that does recruitment, and SMC that does pneumatic equipment. And those saw reasonably good operational performance, but also buybacks kicking in, so capital allocation improvements coming in, in those.

So, lots of positives, and a lot of different company types performing well operationally and that showing through, in terms of performance. There were some smaller headwinds in the fourth quarter. China direct and indirect exposure. Lonza, which is a fairly recent purchase from a couple of years ago now, the outsourcer for pharmaceuticals and biotech, saw quite soft demand. It's going through a management change, but that's one we've been doing a lot of work on testing the resilience, the quality of that company. Iain and Stephen were out, spending time with Management, the interim CEO, the Chair, so we've done a lot of testing of the conviction behind that business.

And then a few holdings that we monitor on an ongoing basis, we felt there were sort of slightly softer growth from the likes of United Overseas Banks, DSV in logistics and Xero. But more broadly, it was a tough spell, the last full calendar year, but the fourth quarter certainly gave us a lot of grounds for optimism or to be upbeat about what we're seeing across the holdings.

So, that's on investment performance and returns. I now want to segue onto operational performance, and I think there's three key callouts here. We're seeing really strong top-line growth. We're seeing really strong pricing power and margins and encouraging capital deployment, companies investing for the years/decades to come. We assess and we monitor these at our weekly portfolio monitoring meeting as investors from all of the analysts that surround us on the different regional teams across the floor and our ongoing work, meeting and interacting with management teams.

And if we generalise, about a quarter of the portfolio is tracking well ahead of our expectations, about a half are in line, and a quarter we're scrutinising or monitoring. They might be falling a little bit short on a short-term basis, and it's important we test our resolve. But just to walk through a few different examples, an eclectic mix of names across the portfolio, but strong top-line growth from the discount food retailer, Jeronimo Martins. Seen double-digit growth across Poland, Portugal, Colombia. It's great to see from that discounter.

Spotify, I mentioned earlier, it's now up to 600 million users. One in ten people around the world are using Spotify. It's pretty formidable, and it's pivoting towards more profitable growth, and scale advantages are really kicking in there.

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And another example would be Exor, the holding company behind Ferrari. Now half of the demand is electric or hybrid, and we're seeing really strong demand and order growth there. So, strong top-line growth examples. Those are just a few from across the portfolio.

Pricing power across lots of different consumer goods and service types, so paint with Nippon Paint, which has got really strong brands across a number of Asian countries. In auto classify, it's the Auto Trader, the dominant platform in the UK for anything to do with used car sales, and then in credit checking, Experian just eking out pricing strongly there in the UK, US and Brazil where it has its key presence.

And the last operational factor would be investing for future growth, so it's about high sustainable growth rates, high levels of R&D. And there's longstanding holding in the likes of TSMC, seeing $30bn-plus of annual capex, Reliance $10bn-plus of annual capex. But I'll bring Katie in, in a second, talking about a couple of newer holdings. There's Ryanair, the airlines low-cost carrier, and BHP abroad, a multinational, but deploying lots of capital in copper. So, some of the newer names being in that capital deployer type of business. So, it's good seeing companies investing for the future growth as well.

So, I'll try and pull this all together. Ultimately, our job is to manage a portfolio, on your behalf, of this eclectic mix of world-leading businesses. They happen to be international. We're seeing strong operational growth, and we're trying to balance that with the appropriate amounts of quality and resilience. And we're optimistic about what we're seeing when we think through what we're seeing and hearing from companies and how are they delivering on, ultimately, earnings and free cashflow-per-share growth.

So, with that, I'm going to hand over to Katie to walk you through what we've actually been up to with the portfolio.

Katie Muir (KM): Great. Thanks, Joe, and good morning, everyone. From a research perspective, the pace of idea generation remains strong. Lots of new ideas vying for space in the portfolio, which is great to see. There's also been lots of company meetings, around 1,000 in the most recent quarter across BG, almost 4,500 in the last year, all of 2023. And the team have also been out on the road. Joe mentioned, Iain and Stephen were in Switzerland, seeing Lonza, as well as some new ideas. That was in November.

Joe was in India with some of our EM investors, Sophie was back in China again, and Milena has had her usual cadence of full-day due diligence meetings with UK holdings, something a little bit different that they do within the UK Equity team. And the team are keen to keep the portfolio evolving, make sure they're refreshing the growth ideas and opportunities and have been continuing to latch on to new growth types.

So, new purchases, Joe touched on two of them briefly there, in the past quarter, include Ryanair and BHP. And where portfolios have exposure to emerging markets, we also bought the Mexican conglomerate FEMSA. So, just to touch on them quickly, Ryanair, Europe's leading low-cost airline. The business was originally modelled on Southwest Air, which you'll be very familiar with. However, the European market for air travel is actually quite different to that of the US market.

We think Ryanair can go from 20 to 30 per cent market share in Europe. Last year, it carried around 200 million passengers. It's aiming to grow that to 300 million over the next ten years, and to do that, it's investing heavily in its fleet. So, 400 aircraft on order with Boeing, as Joe mentioned, and it has one of the largest and newest fleets of 737s out there. So, newer aircraft can carry more passengers, more fuel efficient, so less carbon emissions, and are less noisy as well.

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So, we think it's a really high-quality operator with a rock-solid net cash balance sheet, and that allows it to continue to invest through cycles.

And then, finally, from a management perspective, there's a very driven Management team led by Michael O'Leary, and they have a top-down, low-cost culture, which really permeates everything they do. So, we think combination of that being the lowest-cost operator, combined with their balance sheet strengths, really provides a strong competitive edge, which will allow Ryanair to be a long-term winner.

So, the second new purchase is BHP, the Australian-listed global mining group. It's got a great track record of capital allocation and its production practices, as well as access to low-cost resources around the world. But part of the reason for taking a holding now, as Joe touched on, is that it has shifted its business mix towards copper, particularly with the recent purchase of OZ Minerals, which is another business we've discussed.

We've done a lot of work on copper as a team over the last year or two, and particularly its role in the energy transition, and we believe the supply/demand dynamics will mean there is a long-term outlook, which is favourable for both copper demand and pricing. It's a business we also know well. We've owned it in the past in International All Cap, and it's one we're returning to, so there's a lot of institutional memory with this company.

And finally, for portfolios with EM exposure, we also bought FEMSA. We've been exploring and discussing a number of ideas in Latin America. FEMSA's core businesses are in retail and beverages. So, in retail, it operates OXXO convenience stores, and it's considered to be a world-class operator and taking market share. It's got 23,000, roughly, stores across Mexico, looking to grow. They think they can grow that to about 30,000 over the next decade and also expand into Brazil. So, we think there's a long growth runway there.

It also has a Coke bottling business in Mexico, which is a smaller part. It's still a decent business, and that generates lots of free cashflow, which it's using to reinvest in other growth opportunities. And we've been impressed by Management's strategic focus. It's been divesting and restructuring bits of the business over the years and using that free cash to really reinvest in where it thinks the growth's going to be. And we believe that valuation provides good upside potential. So, three new purchases, all very different, and I think, a good example of lots of new and interesting ideas that the team have been discussing recently.

Moving on to the sales, we sold five holdings in the most recent quarter, Farfetch, Ubisoft and Nidec, which are shown on the slide, plus Denso and AUTO1. So, maybe just to touch on our sell discipline for a second before we talk through those, so our sell discipline is based on weighing up whole investment case and its relative attractiveness, compared to other holdings and opportunities that the team are seeing. This is something we wrote about in the most recent quarterly letter.

And when we look back at why we've sold over the last decade, around half of the time, it's really down to growth, and sometimes the competitive landscape and how that impacts growth, a quarter of the time, down to management or governance, and a quarter of the time, on valuations grounds. So, the reasons for selling really mirror or map the same things we look at when we buy.

The first two sales were really down to us losing faith in management. So, global luxury platform and marketplace, Farfetch, that was sold in early October. Milena had spent a full day in London in September with the Senior Management team of Farfetch, and really, the conclusion was that the business has become unnecessarily complex since we first invested, and the bar for successful execution has become much higher.

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So, really it's about a loss of faith in Management's ability to execute on the growth opportunity.

For Ubisoft, which is a French-listed videogame developer, we've been speaking to the company for some time about governance matters. We pushed for more board independence there, but also, Management's execution has been disappointing, so that was the reason for the sale there. The other three sales are all loosely linked, in that they're all part of the automotive value chain, although the decision to sell was based on our bottom-up fundamental analysis.

This includes two Japanese businesses, one, the first is Nidec, which makes electric motors. And really, the decision there was down to operational disappointments. Our original investment thesis was based on the growth potential from supplying traction motors for electric vehicles, and while they've made some progress there, it really just hasn't played out as we'd hoped. The other Japanese business was Denso, which has been held in the strategy for close to nine years.

The shares performed. It was actually one of our Japanese holdings that performed quite well in 2023 with the recovery in vehicle production, and was also boosted by a weak yen in particular. So, the sale here was really down to the growth outlook from here and our assessment of that, relative to the valuation it was now on.

And finally, on the consumer auto distribution side, we sold AUTO1, which is the online marketplace for used cars in Continental Europe. The business had made decent operational progress, but we revised our growth expectations and the potential addressable market that we thought it might have. And, based on that revised opportunity, we decided to sell the position. So, with all of these sales, there's robust challenge to each individual case from across the Investment team, and a long pipeline of new ideas vying for a place in the portfolio, which is really encouraging to see.

If we, maybe, turn to the next slide, Chris, please. This slide, we call our Growth Waves slide, which many of you may recognise from previous webinars. We've updated this to the end of last year. So, if we step back and look at the shape of the portfolio and how it has evolved since the strategy inception in the late 80s, the line at the top of the chart indicates some of the key market events that the strategy has lived through, through time. And the circles below are some of the portfolio trends that we've seen through the years.

The different-coloured waves in the chart on this slide show the strategy sector exposures and how those have ebbed and flowed over the past three decades or so, and the circles on the waves show the top ten holdings in the portfolio at different points of time in its history. So, those holdings and sector exposures have clearly not been the result of deliberate top-down repositioning of the portfolio, but instead, from applying our consistent philosophy and bottom-up process. And also being open-minded to where growth may come from, so when looking for the best growth companies in international markets.

And some of those businesses might be businesses that we've held previously and sold for various reasons, that we know well and have come back to. BHP is a good example of that more recently where we see a new growth opportunity or a new [wave] in front of it with its repositioning and exposure to copper. What's also interesting is the different types of businesses held in the portfolio within those sectors and that we've found over the years in the hunt for growth.

If we look at the industrials wave, which is roughly the fourth one down, if you're looking on the right, in the pale green, you can see this exposure has steadily increased over time and is an area where the portfolio has a diverse range of businesses within that. And we're continuing to seek out new opportunities. We were discussing just a few of those this morning.

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And then, when you look at our healthcare exposure, ten years ago, the portfolio had a greater exposure to some of the large, patented pharma companies like Roche. Whereas today, we own a mix of medical devices companies, such Cochlear, clinical diagnostics and testing businesses, such as Sysmex, plus the more picks-and-shovels-type businesses that are key suppliers to the pharma/biotech industry and are benefitting from the growth in R&D spending and drug development, but without the drug discovery risk. So, examples here are companies such as Lonza, which Joe mentioned earlier, and equipment supplier, Sartorius.

And then finally, if we look at financials, which is the first blue wave on the page, or the biggest blue wave, which is actually an area where we have lower exposure, compared to international market benchmarks. If you look at the businesses we invest in today, our financial businesses contain those skewed to the rise of the middle class in Asia, traditional banks, such as United Overseas Bank in Singapore, HDFC in India, for those that have EM exposure, and life and health insurance providers such as AIA, as well as the recent purchase of Hong Kong Exchange.

And then, if you look at developed markets, in terms of financial holdings, we've got a number of fintech businesses that are disrupting large markets, such as payments, savings and investments. So, a really diverse or eclectic mix of businesses just within that sector. But at the portfolio level, the key, as Joe said, is to have a balance of growth, quality and resilience, and our aim is to invest in a flat portfolio of the best ideas we can find in international markets with exposure to a broad church of both types. I'll now hand back over to Joe, who's going to provide an update on the team.

JF: Thank you, Katie. So, I think it's a key message to share, that we are adding resource to the strategy, and there are three components to this. We're expanding the Portfolio Construction Group from five to six, so an opportunity arose with Sophie focusing more of her efforts on China, with establishing an Edinburgh desk that concentrates on China, that we could bring in someone else from emerging markets. And we spent some considered time working with Will Sutcliffe, the head, [of] that team. Amy Atack, the chief [of] investment staff.

And last summer, we decided we'd like to bring Alex Summers through onto the team. We've worked very closely with him since last September, bringing him along to the various meetings. He focuses very much on quality growth, so alongside being focused on emerging markets, that's another helpful investment behavioural trait we cherish, or we're trying to bring more of into the group. And Alex will formally join, effective 1 March, so in a few weeks' time.

I will add and emphasise that, clearly, that's really important for the ACWI ex US, and EAFE Plus variant where there's direct EM exposure, but also for the developed variant where, give or take, 30/35 per cent of the portfolio is exposed to emerging markets. And the trends in those markets, it's really important for us to be latching on, thinking about competition, supply chains. And that's what Alex and Sophie and whoever's been involved with emerging markets on the group or us all more broadly, have felt has been very important for the strategy through the years. So, we're adding Alex to the team.

The second development is also quite key, is that Iain and myself are committing even more time to the strategy. We're setting up a central desk, and we want to try and boost the complementary idea generation, portfolio monitoring, portfolio construction aspects of our work and the administrative side to what needs to be done on the strategy. This is something we have considered though the years for pretty much over a decade. We see it as being a function of where Iain and myself are at in experience levels.

It's listening and considering the feedback that we have received, external and internal. It's a tried and tested path for what we've done with various other Baillie Gifford strategies, and we think it's invaluable trying to get this right balance of

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centralised ownership, accountability, joined-up thinking across the portfolio with, also, the sheer strengths of the regional plugin approach. So, that's the second main development.

The third one that I think is also noteworthy is Stephen's promotion to the partnership, and that will mean there's three Baillie Gifford partners on the strategy. Now, all of this has been done, it's considered in the spirit of trying to improve how we invest on your behalf. We review that annually at our on/off site, our away day in the spring, and explore these plans. It's been based on feedback, as I mentioned, and then also, that's internal. So, we had the likes of our Equity Leadership group, our North American Management group and our chief of investment staff, who have very much helped shape our thinking across the team, and Iain and myself, as to how we would like to go about doing this.

I want to be very crystal clear, though. The process and core beliefs remain exactly the same. We see this as being an enhancement, in terms of adding resource to the team. I'm going to pull that all together with what we've shared today. Deep down, this gives us that even more confidence in our approach and ability with our sheer aim of trying to deliver good performance for you over the long term. So, with that, I'll pass it back over to Chris, and I've no doubt there'll be questions on performance, what we've been up to, and also the team.

CH: Thanks very much, Joe. Thanks, Katie. Yes, we do have time for some questions, and I'll turn straight to the first one that's come in, which is a question that relates to China. And the question is, how are you thinking about what types of European or Japanese companies can still grow into China, for example, Nippon Paint, which is one of the ones we talked about?

JF: I'll start, and I'm sure Katie might want to segue in. So, we've been quite vigilant about the size of exposure there is in China direct in ACWI ex US, so we've been roughly index-like. And to the crux of the question, spending a lot of time thinking about the overall indirect. So, the georev exposure, and that applies all the different model types. And we've been trying to keep deliberately at, or slightly below, index levels. We think there's a lot of opportunity for growth in China. We've been quite concerned about some of the risks.

And what we've been trying to navigate is, basically, the state veil, degrees of regulation that you've seen across large number of business or company types. And we're all familiar with that, the internet platforms, financials, healthcare, what happened to education companies. And we've tried to navigate that as best we can. There's been the occasional one that we have been blind or wrong-sided by. Treasury Wine Estates, a few years ago, is a firm reminder of that, when you wake up overnight, and your high-end Australian wine is no longer going to be sold into China because there's punitive tariffs.

So, things are going to happen. We see our job as trying to best navigate the size or degree of exposure and try to make sure it's the right side of that regulation, or almost quasi-immune from that. And I think it's interesting Nippon Paint gets mentioned there. One would hope that paint is quite agnostic. It's a business or a brand. It shouldn't be called Nippon Paint. It's not really Japanese anymore. It should call this China, or each of its markets' national paint company. And actually, that business has been growing really well. It's double-digit, I think it's 10 per cent plus top-line growth. Far quicker, it's surprised on margins. They've been doing bolt-on deals in lots of interesting markets.

So, I think there are some of these companies out there that are almost quasi-immune and have just been seeing good, gradual, ongoing growth and good operational performance. There will be cycles. There'll be tougher periods, and we're doing what we can to navigate through that.

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The one little additional comment I want to make, and there's been a lot of debate recently on the PCGs around the luxury goods companies, and maybe one example there, we were literally debating this, this morning, is, LVMH will say 10 per cent of sales of China, but it's actually 30 per cent of sales are to the Chinese. So, again, we've got to almost unpick or go through each business type and think really carefully about China. Is it sales? is it cost base? Is it supply chains, or is it Chinese customers more broadly?

So, we have some of these guardrails or rules in place about size of exposure, trying to step back and making sure that companies aren't going to get caught up or wrong-sided by regulation, but they're thinking very carefully about the degree of immunity or what is in the share price for that as well.

CH: Thanks, Joe. And a related question actually, maybe broadening it out slightly, relating to deglobalisation. Lots of discussion about that. What's the views of the PCG on that? And how, if at all, is it going to affect the portfolio?

JF: So, if I step back, we've really challenged ourselves for a good number of years on this now. It's been interesting, some of the names we've been bringing through into the portfolio. So, DSV, the logistics solutions provider, Canadian Pacific, or CPKC, as it's now called, in terms of reshoring, and Mexico doing that much better and excitement around that. Some of the long-established holdings. TSMC seems to be doing a remarkable job of floating above all forms of geopolitics, and it's clear there from capex plans, and where it's expanding facilities.

And so, we've been trying to lean into this, where we see, actually, there's opportunities arriving from companies that can really help and facilitate, or that'll be quasi-immune from this. And I think there's probably quite a lot more to be done here. There's the purchase of Air Liquide in the summer last year, and we think that benefits from decarbonisation, but also reshoring, and I'd say, the door's quite open, or ajar, for seeing capital deployers.

And Katie and I were talking about this, this morning. We feel there's this trend, there's going to be more kit in more places, and that'll be a good, encouraging backdrop for a large number of industrial companies. So, I think, yes, there's this degree of caution and what this can mean for cost pressures, etc., and thinking through that for supply chains of existing holdings or companies. But also trying to see this as a big opportunity for companies that can really help facilitate or benefit, as a result of more deglobalisation or reshoring.

CH: Thanks, Joe. And Katie, maybe one for you, actually, on transactions and turnover. An observation that it seems, maybe there's been a little bit more activity than is usual in the recent quarter. Does that indicate that turnover has started to tick up? Has there been a change there?

KM: That's a fair question. When we look back over the past year, so the whole of 2023, we had 11 new buys, roughly, for the ACWI ex US portfolio. It was nine for the developed EAFE-only variant, and 17 complete sales for ACWI ex US and ten for pure. So, when we look back over the years, it obviously ebbs and flows in different years, but actually, it doesn't look all that different than we've seen in previous years. And when you look at it on an annualised turnover basis, we're right in the midpoint of our expected range, which is the 10 to 20 per cent annual turnover over the long term.

If anything, levels of turnover had probably got a bit low before that. It fell to the high-single-digits level, but I think what's been really encouraging to see is just the breadth of names that had been coming into the portfolio. Clearly, it's been a difficult environment to navigate from a performance perspective, but that's also thrown up quite a lot of compelling opportunities. Name turnover is definitely a little bit higher, ticked up a little bit, but no big trend or change, though.

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And I think the positive thing we take from it is that healthy competition for space in the portfolio. All those ideas coming up through the regional research teams and from the broader investment floor, all those meetings and research that investors are doing.

CH: Great, thanks, Katie. Switching gear a little bit to resource, Joe, you mentioned the forthcoming addition of Alex to the Portfolio Construction Group. You also mentioned, he perhaps has a preference for quality growth. So, what can you tell us about his temperament? What will he bring to the group?

JF: Yes, so I think it's an interesting one. So, full disclosure, Alex was actually down the road for ten years at a firm called Stewart Investors. We hold them in high regard. They have much more a quality-durable growth skew, compared to ourselves, and Alex has been coached or trained up that way, so he does bring this slightly different style, in terms of growth investing. He spends a huge amount of time thinking about management, governance and alignment. That's a key area we think about, but I would argue, Alex even overweights that much more as well. And I think that's going to be quite valuable for us, trying to get the correct balance of growth, quality and resilience across the portfolio.

I think he adds a little bit more to those latter two components, and we're seeing early signs of that, the way he's adding to debate. He's really willing to speak up. He's quite similar to Sophie in that vein, the questioning and the scrutiny, so there's really robust debate already across the PCG. And I think that bodes well for, overall, what he'll add to the debate and the discussion, this temperament for the types of growth he goes after.

And also, what we want to try and draw on from the Emerging Markets team directly for where there are those emerging markets names, or how we think about the emerging market exposure for companies when it's multinationals, industrials, consumer companies that are selling into some of these EM economies, the quality traits that we really need to go after. So, early days, but we have worked with him since last summer. It's going to be great. That's formalised, effective, end of a few weeks, and we're really looking forward to getting him being a core member of the team.

CH: Thanks, and just sticking with the Portfolio Construction Group, when we think about the new central desk, what will be the priorities for you and for Iain, once that starts?

JF: I think of it as three ways. It's complementary idea generation, it's portfolio monitoring, and then it's portfolio construction or the administrative aspects. And what I want to make very, very clear, we're not changing almost any other aspect of our process. So, the portfolio meetings remain exactly the same, where we air all the ideas, and we sit down as a group of five, or now become six. The stock discussion, so we narrow those potential ideas down. The five question [framework] gets done. The stock discussion will be attended, the five now becomes six, and it's a sponsor and seconder, and it's the same vetting process, the same decision-making of what goes into the portfolio.

But you think of that funnel, Iain and I will be almost deliberately able to, perhaps, fast-track a little bit some of the additional research areas that could have perhaps taken that bit longer, the gestation period of them happening across the regional teams. And that bodes well for the agility around idea generation or being a bit nimble around scrutinising some of the existing holdings. But in short, we don't see this being any key change to process or philosophy, but just almost oiling or making that flywheel just flow a little bit more smoothly over the course of time.

CH: Thanks, Joe. Katie, or Joe indeed, you've talked about transactions that have happened recently, but if we look forwards, what opportunities are likely to come up? What new areas of excitement do you think there are going to be?

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KM: Shall I start, Joe, and you can jump in? I think Joe touched on one of the areas recently. We've been spending a lot of time thinking about capital deployers, that reshoring theme, deglobalisation, the energy transition, where there's going to be large amounts of capex spend needed and who's going to be driving that and able to extract value from that. High-quality industrials in that area have been quite a focus, so potentially more there to come. And I think the other aspect, which Joe touched on, and with Alex joining, will really help with this too, is emerging markets and frontier consumption.

There's definitely been periods more recently where it feels like everyone's forgotten about the opportunity there is in emerging markets and, as the middle class develop and rise in incomes there, so people want that little bit more. It's not necessarily just high-end luxury stuff. It's consumer goods, it's financial products, it's lots of other things, so we think there's lots of opportunity there, which you can either play, finding good domestic local champions, potentially, in those markets, or indeed through the larger developed market companies.

JF: Chris, I think the only thing I would add is definitely these almost areas that feel particularly appealing, but if you look back at transactions in the last year, what I'd expect to continue is just that eclectic mix. So, it's like when you look at last quarter, and it's an airline, a miner and convenience store/Coke bottler, you almost can't get as different to that.

So, as long as there's breadth of ideas and it's about idiosyncratic risks, there'll be a clustering around, certainly some of these capital deployers, EM consumption, etc. But it's all about that breadth and lots of different names coming across, different geographies, different sector types.

CH: Well, thanks very much. It'll be interesting to reflect in a year's time or so and see what progress we've made on that front. So, I think we're just about out of time. Just remains for me to thank Joe and Katie for sharing their thoughts today and, indeed, to everyone who's dialled in. We really do appreciate it, setting aside time to listen to us. If there are any questions or observations that occur to you afterwards, or that you didn't have time to ask today, just please, do get in touch with us or your contact at Baillie Gifford, and we'll certainly do our very best to help you. Thanks very much, and goodbye.

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

	2019	2020	2021	2022	2023
ACWI ex US All Cap Composite	33.4	33.2	3.2	-32.0	10.4
MSCI ACWI ex US Index	22.1	11.1	8.3	-15.6	16.2
EAFE Plus All Cap Composite	32.2	28.2	3.8	-30.9	9.8
Developed EAFE All Cap Composite	32.8	27.3	7.4	-32.2	10.1
MSCI EAFE Index	22.7	8.3	11.8	-14.0	18.9

Annualised returns to 31 December 2023 (net%)

	1 year	5 years	10 years
ACWI ex US All Cap Composite	10.4	6.6	4.1
MSCI ACWI ex US Index	16.2	7.6	4.3
EAFE Plus All Cap Composite	9.8	5.9	3.7
Developed EAFE All Cap Composite	10.1	6.3	3.7
MSCI EAFE Index	18.9	8.7	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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