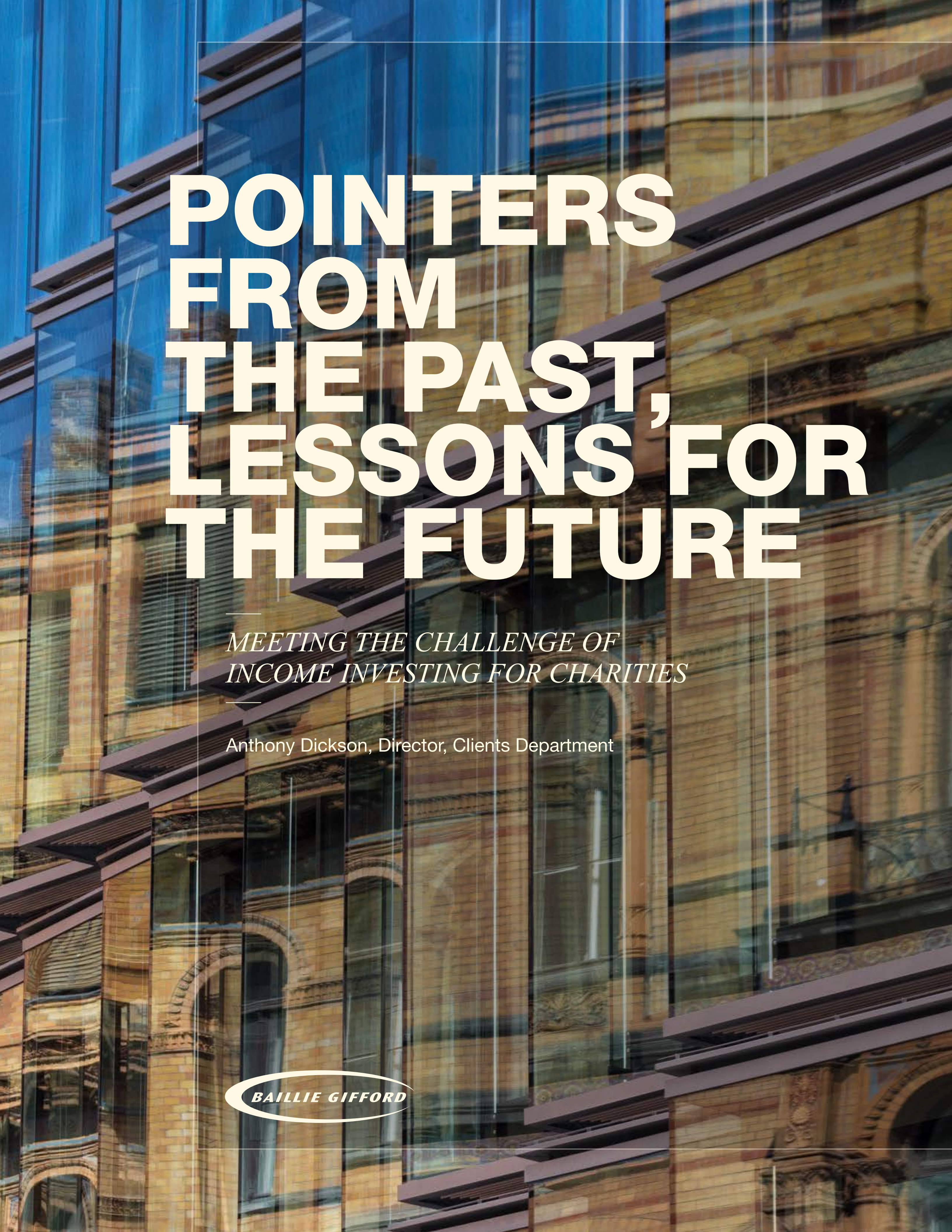

POINTERS FROM THE PAST, LESSONS FOR THE FUTURE

MEETING THE CHALLENGE OF INCOME INVESTING FOR CHARITIES

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BAILLIE GIFFORD

RISK FACTORS

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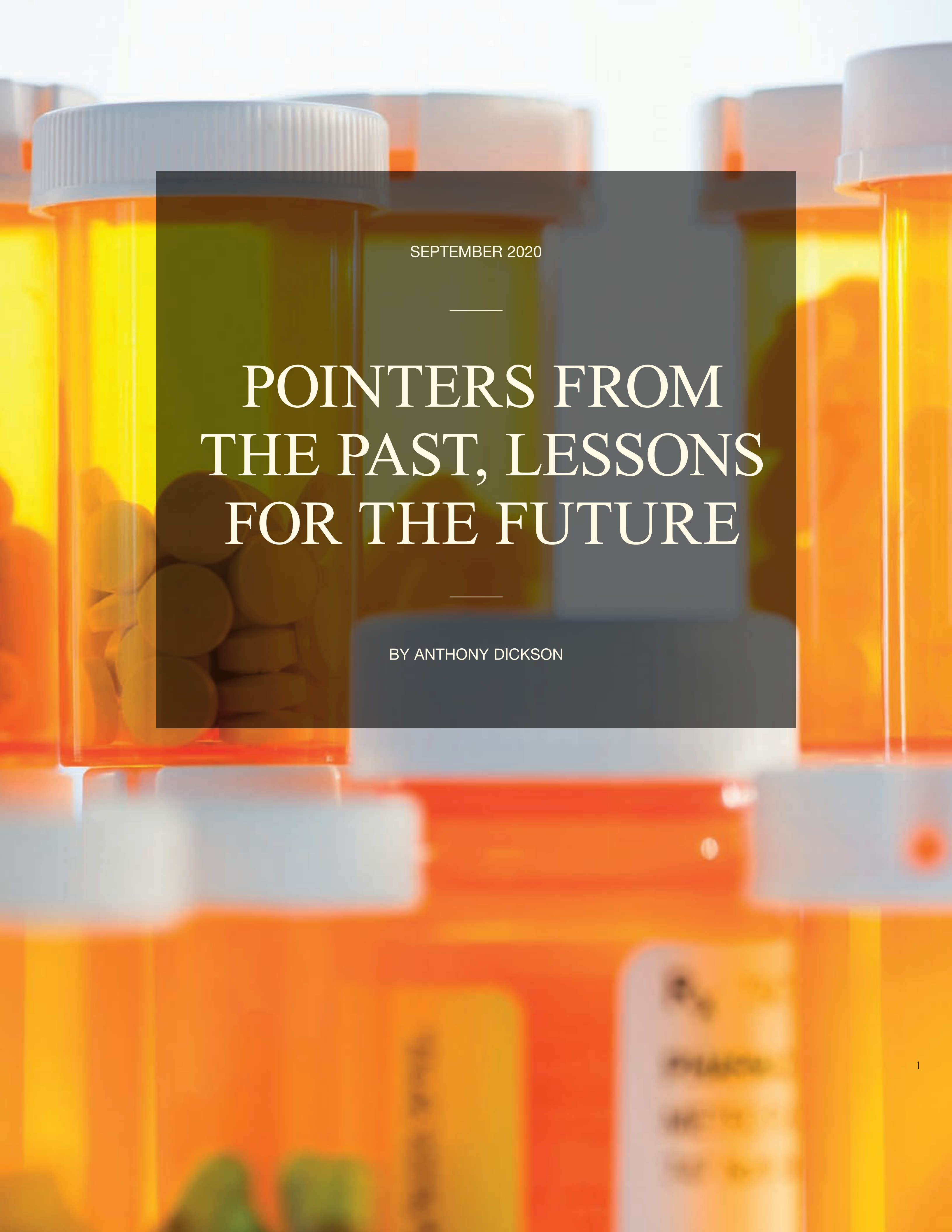

SEPTEMBER 2020

POINTERS FROM THE PAST, LESSONS FOR THE FUTURE

BY ANTHONY DICKSON

John Maynard Keynes
© Picture Post/Getty Images.

The challenges of running a charitable institution have been amplified by the current crisis. The need to spend money is greater than ever, the provision of services has become harder and at the same time many sources of income – from overseas student fees, commercial revenues and rent from property to donations – are under pressure.

Income from investments has become doubly important to those charities which have them. But in many cases those investments have also been found wanting. It is expected that income from the UK equity market will fall by over 40 per cent in 2020, and it is often the highest yielding stocks which turn out to be the most vulnerable in times of crisis. Such businesses have tended to be well-represented in charities' portfolios.

Some charities' investments are managed on a total return basis, but even they will have to consider how much capital they can sustainably spend in the face of considerable uncertainty. The challenge of 'inter-generational equity' or, put another way, the risk of supporting today's beneficiaries at the expense of tomorrow's, has been heightened for everyone.

That challenge is not a new one, but neither is the solution. From 1921 to 1946, the economist John Maynard Keynes was bursar of King's College in Cambridge, and managed its investments with notable success. Over that time, he learned from his mistakes and changed his approach, evolving away from attempts to time markets and becoming instead an accomplished long-term investor. As he wrote in 1934:

"As time goes on, I get more and more convinced that the right method of investment is to put fairly large sums into enterprises which one thinks one knows something about and in the management of which one thoroughly believes."

In *Keynes the Stock Market Investor: A Quantitative Analysis**, David Chambers, Elroy Dimson and Justin Foo chart this evolution and evaluate Keynes's approach and success. This was built not just on having a fairly concentrated portfolio (eventually around 60 stocks) with low turnover and an international flavour, but also on investing in equities in the first place.

While this was a radical step for charities in the 1920s, it is now widely accepted that equities should represent the bulk of a charity's investments. When charities own shares, they own slices of real, cash generating businesses, and if they own shares in companies which can grow their cash flows over time, then the dividends they receive will also grow, and this in turn will lead to capital growth as well. This ability to deliver both income and growth is what makes equities such a good fit for charities with a long-term timeframe.

The investment industry, however, has tended to overcomplicate matters, interposing complicated benchmarks, as well as agonising over targets and layering costs. So, it is reassuring to note that in the right hands, the intuitive approach of investing in dependable, growing businesses from around the world to provide dependable income, and also growth in income and capital over time, has more than held its own in recent months and years. As an illustration, we estimate that, even in the ultimate stress test of the current crisis, the drop in income from the Baillie Gifford Responsible Global Equity Income Fund will be limited to around 5 per cent in 2020.

*Chambers, David and Dimson, Elroy and Foo, Justin, *Keynes the Stock Market Investor: A Quantitative Analysis* (26 September 2013). Journal of Financial and Quantitative Analysis.

In many ways, the world of charity investment has changed for the better since Keynes's day. Trustees today are now accountable to all their stakeholders and so, rightly, pay more attention to whether their funds are invested responsibly. For some time, excluding harmful areas, such as tobacco, from which charities do not wish to profit has been part of this, but charities today are also trying to consider whether their investments are influencing climate change. With tobacco firms and fossil fuel companies having been notably poor investments over recent years (and a source of many dividend cuts), it is hard to argue that charities avoiding these areas have 'missed out', as they were once warned that they would.

However, we would assert more broadly that it is important to invest sustainably, because over the long term it is growth that delivers a rising income, and sustainable growth is more likely to be delivered by companies which think holistically about risks such as climate change, about the welfare of their staff and about the safety of their products. Keynes was right to highlight the importance of management you can truly 'believe' in – but today there's also a role for asset managers to play in encouraging companies to put long-term considerations ahead of pleasing 'the market'. This engagement is an essential element of investing responsibly, and has rarely been as relevant as it is today, when there are so many pressures on companies to take the short-term view.

The challenges facing charities are manifest but, in the field of investment at least, there are solutions and approaches available which marry the best of the past with the needs of the present. Such funds invest responsibly and thoughtfully in resilient companies that are well-placed to deliver for beneficiaries today and in the future, and that do so transparently and cost-effectively. Funds like these are well-placed to meet charities' needs, even in today's uncertain world.

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Anthony joined Baillie Gifford in 2001 and is a Director in the Clients Department with responsibility for UK clients. Prior to joining Baillie Gifford, Anthony worked at Abbey National Asset Managers and prior to that, at the stockbrokers Bell Lawrie White. Anthony graduated LLB in Law from the University of Glasgow in 1988.

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