

WIDER HORIZONS

THE CASE FOR INTERNATIONAL EQUITIES

Stephen Corr, Client Service Director.



Investors should carefully consider the objectives, risks, charges and expenses of the fund before investing. This information and other information about the Fund can be found in the prospectus and summary prospectus. For a prospectus or summary prospectus please visit our website at <https://usmutualfund.baillieghifford.com>. Please carefully read the Fund's prospectus and related documents before investing. Securities are offered through Baillie Gifford Funds Services LLC, an affiliate of Baillie Gifford Overseas Limited and a member of FINRA.

RISK FACTORS

This article contains information on investments which does not constitute independent research. Accordingly, it is not subject to the protections afforded to independent research and Baillie Gifford and its staff may have dealt in the investments concerned.

Any stock examples, or images, used in this article are not intended to represent recommendations to buy or sell, neither is it implied that they will prove profitable in the future. It is not known whether they will feature in any future portfolio produced by us. Any individual examples will represent only a small part of the overall portfolio and are inserted purely to help illustrate our investment style.

As with all mutual funds, the value of an investment in the fund could decline, so you could lose money. International investing involves special risks, which include changes in currency rates, foreign taxation and differences in auditing standards and securities regulations, political uncertainty and greater volatility. These risks are even greater when investing in emerging markets. Security prices in emerging markets can be significantly more volatile than in the more developed nations of the world, reflecting the greater uncertainties of investing in less established markets and economies.

Currency risk includes the risk that the foreign currencies in which a fund's investments are traded, in which a fund receives income, or in which a fund has taken a position, will decline in value relative to the U.S. dollar. Hedging against a decline in the value of currency does not eliminate fluctuations in the prices of portfolio securities or prevent losses if the prices of such securities decline. In addition, hedging a foreign currency can have a negative effect on performance if the U.S. dollar declines in value relative to that currency, or if the currency hedging is otherwise ineffective.

The most significant risks of an investment in The Baillie Gifford International Alpha Fund are Investment Style Risk, Growth Stock Risk, Long-Term Investment Strategy Risk, Geographic Focus Risk, Asia Risk, China Risk, Conflicts of Interest Risk, Currency Risk, Emerging Markets Risk, Equity Securities Risk, Focused Investment Risk, Information Technology Risk, IPO Risk, Japan Risk, Large Capitalization Securities Risk, Liquidity Risk, Market Disruption and Geopolitical Risk, Market Risk, Non-U.S. Investment Risk, Service Provider Risk, Settlement Risk, Small-and Medium-Capitalization Securities Risk, Valuation Risk.

For more information about these and other risks of an investment in the fund, see 'Principal Investment Risks' and 'Additional Investment Strategies' in the prospectus. The International Alpha Fund seeks capital appreciation. There can be no assurance, however, that the fund will achieve its investment objective.

The Baillie Gifford International Alpha Fund (Share Class K) as at 30 September 2020

	Gross Expense Ratio	Net Expense Ratio
Share Class – K	0.61%	0.61%

Source: Baillie Gifford & Co.

Annualised total returns as at 30 September 2020 (%)

	1 Year	3 Years	5 Years	10 Years
The Baillie Gifford International Alpha	23.41	8.61	12.59	8.20
MSCI AC World ex US Index	3.45	1.64	6.73	4.48
MSCI EAFE	0.93	1.11	5.77	5.10
S&P 500	15.15	12.28	14.15	13.74

Source: Bank of New York Mellon and relevant underlying index provider(s). Net of fees, US dollars. Returns are based on the K share class from 28 April 2017. Prior to that date returns are calculated based on the oldest share class of the Fund adjusted to reflect the K share class fees where these fees are higher.

The performance data quoted represents past performance and is no guarantee of future results. Investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. For the most recent month-end performance please visit our website at www.bailliegifford.com/usmutualfund/internationalalphafund

The Baillie Gifford fund's performance shown assumes the reinvestment of dividend and capital gain distributions and is net of management fees and expenses. Returns for periods less than one year are not annualised. From time to time, certain fees and/or expenses have been voluntarily or contractually waived or reimbursed, which has resulted in higher returns. Without these waivers or reimbursements, the returns would have been lower. Voluntary waivers or reimbursements may be applied or discontinued at any time without notice. Only the Board of Trustees may modify or terminate contractual fee waivers or expense reimbursements. Fees and expenses apply to a continued investment in the funds. All fees are described in each fund's current prospectus.

Expense Ratios: All mutual funds have expense ratios which represent what shareholders pay for operating expenses and management fees. Expense ratios are expressed as an annualized percentage of a fund's average net assets paid out in expenses. Expense ratio information is as of the fund's current prospectus, as revised and supplemented from time to time.

The MSCI All Country World ex US Index is a free float-adjusted market capitalization weighted index that is designed to measure equity market performance in the global developed and emerging markets, excluding the United States. This unmanaged index does not reflect fees and expenses and is not available for direct investment. The International Alpha Fund is more concentrated than the MSCI All World ex US Index.

International Alpha Fund Top Ten Holdings as at 30 September 2020

Holdings	Fund %
1 MercadoLibre	4.58
2 TSMC	4.25
3 Alibaba	3.24
4 Scout24	2.91
5 Tencent	2.56
6 SAP	2.41
7 Deutsche Boerse	2.33
8 Nidec Corporation	2.15
9 AIA	2.07
10 Samsung Electronics	2.06

The undernoted table shows which examples from this paper were held by Baillie Gifford at 30 September 2020.

Company	Baillie Gifford Share Holding in Company (%)
Meituan Dianping	5.35
Softbank	2.48

It should not be assumed that recommendations/transactions made in the future will be profitable or will equal performance of the securities mentioned. A full list of holdings is available on request. The composition of the Fund's holdings is subject to change. Percentages are based on securities at market value.

Source: MSCI. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indexes or any securities or financial products. This report is not approved, endorsed, reviewed or produced by MSCI. None of the MSCI data is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such.

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MARCH 2019

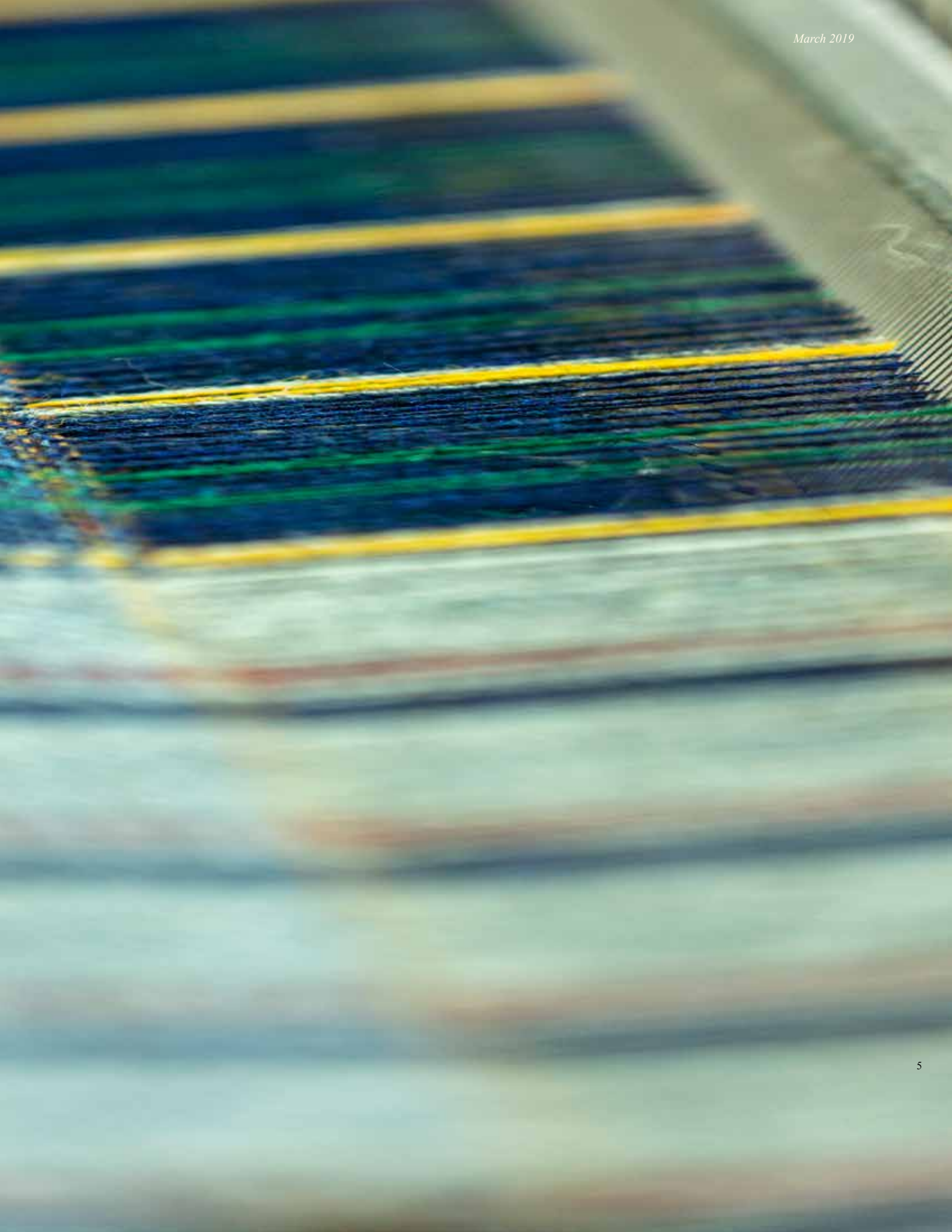
THE CASE FOR INTERNATIONAL EQUITIES

BY STEPHEN CORR

More than ever, we find ourselves making the case for the defence of international equities. We have been asked to do this so often, we thought it worth sharing our thoughts more broadly.

The 'international' asset class has grown in prominence in recent decades. Our own experience in managing such mandates dates back to the 1980s but investing overseas is more deeply embedded in our firm's DNA. The Scottish Mortgage Investment Trust, founded in 1909 and managed by Baillie Gifford for 110 years, made one of its first investments in Malayan rubber plantations.

As growth investors we're optimistic by nature, and as such we start with what we see as the positives for international markets. Quite simply, the opportunity set for growth beyond the US market is expanding, while the US quoted market is shrinking.



US LISTED OPPORTUNITY SET SHRINKS

For the purposes of this report, we define our investible universe as stocks with a market capitalisation above \$1 billion. The universe is summarised below.

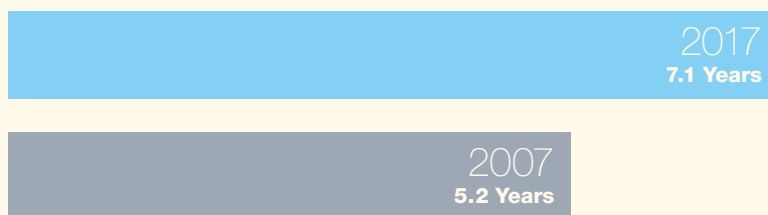
Our Investible Universe

	\$ Value	% \$ Value	No. Stocks	% Stocks	No. Countries
US Market	30,084,380,443,008	55%	2,191	27%	1
International Market	24,379,414,813,840	45%	5,841	73%	101
Total Universe	54,463,795,256,848	100%	8,032	100%	

Source: Bloomberg. Data as at 31 December 2018.

Whilst a higher percentage of value resides in the US market, the vast majority of investible stocks reside outside the US. Consider too that there is a de-equitisation process in the US that gets little attention. Since 1997, the broader universe of US-listed securities has declined from a peak of 7,433, to a 2017 count of 3,616, a 51% fall.¹ Today, there are fewer US-listed companies than in the early 1980s, when the US economy was less than half its current size. There are multiple reasons for this shrinking stock count.² Our own Unlisted Equities team was established so that clients could access exciting growth opportunities at a time when listed market opportunities were falling, and when companies were taking longer to list on the stock market.

Median time from initial funding to Initial Public Offering (IPO)



Source: National Venture Capital Association 2018 Yearbook, Data provided by PitchBook. US companies.

To the best of our knowledge, there is no shrinkage of international equity markets. Quite the opposite in fact, as international markets are offering more listed investment opportunities while the US universe shrinks. For a number of years, Ernst and Young has tracked global IPO trends. In 2014, its research showed that the Americas accounted for 25% of all IPOs and 38% of the proceeds of those IPOs. For 2018, the US share had fallen to 19% and the proceeds to 29%, with more fallow periods in the intervening years, as can be seen in the following chart.

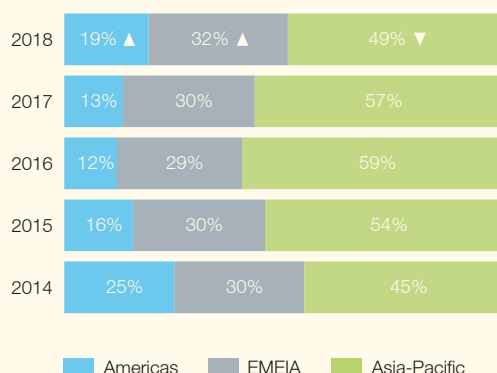
1. Centre for Research in Security Prices, Booth Business School, University of Chicago.

2. Mauboussin, Michael J. et al, The Incredible Shrinking Universe of Stocks, Credit Suisse. March 2017.

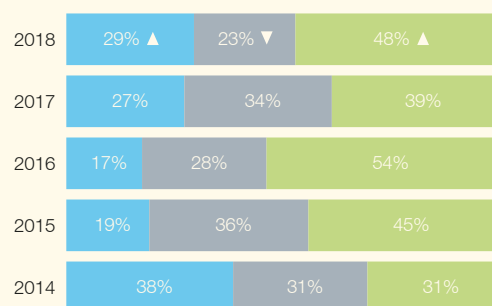
INTERNATIONAL LISTED OPPORTUNITY SET EXPANDS

Global IPO Trends

Regional share by number of IPOs



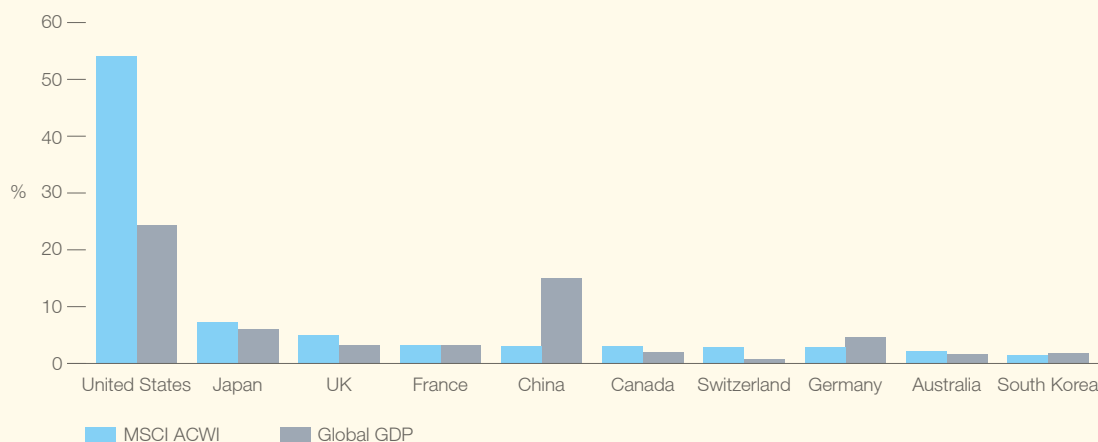
Regional share by proceeds



Source: Ernst & Young, Global IPO Trends, Q4 2018.

Between 2016 and 2018, few of the largest IPOs globally were US domiciled companies. For three years running, Hong Kong and China have topped the league table for IPO activity, according to the Ernst and Young study. As the chart below illustrates, this trend could continue as emerging market companies flourish, redressing the imbalance imposed by legacy benchmarks, and contributing to much of global GDP growth. The link between GDP and market cap is far from linear, but the direction of travel seems clear to us.

Benchmarks are not necessarily representative of investment opportunities

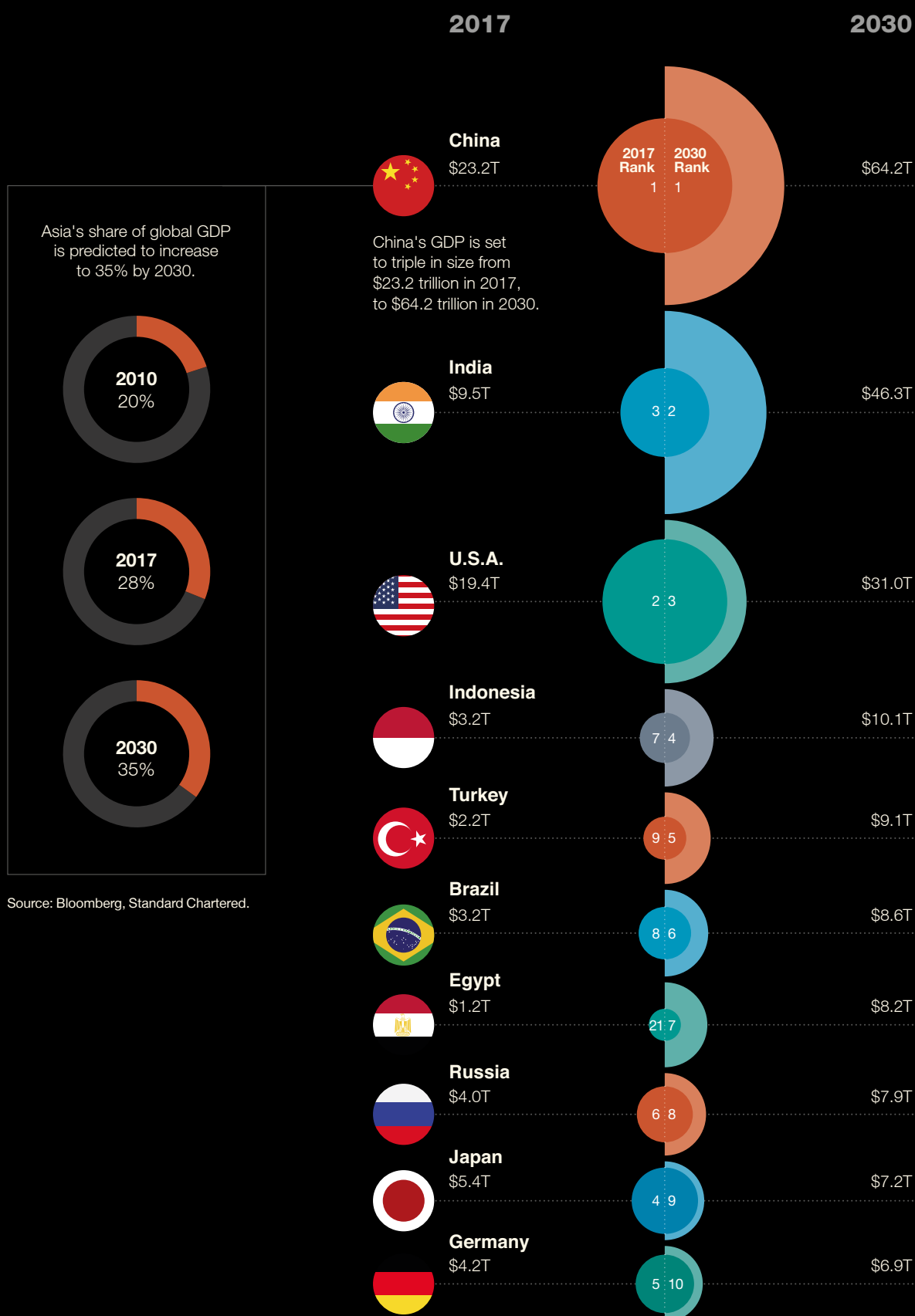


Source: Bloomberg, IMF World Economic Outlook. MSCI ACWI data as at April 2018. Global GDP data as at August 2018.

*A DECADE OF DRAMATIC
GROWTH IN ASIA*

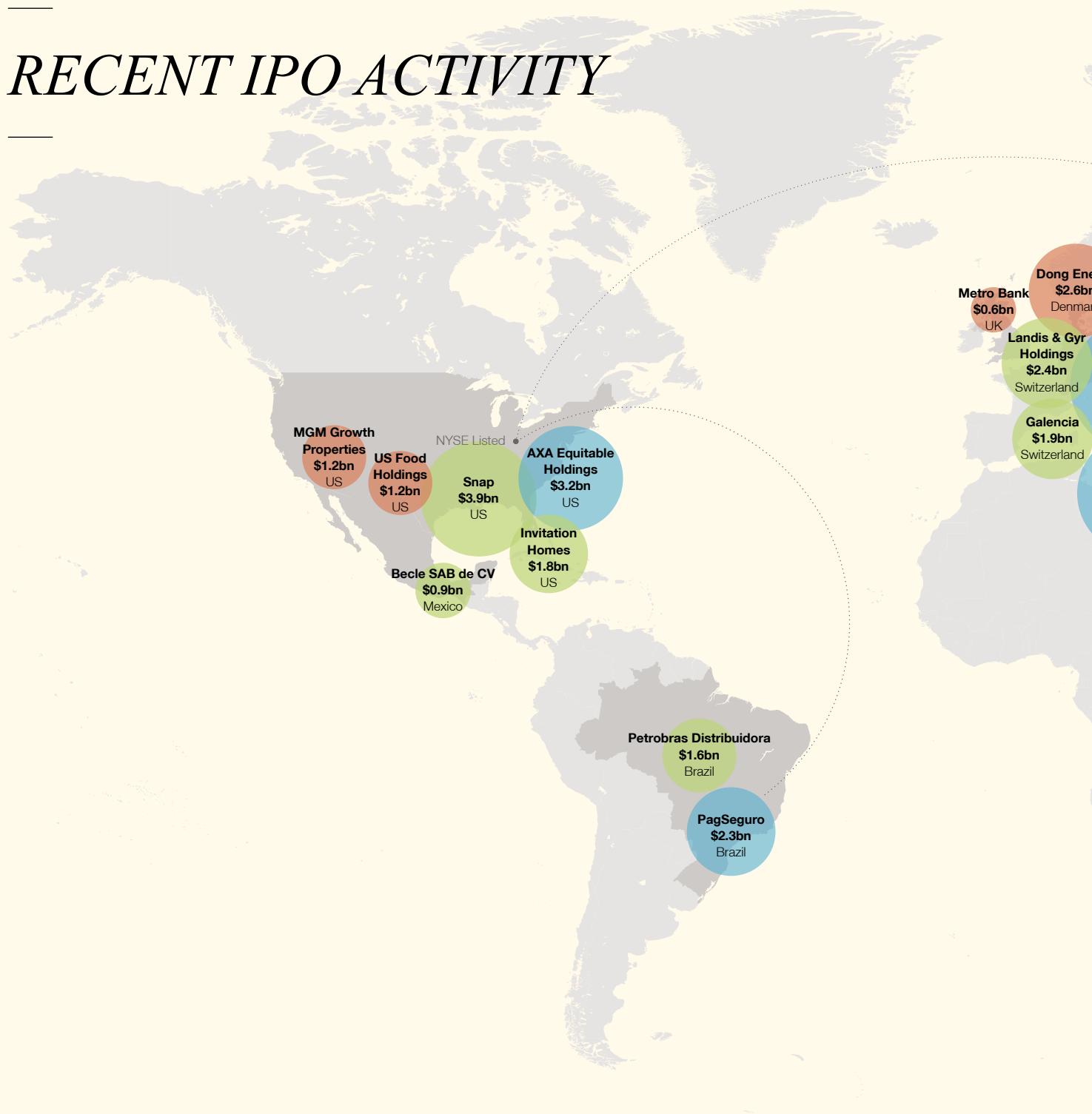


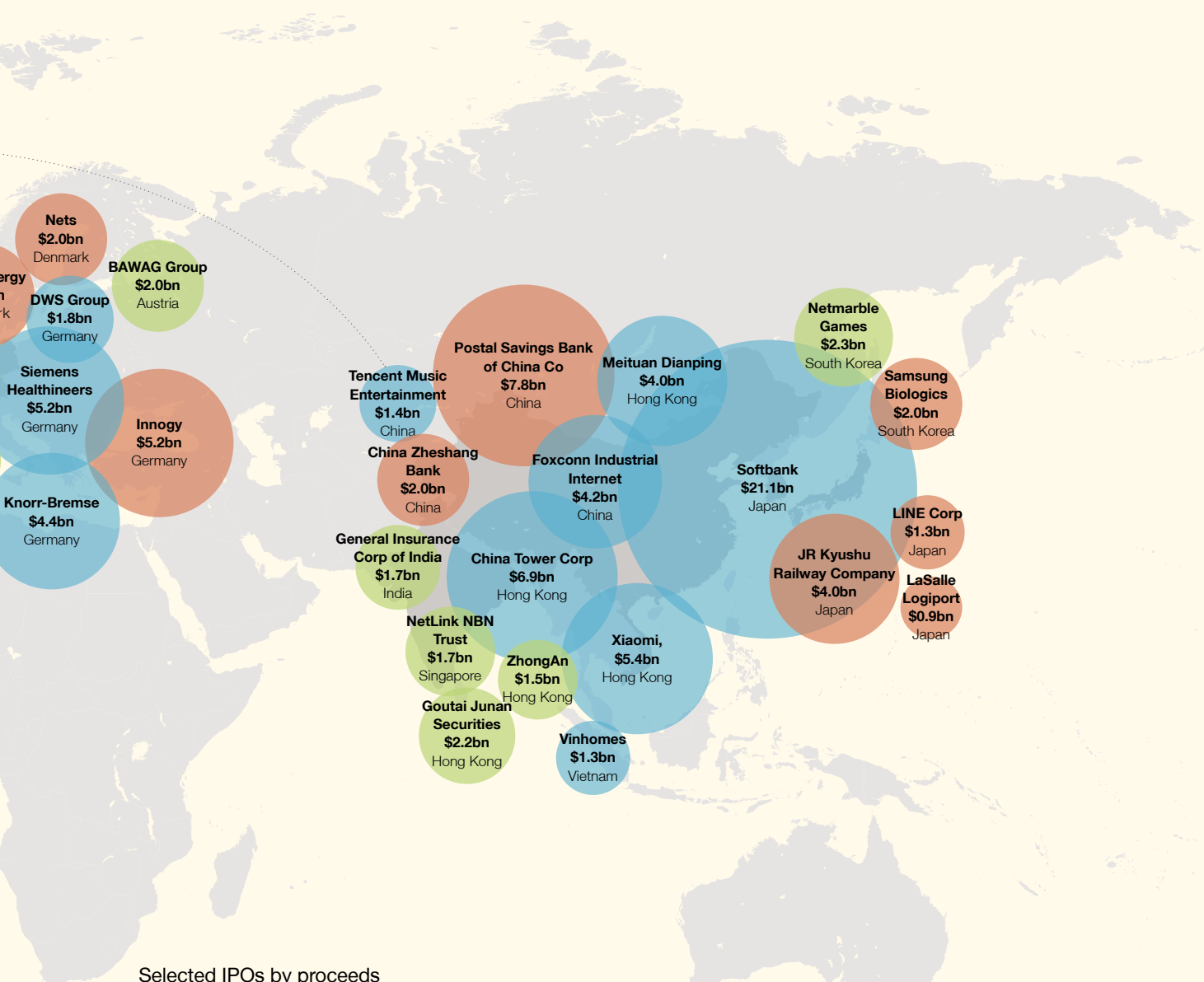
Top 10 Countries, by GDP (purchasing power parity)



Source: World Bank, Standard Chartered. 2030 figures are estimates only.

RECENT IPO ACTIVITY





Selected IPOs by proceeds

2018	\$bn	2017	\$bn	2016	\$bn
Softbank	21.1	Snap Inc	3.9	Postal Savings Bank of China Co	7.8
China Tower	6.9	Landis & Gyr Holdings	2.4	Innogy	5.2
Xiaomi	5.4	Netmarble Games Corp	2.3	JR Kyushu Railway Company	4.0
Siemens Healthineers	5.2	Goutai Juron Securities	2.2	Dong Energy A/S	2.6
Knorr-Bremse	4.4	BAWAG Group	2.0	Samsung Biologics	2.0
Foxconn Industrial Internet Co	4.2	Galencia AG	1.9	Nets	2.0
Meituan Dianping	4.0	Invitation Homes	1.8	China Zheshang Bank Co.	2.0
AXA Equitable Holdings	3.2	Netlink NBN Trust	1.7	LINE Corp	1.3
PagSeguro	2.3	General Insurance Corp of India	1.7	MGM Growth Properties	1.2
DWS Group GmbH & Co	1.8	Petrobras Distribuidora SA	1.6	US Food Holdings Corp	1.2
Tencent Music Entertainment	1.4	ZhongAn Online P&C Insurance Co	1.5	LaSalle Logiport	0.9
Vinhomes	1.3	Becle SAB de CV	0.9	Metro Bank	0.6

Source: E&Y, Global IPO Trends, 2016, 2017, 2018. The 36 IPOs selected represent the top three listings by proceed in each quarter between 2016 and 2018.

Note: Baillie Gifford does not necessarily hold these companies.

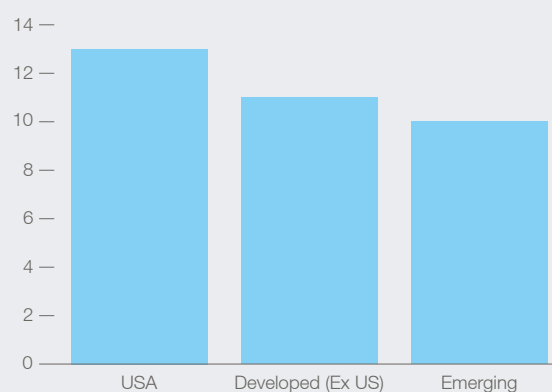
GETTING OUT MORE

We live and invest in a world overflowing with ‘information’. Hardly a day goes by without a new study telling us that ‘screen time’ is dominating our lives. Fewer reports ask whether more information is a good thing, or how much of it is mere noise. Fake news abounds. Baillie Gifford’s investment department consists of over 100 investment managers and investment trainees, each tasked with producing research to be shared company-wide. Our investment department is the best generator of good investment ideas for client portfolios.

It helps that there are fewer investment banking analysts ‘covering’ stocks outside the US. For our investible universe there are two fewer analysts covering stocks in developed international markets than there are covering the US, and three fewer analysts covering emerging market stocks. As investment banks shrink and regulators look for managers to become less reliant on broker services, a well-resourced investment department grows in importance.

Our roots are in Edinburgh, but when it comes to research, we’re getting out more. In 2019, we expanded our research capabilities by hiring a senior investment analyst to be based in our US office. Extended research placements in our Hong Kong office are also on the cards for 2019.

Average Global Analyst Cover



Source: Bloomberg. Based on a global universe of companies with a market capitalisation over \$1 billion. 31 October 2018.

Trade-weighted US Dollar Index



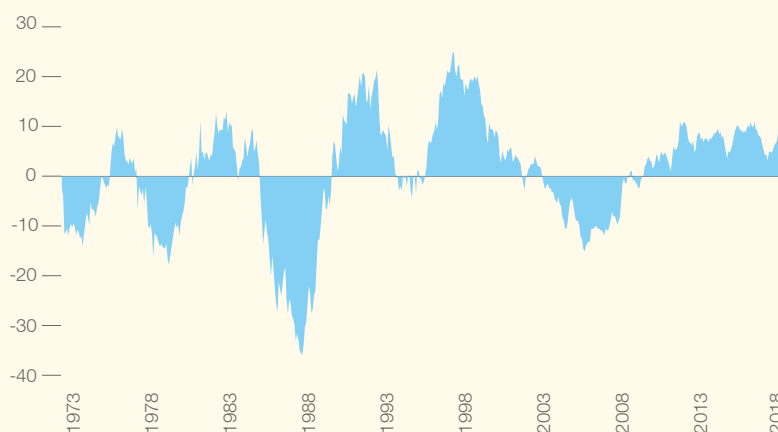
Source: Bloomberg.

Note: The trade-weighted US dollar index measures the value of the US dollar against other foreign currencies.

Perhaps the starkest but simplest point to be taken from the table on page 6, is the number of countries. Having all your eggs in the US equity basket seems imprudent.

Clichés only become clichés with repetition. They were first coined as valuable life lessons by those who had learned the hard way. The trade-weighted US dollar index has been on a strengthening, if volatile, path since 2008. It has strengthened 30% compared to other international currencies. If that strengthening ends, exposure to a portfolio of international stocks and currencies, as opposed to solely US equities, will become increasingly important.

Three-year Rolling Returns – S&P 500 vs MSCI EAFE



Source: Bloomberg. Annualised 3-Year relative rolling returns (S&P 500 vs MSCI EAFE).

Past performance is not a guide to future returns.

Over the years, the level of interest in US domestic equities versus international equities has waxed and waned, most commonly when one asset class has enjoyed a prolonged period of outperformance. We are at one such juncture today. Taking three-year rolling returns for the S&P 500 and the MSCI EAFE index as our comparative benchmarks, domestic US equities have enjoyed nine consecutive years of outperformance over international equities. As this is one of the longest periods of outperformance in the last 45 years, it is not surprising that more people are calling for more assets to be allocated domestically. However, after such a lengthy period of outperformance, this may not be the best time to make that switch.



Comparing the performance of one asset class against another is all well and good, and simply looking at historic earnings growth of respective benchmarks shows that such outperformance is justified. The question for allocators of capital is surely ‘where do we go from here?’ Most white papers making the case for international equities will focus on diversification and valuation. The diversification point is almost always valid, and the valuation case happens to be valid at this point in time.

On a forward price/earnings³ basis, the international benchmark is almost 3.0x multiple points cheaper, at 11.6x versus 14.5x and financial leverage is lower in international markets at 39% versus 55% for S&P 500 stocks. However, when it comes to earnings growth and profitability, the markets struggle to measure up to the US market. Historic earnings growth for the S&P is far superior to international markets. It would appear that US companies have done a better job of generating superior returns for shareholders too, albeit with more leverage. Rather than speculate as to whether US profitability margins have peaked, as many have claimed, we would again ask; where do we go from here?

Finally, the tsunami of US domestic money flowing into passive funds continues unabated. A similar acceleration of flows into international passive funds cannot be ruled out, but the following table is illustrative for those who believe in active management. Taking the 5 year column as our example (our typical investment horizon), the benchmark has returned an annualised 0.67%. A first quartile manager has returned an annualised 3.03%, and the top 5% of managers have returned an annualised 5.10%. Done correctly, truly active management can outperform. Glib statements that active managers cannot add value are simply misleading.

Table 2 – ACWI ex US Active Management Universe

% Returns	3 Year	5 Year	10 Year
ACWI ex-US benchmark*	4.48	0.67	6.57
5th percentile	8.94	5.10	12.16
First Quartile	6.28	3.03	9.47
Median	4.38	1.71	8.07
Third Quartile	2.63	0.42	6.94
95th Percentile	0.38	-1.57	5.81

*MSCI AC ex US Free

Source: Intersec. Annualised returns to 31 December 2018.

Past performance is not a guide to future returns.

3.Price/Earnings is the weighted average ratio of current share price divided by the 12 month forward earnings per share. This represents a measure of valuation levels.

The opportunity set in international markets continues to expand while the US market shrinks. You will excuse us if some of this commentary seems self-indulgent, but as passionate believers in long-term, active investment management, we think it strange to have to defend the benefits of international equities. But defend them we must, and defend them we will, for another 110 years if necessary.

ABOUT THE AUTHOR



STEPHEN CORR

Client Service Director

Stephen joined Baillie Gifford in 2016 and is a Client Service Director within the International Alpha Team. He previously spent 16 years as a Global, International and EAFE portfolio manager with Blackrock, Scottish Widows Investment Partnership and, most recently, Nikko Asset Management. Stephen graduated Bachelor of Business Studies (BBS) from Dublin City University in 1998 and became a CFA Charterholder in 2003.

CURIOUS ABOUT THE WORLD

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