# *EUROPEAN FUND – THE HUNT FOR EUROPEAN TENBAGGERS*

Investment managers Moritz Sitte and Stephen Paice dispel the negative perceptions of the European market by discussing two exciting companies which exemplify the growth potential in Europe, and their investment strategy which aims to seek out European tenbaggers.

*The value of your investment and any income from it is not guaranteed and may go down as well as up and as a result your capital may be at risk.*

*This communication was produced and approved in June 2019 and has not been updated subsequently. It represents views held at the time of recording and may not reflect current thinking.*

**Moritz Sitte (MS):** I don't think it's controversial to state that the overall perception of Europe – from never-ending Brexit negotiations to economic stagnation - has been truly awful for a long time now. But what I find fascinating is that there's a huge discrepancy between this poor top-down perception on the one hand, and the reality which we, as bottom up investors, are witnessing on the other hand. As it turns out, Europe offers us fantastic opportunities to own exceptional businesses. And that is why we spend all our time thinking about a company's growth opportunity, its edge and the alignment between stakeholders. And that is also why we seek to be long-term owners of businesses.

**Stephen Paice (SP):** We now have a much better understanding that portfolio and stock market returns are driven by a relatively small number of companies. Shares in these companies will not just go up 2 or 3 times, but 5, 10 or 100 times. And this is what's driving our enthusiasm for European companies. When we look at the distribution of returns in Europe, we find that the probability of finding one of these big winners is the same as it is in most other regions. It's just the opportunity set is very different: Europe specialises in niche B2B businesses, industrials, MedTech, some fantastic consumer discretionary brands, and increasingly, some very small but disruptive online platforms. But to benefit from the asymmetry in these companies, you need to focus on what might go right rather what might go wrong, and be willing to hold them for a very long period of time.

**MS**: Avanza is a great example of the type of business that we get excited about: as the leading online savings platform in Sweden, it is disrupting the Swedish savings market by offering fantastic service whilst charging very low fees. It has been voted Sweden's savings bank of the year for the ninth year in a row now, thanks to outstanding customer satisfaction scores. And it has deliberately lowered its brokerage fees by almost 60 per cent over the last five years. We think this is a business that could be multiples of its current size in ten years' time.

**SP:** The economics of online businesses can be fantastic because of the network effects and because of the low capital intensity, but you can find these characteristics in other industries that are less glamourous and that tend to be overlooked. IMCD is one of our largest holdings. This is a founder-run Dutch speciality chemicals distributor so acts as a consultant and it connects lots of smaller chemicals suppliers to its customers. And because it's the largest player in what is a very fragmented industry, the value of its network increases to both the buyers and the sellers. Can this be a tenbagger over the next 10 years? I think it can. The chances are fairly slim, however they are much better than average – and that's what matters.

**MS:** What we want to do with our fund is to expose ourselves to owning big winners. Doing so requires ignoring the index. After all, it's the large constituents in the index – from banks to big pharma – which in our opinion are structurally challenged because they're being disrupted. We get asked a lot about active versus passive investing. Europe really is the last place you would want to invest [in] passively by buying the index.

**SP:** What fund managers say and what they actually do are sometimes very different, so when we talk about investing in high quality, growth companies, managed by people we trust, you can see this reflected in the characteristics of the fund. So our companies typically grow much faster than the market, they generate higher returns, and the majority are owned and managed by insiders. We also want to stand out in an industry which is still far too prone to short-termism and self-serving behaviour. So we want to be long term, and you can see this through the turnover which is typically between 10 and 20 per cent. Our active share is very high and we're offering what we think is very good value for money. Beyond that, we want to take advantage of the negative top-down sentiment towards Europe and help provide capital to those entrepreneurial businesses that have the best chance of generating outstanding returns.

**Annual Past Performance to 31 March Each Year (net %)**

| | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|
| Baillie Gifford European Fund | 2.1 | 12.8 | 23.3 | -9.3 | 0.9 |
| MSCI Europe ex UK Index | -7.6 | 11.7 | 16.4 | -4.3 | -12.0 |
| MSCI Europe ex UK Index+ 1.5% p.a over rolling five-year periods | -6.2 | 13.3 | 18.1 | -2.8 | -10.6 |

Source: StatPro. Based on B share classes in US dollars. Returns reflect the annual charges but exclude any initial charge paid.

The managers believe the MSCI Europe ex UK Index + 1.5% is an appropriate benchmark given the investment policy of the fund and the approach taken by the manager when investing.

Past performance is not a guide to future results.

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