THE SCOTTISH AMERICAN INVESTMENT COMPANY P.L.C – MANAGER INSIGHTS

Investment manager Toby Ross gives an update on The Scottish American Investment Company P.L.C.

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A Key Information Document for SAINTS is available by visiting www.bailliegifford.com

Toby Ross: The coronavirus has already had a tragic human cost and caused a lot of disruption to many peoples' lives. It has also brought unprecedented uncertainty for companies, and so for income-seeking investors. In the UK, current estimates are that the dividends paid by British companies will fall by more than half this year. That would be a bigger drop than was even seen during the Financial Crisis.

For many savers, this potential dramatic fall in income is another thing to worry about at an already worrying time. As investors in SAINTS, however, we believe that there are two reasons why you can feel confident in the outlook.

An investment approach built for resilience

Firstly, the nature of the underlying investments which you own through your holding in SAINTS.

Our investment approach has always been focused on finding high-quality, robust companies, that are capable of paying resilient dividends over time. We think we own through-cycle winners, not companies that are relying on a favourable economic backdrop in order to be able grow. That's why the biggest holdings in SAINTS' equity portfolio are companies like Roche or Procter & Gamble or Deutsche Boerse, not Lloyds, or big oil companies.

Indeed, a key question we've asked ourselves when picking stocks for SAINTS over the past few years is: 'How resilient might this dividend be in a time of stress?' We asked that question when the sun was shining so that SAINTS investors could feel reassured when the outlook looked more difficult - as it does now.

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We've been massively helped in our stock-picking by having a global universe of 4,500 dividend paying stocks from around the world to choose from. And that's made it much easier for us to avoid many of the areas that are causing so much disruption to dividends in the narrower UK market. But it also gives us a big diversification benefit - companies like Anta Sports, the Chinese Sportwear business, are already returning to work again, even while Europe remains in lock-down.

In our property portfolio, SAINTS is also biased towards strong tenants, with little exposure to the most challenged areas, and the property manager has been increasing that resilience over the last few years, by reducing exposure to areas like restaurants or retail or pubs.

So the investment approach, and your underlying investments – which are global, long-term, genuinely diversified equities focused on resilient growth, combined with conservatively managed property investments – both of those are really proving their worth at the moment.

Revenue reserves and strong board commitment

The second reason to feel confident is because SAINTS is an investment trust, it has revenue reserves that the board can use to support the dividend stream when things get more difficult.

Because in this extreme environment we are expecting some companies, even strong ones, will cut their dividends. And indeed, we recognise that in some cases that is absolutely the right decision for boards to take. So, despite our focus on resilience, we are expecting that the income from SAINTS' equities will be lower in 2020 than it was in 2019.

Equally the board is also clear that they wish to be a responsible landlord and support our property tenants if they need it.

But SAINTS has been able to build up revenue reserves in the good times to support its income in the bad. The ability to use such revenue reserves to smooth income is one of the great advantages of the investment trust structure. SAINTS currently has around 9 months' worth of dividends in its revenue reserve. And in their recent announcement, the board has reaffirmed just how committed they are to that dividend.

So resilient income streams, combined with healthy revenue reserves and a strong degree of board commitment, all mean that SAINTS shareholders should feel confident about continuing to receive their dividend – as indeed they have done since it was last reduced in 1938.

What have we been doing as managers?

That hopefully gives some reassurance that SAINTS enters this period well-positioned. But what have we been doing as managers?

Well, as responsible stewards of our client's capital, our first priority has actually been to get in touch with many of the management teams of the companies in which we invest, to offer them our support in a challenging period. We know that they are trying to do the right thing for their employees, their customers and their communities as well as for their shareholders. We want them to know they've got our support in doing this.

And we've been really glad to see holdings like Sonic Healthcare and Roche going to great lengths to help solve the testing crisis that society is facing. Really going the extra mile.

When it comes to making changes to the portfolio, we think it's more important than ever that all our decisions as managers are guided by what's best for SAINTS' long-term income stream. This means we need to resist the temptation of apparently cheap, high-yielding stocks. The income may turn out to be illusory and often the long-term prospects look pretty poor. So we aren't tempted to pile into the oil majors, or retailers, or go bargain-hunting in the banking sector.

Instead, we need to focus, at the individual company level, on where are the biggest long-term income growth opportunities? Who are the most adaptable management teams? Who's going to emerge from this period of disruption stronger?

So with that as our guide, we have started to make a couple of changes to the portfolio. We've added to some of our favourite names, at more attractive valuations. We've also taken new holdings in a couple of businesses that we've admired for some time, where we think the market is now unduly focused on the short-term profit outlook. The great American asset manager T Rowe Price, for example, and Hargreaves Lansdown, which is the dominant savings platform in the UK.

And on the other side, we've moved on from a couple of stocks where our conviction in the long-term case had been ebbing, and which we think won't emerge from this crisis stronger.

Time to invest for long-term income, not short-term yield

2020 will go down as a momentous year for dividend investors. Hopefully we have reassured you that SAINTS' own dividend is likely to be solid in this time of uncertainty.

But if there is a bigger lesson for income investors to take from this year, we think it's around the importance of focusing on long-term income from a global opportunity set. We think investors need to stop chasing high and near-term yields, and embrace a much richer, broader opportunity set than perhaps they've typically done in the past.

We strongly believe that it's that focus on the long term that will help your income not just be resilient today, but also grow over time.

So thank you for your time and for your trust; and we hope you and all your families stay well.

Share Price Performance to 31 March each year

	2016	2017	2018	2019	2020
Scottish American Investment Company P.L.C share price performance (%)	9.3	34.6	10.8	7.7	-4.1

Source: Baillie Gifford & Co, Morningstar and underlying providers.

Dividend Performance to 31 December each year

	2015	2016	2017	2018	2019
Total dividend per ordinary share (net) – (pence per share)	10.70	10.825	11.10	11.50	11.875

Source: Baillie Gifford & Co, Morningstar and underlying providers.

Past performance is not a guide to future returns.

SAINTS invests in overseas securities and changes in the rates of exchange may also cause the value of your investment (and any income it may pay) to go down or up.

The trust invests in emerging markets where difficulties in dealing, settlement and custody could arise, resulting in a negative impact on the value of your investment.

SAINTS has some direct property investments, which may be difficult to sell. Valuations of property are only estimates based on the valuer's opinion. These estimates may not be achieved when the property is sold.

The trust can borrow money to make further investments (sometimes known as "gearing" or "leverage"). The risk is that when this money is repaid by the trust, the value of the investments may not be enough to cover the borrowing and interest costs, and the trust will make a loss. If the trust's investments fall in value, any invested borrowings will increase the amount of this loss.

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