SCOTTISH MORTGAGE AGM – MANAGER INSIGHTS

JAMES ANDERSON

In this AGM film, James Anderson, co-manager of the Scottish Mortgage Investment Trust, reflects on the biggest lessons he has learnt during his time managing the trust.

All investment strategies have the potential for profit and loss. Past performance is not a guide to future returns.

A Key Information Document for the Scottish Mortgage Investment Trust PLC is available by contacting us.

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James Anderson: Hello, and welcome to the Scottish Mortgage AGM. I'm very upset that this is a distant meeting, but I would still like to express my extreme gratitude to you all for listening and for your support over many years. It means a very great deal to all of us.

Having said that, I think it's still an important moment to reflect on the over-20 years that I've been managing and co-managing Scottish Mortgage, perhaps to give a few impressions of what I've experienced and learnt.

The first comment that I'll make is that we have to be prepared to follow our own route. Famously, John Maynard Keynes said that it was often better to fail conventionally than to succeed unconventionally. I'd take that a step further. If I may be so bold as to offer the maestro some advice, it would have been that if you were conventional, you would fail.

I think that the investment world we live in is even more biased in that direction. When you have thousands upon thousands of people believing that value exists as a prime motivation in an investment, that value is measured by a near-term P/E, that macroeconomic conditions over the next six to 12 months matter, then I don't think you have much chance of being able to produce returns for shareholders competing in such a crowded market.

Instead, I would say to you that, for us, why we believe and how we think is more important, at any point, than the precise what we believe or what companies we own. It is that background noise of thought that you should emphasise, not the current noise of emotion.

So what do we believe should exist in the background? The first topic is that we think it's quite clear that you should live life in the extremes. Investment performance is a matter of capturing the extraordinary. The extraordinarily successful, the extraordinarily great, the extraordinarily unusual.

Most companies do not matter at all and do not, over the long term, produce returns, and that transcends the divide between value and growth. We are just as uninterested in the average growth company as we are in the average value company. We're interested in the companies that culturally, in the scale their markets and scale of their returns, can produce those extremes of performance. And we've been lucky enough to own several of them over the past decades.

But beneath that reverence for the extreme, what do we think is important to keep in our minds? What's the deep background? The first, inevitably, is to be long term. In the short term, almost anything could matter. In the long term, it's the deep rhythms of success and compounding that should matter to us, and where we can have a difference of view from others.

Those differences of views are really built on two major ingredients. The first is that we would infinitely rather endure drawdowns, disappointments and temporary setbacks than abandon our backing and our experiences of and with great entrepreneurs and great companies.

Almost all companies, even though their share prices look as though they progress from the bottom-left to the top-right, constantly have 35 to 50 per cent drawdowns over the course of time, but it's then, very often, that their most alluring prospects come out.

We have found that our best guides to investing principally come from the great entrepreneurs of our times. I think we've talked enough about them individually that you will recognise many of the cases. But those experiences are quintessentially uncomfortable.

There are no companies that we have been more criticised, internally, externally, by shareholders sometimes but particularly by the media, for owning than Amazon and Tesla. These are companies that obviously run on a rhythm and a notion and an idea of their own, and ones that are not easily assimilated by most observers.

So I would stress to you in this too, endurance and being willing to be misunderstood, being willing to be unpopular, matters a great deal more. And I worry much more when everybody approves of the same people and the same companies as we do, rather than when we and they are being criticised.

Secondly, I'd say that there is a great public knowledge source of information, source not just of information but of high-probability information for making you take good decisions, which resides in serious academic and intellectual understanding and knowledge.

A huge example of this would be our belief in the development, exponential development, of battery technologies, of renewable energies, of storage. We first came to the thesis close to ten years ago now, when, through work we were doing with the Santa Fe Institute and listening to them and other great experts in these areas, it became apparent that the learning rates were somewhere between 50 and 25 per cent per annum.

We all know that if you accumulate that over a decade, then you make huge progress and you make technologies that have already stagnated increasingly vulnerable. So even in the difficult moments of investing with Tesla and NIO and the like, we felt pretty sure that these technologies would matter, that it was really a 90 per cent probability level in recent years, which is something that's most unusual.

We have to carry on looking at serious research rather than the noise of stock markets and the noise of broker reports on this, and that is something I find extraordinarily beneficial, and I think we can build on still more. We're not yet halfway in exploring all the benefits of that.

So where are we now, looking forward? What does all this tell us? I'll go back once more to Amazon. One of Jeff Bezos's greatest sayings in the early days of Amazon was that there was this weirdness about his business, that everything he used got better and cheaper every year, usually by around 50 per cent.

Now, that's played out enormously for the digital giants, but the exciting moment now, the exciting decade ahead, is that the number of areas of our economy, the scale of areas in our economy, where that process of getting better and cheaper by around 50 per cent per annum, is expanding dramatically.

I've mentioned one already, which is the whole notion of renewable energy and storage. Now, in that area, I think we neglect the extraordinary benefits that may be for humanity in this. It isn't just the critically important avoidance of the negative, the avoidance of some of the worst consequences of climate change, but it is that we should have virtually free energy in the future. And that allows for human ingenuity and human productivity, humankind in a much broader way than it is now, to flourish. But even that may be less than the application of deep biology with big data.

We've now got to the position where, literally, in the last year, even more in the last six months, we're seeing the situation whereby the insights from genomics and big data are allowing us to finally move ahead of our very limited biological understanding, by simply the provision of knowledge and data.

Now, I think that is likely to revolutionise human healthcare and the price of human healthcare, the dimensions and the spread of the best healthcare over the coming years. And given that it is so reliant on this huge explosion of data and knowledge, I think we're already beginning to see the business models emerge, from Moderna to Tempus, for instance, that give the possibility of very dramatic improvement, very dramatic corporate returns in the future.

So I really would stress that I feel incredibly envious of my colleagues who're going to be enjoying seeing all this develop and going through the hard-yards with the companies over the decade ahead.

I would also like to stress that I think these examples show that for all the talk and all the procedural measures that people like to think about the governance of companies, that we can be incredibly proud of just how beneficial the impact of many of our investments have been.

To go back to first principles, I think the two greatest dangers currently facing the world are respectively climate change and healthcare, as proven by the dreadful pandemic.

Now, in both those cases, I think Scottish Mortgage and its shareholders ought to be thrilled that we've made a real impact. It's even conceivable that Tesla's existence, or at the very least its progress would have been delayed very substantially without our financial backing. Of course, Elon Musk and his colleagues have done far more than us, but as an individual investment, we have made a real difference.

Secondly, let me take the pandemic example. The pandemic was sequenced and the initial vaccine treatments worked out in less than an accumulated two weeks, by the combination of two of our companies. Illumina, which several years ago we were instrumental in keeping as a private, independent entity, first sequenced the genome, and then it moved on to being able to analyse the Covid virus. Now, within 48 hours they gave that sequence to, amongst others, Moderna, whose treatment has both proven highly beneficial and extremely revolutionary.

Again, I think that in both these cases, we have, as shareholders, made a significant difference, a significant difference to two absolutely dominant problems. I feel much more proud about that than signing up to any number of ESG mantras. We have helped.

So if I were to roll this forward, which is the most important part at the Scottish Mortgage level as well as the general opportunity level, I would say that, for fund management in general, for investment in general, I'm not altogether optimistic. Our industry has become obsessed with its own mantras, obsessed with trying to run businesses for fund-management's sake rather than making great capital allocation decisions.

The CFA has turned itself into the worst type of middle-class trade union, and has thwarted much thought. All too many fund-management organisations are far too interested in their internal bureaucracy and their internal financials, rather than being great investors.

But I can assure you of one thing, and that is that my successors, Tom and Lawrence, will not compromise. They are deeply curious, deeply intelligent people who want to do their absolute best to try and assist the returns that you as shareholders and that society as a capital allocator can make.

So I am very, very optimistic about the future possibilities for Scottish Mortgage and for their tenure. Thank you very much. It's been a joy working with you over the decades.

Scottish Mortgage Annual Past Performance To 31 March each year (net %)

2017	2018	2019	2020	2021
40.9	21.6	16.5	12.7	99.0

Source: Morningstar, share price, total return.

Past performance is not a guide to future returns.

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