MANAGED FUND – MANAGER INSIGHTS

Lucy Haddow, product specialist, speaks to investment managers Steven Hay and Iain McCombie about the Managed Fund, as they discuss the fund's most frequently asked questions and look forward to what's to come.

The value of an investment in the fund, and any income from it, can fall as well as rise and investors may not get back the amount invested.

Past performance is not a guide to future returns.

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Lucy Haddow (LH):
Hello and welcome to this video on the Baillie Gifford Managed Fund. My name is Lucy Haddow. I'm a specialist on the fund and I'm joined today by its co-managers Iain McCombie and Steven Hay. They're here to answer the burning questions that as clients or perhaps prospective clients we know are on your mind. So, Ian, first question for you. Lots of people want to know what the fund looks like at this point in time, so perhaps you could cover that from an equity perspective.

Iain McCombie (IM):
Sure Lucy. Well about 75 per cent of the fund is in equities, and I think the really important point is that it's very broadly diversified. I can say that in two different ways. Firstly by geography, we split the fund into four different regions and we give the money to each of the regions to invest. So that's the UK, the US, Europe and Asia & emerging markets. So, no more than 20 per cent of the fund is in each region so it is well diversified. The second way to think about it is by stock, we have over 200 stocks in the fund and we are trying to find growth stories within that. The largest one is only 1.6 per cent of the fund and is a company called Shopify so again it is very broadly diversified.

LH:
Brilliant. Thank you so much, Steven. Same question for you. But what would be really helpful is if you could bring into that conversation on fixed income, the impact of inflationary pressures because they're dominating the headlines at the moment.

Steven Hay (SH):
Absolutely Lucy. I mean, there is a very strong inflationary dynamic right now, and I think there are good structural and cyclical reasons why we might see a period of sustained higher inflation. But it's important to remember the managed funds been around for 34 years. It's seen periods of high inflation, deflation, market crises, and we have the flexibility in terms of finding investments that can weather these storms. But you're right, inflation is a challenge to bonds, and bonds are less attractive now than they were during the period of low inflation. So from an asset allocation point of view, we have reduced the weight of bonds in the portfolio and increased in equities. Now it's important to remember, though, that the bonds do provide a really important role within the portfolio, providing balance and reducing the overall volatility of the fund, which is what our clients want.

Now within the bond portfolio itself, we have been reducing exposure to rising bond yields by buying shorter-dated bonds. We've also been favouring corporate bonds, so in particular, high yields, where actually a bit of inflation can be quite helpful for these more indebted companies. And as Iain mentioned bond pickers, so we are finding lots of good, idiosyncratic stories. One of these is Netflix, who are a company whose bonds we bought when they came to the bond market to fund their expansion of content. And as they've gained more subscribers and revenues have picked up, then they've hit that cash flow positivity point faster than we expected and are beginning to deliver. The bonds are getting upgraded and the prices are rising. So although the overall backdrop for bonds may be less supportive than it's been in the past, we're still finding lots of attractive, idiosyncratic stories.

LH:
Iain, Stephen talked just then about the fact that the fund has been around for 34 years. It's seen plenty of trends and themes come into the marketplace over that period. The three letters on everybody’s lips at the moment: ESG: environmental, social governance factors. How do you think about those for the Baillie Gifford Managed Fund?

IM:
Oh gosh, it's a really hard one to answer Lucy. It's such an important topic, but actually, I'm worried about it in some respects because I'm worried that the box tickers are taking over. And that's really bad news because actually, this is a really important fundamental long-term trend. And as long-term investors, we've always considered it. But the trouble is, there are so many people talking about it, and what about action? So let me do something different. Let me put my mouth where our money is. So to illustrate that what I'm meaning is that we try to allocate our client's capital to areas where we think there are growth opportunities. So 10 years ago, the fund had 12 per cent of its assets in the oil and gas sector. Today, it's 2.5 per cent. That's a huge drop. Now why is that? Well, because Steven and I and our colleagues are struggling to find the growth opportunities in that area. So we have divested and we put it into other areas.

LH:
That's a really great example. It really brings to life what we're doing with the Baillie Gifford Managed Fund. And perhaps you can add a little bit more to that in terms of engagement examples and perhaps the opportunities that you're finding as a result of these trends.

IM:
Sure. Well, Lucy, if you gave me a script, I'm sure I'd be talking now about lots of worthy the engagements we're having with companies and, you know, blah blah blah and box ticking. We do engage a lot with companies, we've always done that and we do in an integrated manner with our ESG experts. So we think that's very, very useful. I'm not I'm not knocking that at all. But I do believe that that is not everything that's to do with ESG because a lot of people think about ESG as risk. We don't see it like that. We think about ESG opportunities. So let me give you an example of that. We've owned for a number of years a stock in the portfolio called NIBE, which is a Swedish business that makes heat pumps. Now, I'm sure, Lucy, you've seen in the news recently that heat pumps are suddenly come to the front of the agenda as people are now talking about getting rid of gas boilers by 2035 and so on, and people are fretting about how that's going to work. Now what I see as a growth investor is the fact that in the UK, for example, we've virtually got no heat pumps.

We're going to have a heck of a lot more heat pumps over the next 20 or 30 years. That's a great growth market. And for NIBE, the UK is a small country. It's got the whole world to pick from because outside Scandinavia, nobody's really got heat pumps.
So there is a huge opportunity for growth there.

LH:
Over the long term, performance has been absolutely excellent. There has been a bit more volatility in the short term. Volatility is an inevitability when investing, particularly in equities and without wishing to dwell too much on the short term, I think a lot of people would find it quite helpful to get a sense of the outlook from here. So, Iain, back to you. Could you talk a little bit about how you're challenging the ongoing investment case for holdings in the portfolio?

And indeed, perhaps just touch on how we think about valuation?

IM:
Sure, first of all, can I reassure clients that we don't dwell in the short term. We are resolutely long term in our approach, but valuation is incredibly important, and we do think of it differently to a lot of people. It's not about setting a price target and then when it gets that price, we sell it. It's a much more dynamic process. What we're trying to say is at any point in time when we do a review of a company, where's the upside from here? Can we see that business growing significant over the next five years? And a good example of that process in action recently was Amazon, which used to be one of our biggest holdings in the fund. And when we did that review process, we found that actually, although there's still growth potential in Amazon, we don't think it's quite as much as it used to be. And add on top of that, the significant management change that Jeff Bezos, the founder of Amazon, is now stepping back as chief executive, we decided to reduce our holding. But the other thing I think is very important is the opportunities we're still finding in the fund.

And Lucy, I bet you and I never thought we'd ever be talking about Marks and Spencers in the Baillie Gifford Managed Fund because we've never owned it in the fund for over 20 plus years.

Why was that? Well, because it wasn't a growth business, but we think that might be changing now.

And that's really quite exciting because it got the food business, which has always been good and they've got the Ocado joint venture now for delivery, which I think is a tremendous growth opportunity. And you never know, maybe the clothing business is finally turning around under new management, so that's really exciting.

LH:
And Steven, you've already talked a little bit about the opportunities that are available at this point in time for fixed income. Perhaps you can bring this all together from a whole portfolio perspective to give a sense of the outlook from here and answer that question of are you optimistic?

SH:
Well, Lucy there’s so much doom and gloom about, whether it's about covid or to do with inflation or climate change. Now, don't get me wrong, these are big challenges and I don't want to make light of them. But I see these challenges as an opportunity, an opportunity for companies to help meet those challenges and bring us the solutions that we need to get through these problems. We're seeing lots of exciting ideas, an example would be in health care, innovation and health care, a company called Recursion Pharmaceuticals, and it's using machine learning to develop new ways of discovering drugs, which is really exciting and potentially transformational.

We've also got a company, Ashtead, which we have held for a long time. With really good management and a great growth story, it is still very exciting, even though it's been around for a long time. Now balancing those exciting equity ideas, we do have our best ideas, global bond portfolio and allocation to cash, so lots of reasons to be optimistic. And I think that's why we people refer to the Baillie Gifford Managed Fund as the one-stop shop for the best ideas in equities and bonds which Baillie Gifford has to offer.

LH:
Well on that optimistic note, thank you both so much for your time. And thank you to you for watching as well. If you'd like to find out more about the fund, there's plenty of information available on the website, as well as ways for you to get in touch.

Annual Past Performance to 30 September Each Year (%)

	2017	2018	2019	2020	2021
Baillie Gifford Managed Fund	13.9	13.3	3.6	26.9	16.5
IA Mixed Investment 40-85 per cent Shares*	9.1	5.4	4.5	-0.5	16.8

Performance source: StatPro, FE, total return in sterling.
*IA Mixed Investment 40-85% Shares Sector.

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The manager believes an appropriate comparison for this Fund is the Investment Association Mixed Investment 40-85% Shares Sector median given the investment policy of the Fund and the approach taken by the manager when investing.

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The fund's share price can be volatile due to movements in the prices of the underlying holdings and the basis on which the fund is priced.

Bonds issued by companies and governments may be adversely affected by changes in interest rates, expectations of inflation and a decline in the creditworthiness of the bond issuer. The *issuers of bonds in which the fund invests, particularly in emerging markets, may not be able to pay the bond income as promised or could fail to repay the capital amount.*

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