

# Philosophy and Process



*Worldwide Discovery*

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# Baillie Gifford

*Since 1908, when Baillie Gifford was founded as an investment partnership, the firm has been wholly owned by the people who look after and invest for our clients.*



Through each successive generation of partners our single focus on generating superior, long-term investment results for our clients has been the bedrock of our growth.

## **Partnership defines us**

The absence of external shareholders allows us to put our clients' needs first. It brings stability and a long-term time frame to everything we do in our business, whether choosing the best investments for our clients' portfolios or continually investing in the firm and developing our people.

Our partnership structure brings freedom from short-term pressures, allowing us to be truly active investors. Portfolios are shaped by where the best investment opportunities lie, rather than where the index dictates. We encourage a strong culture of inquisitiveness, debate and respectful trust in which our investors are nurtured and thrive.

## **Our investment approach**

### **Curious about the world**

The best investment ideas spring from analysis of future possibilities, not short-term probabilities. Our research covers the globe. We set no barriers to the scope of our research, encouraging fresh perspectives and the use of diverse sources of information.

### **Fundamentally driven**

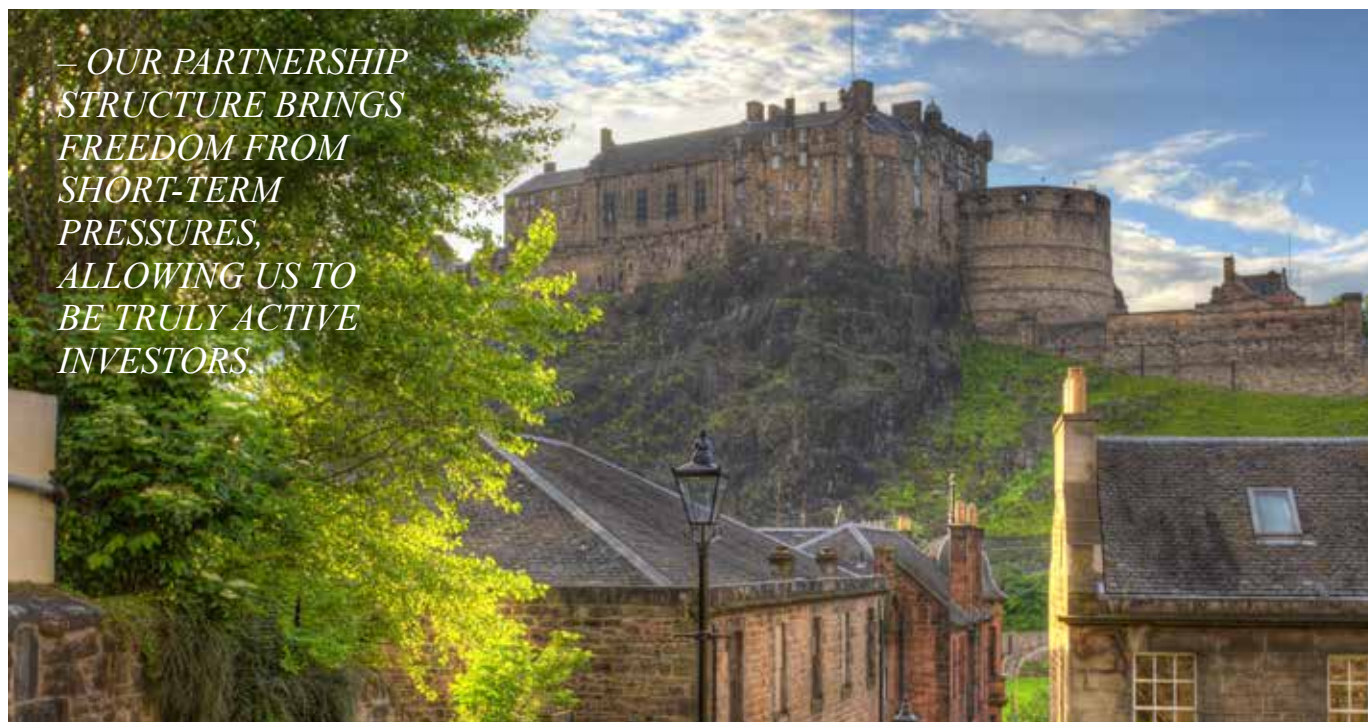
The world is complex. We believe that the way to generate long-term returns for our clients is to focus on identifying and investing in those companies which have the potential to grow at a faster rate, on a more sustainable basis, than the market believes.

We conduct rigorous qualitative research to establish whether prospective investments have the competitive, financial, and strategic advantage to deliver on that potential.

### **Collaborative research**

We like to share. Investment ideas are discussed and debated across our investment teams, from those of the most junior analysts to partners of the firm. We are always looking for that novel insight, offbeat observation or penetrating challenge to enhance our collective understanding. There are no enduring right answers in investment, so we never stop asking questions.





– OUR PARTNERSHIP  
STRUCTURE BRINGS  
FREEDOM FROM  
SHORT-TERM  
PRESSURES,  
ALLOWING US TO  
BE TRULY ACTIVE  
INVESTORS

### **Global perspective matters**

Companies increasingly operate in a global environment – it is not sufficient to consider investment opportunities in isolation. We also need to understand their competitive positions and underlying attractiveness against their international peers. Having nearly all of Baillie Gifford’s decision makers in one building enables us to easily share perspectives and debate issues – the constant flow of formal and informal investment discussions allowing us to draw together all the pockets of expertise that reside in our investment teams. We further ensure a global perspective by occasionally moving individuals between these teams: we value breadth of perspective and experience over narrow specialisation.

### **Clients come first**

Baillie Gifford is solely an investment management company. We close our investment strategies to new clients before we gain too many assets to reasonably manage, and we keep our business simple so that we can focus on investment activities. Client relationships are handled by members of our highly experienced Clients Department, who oversee all aspects of delivering our services to clients, ensuring that investment managers are free to concentrate on investment issues.

# Introduction to Worldwide Discovery

At Baillie Gifford, we have enjoyed significant success over the last century by identifying and owning shares in growth companies; that is, companies which grow their profits at an above average rate over the long term. We have observed that some of the best growth opportunities are in smaller stocks: early stage businesses with the drive, energy and entrepreneurial spirit to transform their own fortunes. Worldwide Discovery is our way of capturing these opportunities.



# Investment philosophy

The universe of smaller companies is vast – perhaps 50,000 globally – and exciting, because it may contain the winning companies of the future. Worldwide Discovery aims to produce superior long-term returns by investing in a portfolio of these smaller, immature companies with significant growth potential.

The opportunity for superior returns arises because:

- We routinely observe that *it is the less mature, more entrepreneurial companies that shape the evolution of an industry*. It is striking how little innovation originates directly from large businesses, and how often bigger corporations are bad at dealing with change. Size and market dominance

often create a formidable barrier to competition, but the cultural baggage and management dislocation that inevitably builds can be a significant impediment to the necessary evolution of a business.

- Smaller companies are therefore interesting not because they are small, but rather because *the stage of development of their business can offer significant upside potential* with regards to profit growth and, ultimately, share price appreciation.
- *Bottom-up research is at its most valuable* when assessing immature businesses. The businesses are often simpler and yet it is typically during this early stage that the market's understanding of a company's growth

potential is at its least developed.

- *Inefficiencies and valuation anomalies* are more common further down the market cap scale.
- *Our style of investment is well suited*, first, to identifying interesting businesses early in their development and, subsequently, backing them with a long-term investment horizon and ability to look through short-term volatility.

We focus our new idea generation on investment opportunities in companies with a market capitalization of \$10bn or below.

# Investment process

## Opportunity set

We estimate that there are roughly 15,000 smaller companies that are of sufficient size and liquidity for us to invest in.

We cannot cover all of these stocks, and indeed we have no desire to – Worldwide Discovery's performance will be driven by what it owns rather than what it does not. Instead, we focus our efforts on businesses which we believe will benefit from a combination of:

1. *a structural change in the company's market backdrop*, be it due to societal change, technological change, demographics or environmental issues/ imbalances (e.g. food, water, clean energy).
2. *the company's response to such change*, through innovation, the use of (sometimes disruptive) technology, or a new business model.

We quickly, qualitatively, screen out stocks that we do not believe exhibit both of these characteristics. This leaves us with a more manageable universe.

We consider approximately 500 stocks per year, which are more than sufficient potential investments for the ultimate portfolio of around 50–75 names.



# Idea generation and portfolio

## Idea generation/stock selection

At Baillie Gifford we are 'bottom-up' stock pickers, and our investment effort focuses on understanding the fundamental drivers of individual businesses' long term earnings trajectory. Company analysis is critical to this end and we concentrate on evaluating three key criteria.

- a) The size and scope of the growth opportunity that the company being considered may benefit from
- b) The tools the company has in its arsenal to exploit this opportunity. This focuses on product/service excellence, competitive edge and an assessment of management calibre and incentivisation
- c) The quantum of investment upside that we believe the company's equity offers, with consideration over the timeframe of achievement

We typically produce regular in-depth reports which focus on the above criteria and are subject to peer group review at a formal stock discussion. The purpose of this discussion is for the researcher to present the investment idea to the whole Worldwide Discovery Team, (see page 10 for team details). Team members are generalists and there are no geographical or sector constraints on what stocks the team can consider – we want our horizons to be as broad as possible.

## Portfolio construction

Stocks under consideration for inclusion in the portfolio are discussed by the Worldwide Discovery Team. While Douglas Brodie, head of the team, is ultimately responsible for portfolio decision making, we actively encourage an environment that gives individual analysts a high degree of influence and, at the portfolio level, accommodates for tentative, individually higher risk stock ideas.

Once purchased, each holding's operational performance and valuation are continually monitored. In addition, the team conducts a regular collaborative portfolio review.

We believe that size is a fairly poor guide to immaturity. Consequently, we would expect some of the companies held to grow to \$10bn and beyond. Should this occur, we would not look to sell the holding on size reasons alone, instead preferring to sell based on our assessment of a company's fundamentals and valuation.

## Portfolio structure

Worldwide Discovery holdings will, by their nature, offer a wide range of potential outcomes. We aim to embrace this uncertainty and believe it is important that the portfolio is:

- i) adequately diversified by name and thematic influence; and
- ii) sufficiently broad so as to be open to the inclusion of new ideas.

Hence, the portfolio consists of 50–75 stocks, with holding sizes typically 0.75%–3% at time of purchase determined purely by investment merit.





# Risk controls

The type of stocks we want to own – early stage or with significantly changing business models – will be individually risky. We therefore seek to mitigate overall portfolio risk, which is the risk of permanently losing clients' capital, by focusing on portfolio diversification. This allows us to accept volatility in single stocks while attempting to limit it at the total portfolio level. The key controls are:

- we will hold 50–75 stocks;
- a minimum six countries will be represented at all times;
- a minimum number of 10 industries will be represented at all times;
- a minimum effective number of 25 holdings\*.

Worldwide Discovery will likely exhibit greater shorter-term volatility than a typical equity portfolio (i.e. the annual standard deviation of returns will likely be higher than that of an 'all cap' global equity index).

\*The effective number of holdings is a measure of diversification based on the number of holdings in an equally weighted portfolio that would have the same level of diversification. The effective number of assets in a portfolio is arrived at by squaring the weighting of each holding, adding them up and calculating the reciprocal number. For example, if we have a 100 stock equally weighted portfolio then the effective number of stocks is also 100. However, using the rules outlined above we can see that if one holding was 10% of the portfolio and the other 99 holdings were equally weighted, then the effective number of stocks would be 55. The effective number of industries represented is calculated using a similar methodology.

## How should we be judged?

The aim of the strategy is to provide superior long-term returns. An appropriate benchmark may be the S&P Global Small Cap Index, MSCI All Country World Small Cap Index or the FTSE Global Small Cap Index, but comparisons with these indices are only expected to be meaningful over periods of at least five years.



# Biographies

INVESTMENT TEAM BIOGRAPHIES



**Douglas Brodie**

Douglas joined Baillie Gifford in 2001 and is Head of the Global Discovery Team. Douglas became a Partner in 2015 and is a CFA Charterholder. He graduated BSc in Molecular Biology & Biochemistry from the University of Durham in 1997 and attained a DPhil in Molecular Immunology from the University of Oxford in 2001.



**Zaki Sabir**

Zaki joined Baillie Gifford in 2007 and is a Senior Analyst in the Global Discovery Team. He has also been a member of the Global Stewardship Team since 2017. Zaki graduated BA in Business Accounting and Finance from the University of Newcastle in 2006.



**Svetlana Viteva**

Svetlana joined Baillie Gifford in 2012 and is an Investment Manager in the Global Discovery Team. She is a CFA Charterholder. Svetlana is also a Deputy Manager of our global small cap investment trust, Edinburgh Worldwide Investment Trust. She graduated BA in Economics and BA in Business Administration from the American University in Bulgaria in 2008, MSc in Investment Analysis in 2009 and PhD in Accounting and Finance in 2012, both from the University of Stirling.



**Robin Nelson**

Robin joined Baillie Gifford in 2016 and is an Investment Analyst in the Global Discovery Team. He graduated MEng (Hons) in Civil and Environmental Engineering from the University of Edinburgh in 2015.



**Luke Ward**

Luke joined Baillie Gifford in 2012 and is an Investment Manager in the Global Discovery Team. He is a Deputy Manager of our global small cap investment trust, Edinburgh Worldwide Investment Trust. Luke graduated MEng (Hons) in Mechanical Engineering from the University of Edinburgh in 2012.



**Josephine Hellberg**

Josephine joined Baillie Gifford in September 2017 and is an Investment Analyst in the Global Discovery Team, having previously worked in the International Growth Team. She graduated MSci (Hons) in Biological Sciences (Genetics) from University College London in 2013, MPhil in Biochemistry from the University of Cambridge in 2014 and DPhil in Physiology, Anatomy and Genetics from the University of Oxford in 2018.



**Georgina Huntridge**

Georgina joined Baillie Gifford as an Investment Analyst in 2019, working on the Japanese Equities and International Alpha strategies before joining Global Discovery. Georgina graduated BSc (Hons) in Chemistry from The University of Edinburgh in 2018.



**Fernanda Lai**

Fernanda joined Baillie Gifford in 2021 as an Investment Analyst in the Global Discovery Team. She graduated from Williams College in 2017 with a BA (Hons) in English and completed an MPhil in European, Latin American and Comparative Literatures and Cultures with distinction at the University of Cambridge in 2018.

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