Reflections

February 2022

'Equity markets will always remain volatile, myopic and unpredictable beasts. However, by trying to separate the long-term value of businesses from the inevitable short-term noise of events, we aim to create a portfolio which rewards our shareholders with outperformance over long-term periods of measurement. Writing this report in the midst of anxiety… [It] feels very much a time to try to ignore the noise.'

The above, from a 2008 LTGG commentary, still chimes today. The drawdown in the global financial crisis remains the largest in absolute terms in LTGG's 17-year history, but it is one of several drawdowns of at least 10 per cent over the years, as the table overleaf shows. The current period (c. -25 per cent so far), once we get through it, will feature high on the list.

Such drawdowns are the scars we wear. They are, for better or for worse, a necessary and essential part of a concentrated, high-conviction portfolio with a philosophy to which we will stick. The volatility might well be a feature of these companies and our portfolio as a result, in so far as they do not maximise for smooth, short-term outcomes, or otherwise make efforts to make themselves appear as if they are not taking risk.

As uncomfortable as such periods are, they haven't stopped LTGG creating value for our clients over the long term. This is because investing in era-defining companies, and exercising appropriate hold discipline, dwarf the impact of any drawdowns along the way.

In every case the core question is the same 'Has anything, other than share prices, changed?' and, if it has, 'What's the impact?'

Well, things have changed. The Federal Reserve is struggling for control in a complex environment, and the first real transition out of a stimulatory regime. Russia is waging war in Ukraine. Global supply chains are under pressure. Chinese regulation rumbles on. But will such things really affect the LTGG holdings in the long term?

It's not that such things 'don't matter.' We should mistrust people who say as much. Rather, it's that they are often not the most important thing in determining the collective value of the particular type of company we seek to invest in over our time-horizon.

For a very large percentage of companies there is a single largest determinant of their returns that is a given top-down factor. Commodity pricing, or rate behaviour, or political settlements. And when you combine them, you get real correlated risk. This is much less true for a certain kind of company over a certain horizon. These are the outliers. And it is these companies, we contend, that will drive policy over the long term, not the other way around.

What determines the value of these companies is their ability to execute on their vision and their ability to finance the growth to achieve those visions. We spend our energy evaluating those considerations. But, by way of example, does it matter for Meituan, CATL, ASML or NVIDIA over the next decade what the US rate environment is? Would a change in the federal funds rate have stopped the rise of Amazon or Tesla?

What matters and determines performance over our horizon are idiosyncratic visions. Whether people will still eat animal products. If battery technology reshapes human energy generation and storage. If south east Asia becomes as exciting and digitised as we believe it might. Or if these balance sheets are so strong they will enable these companies to seize massive secular opportunities even we cannot imagine. And, of course, if we're right that our founder-CEOs are as transformative and thoughtful as we believe them to be. These are the sorts of deep forces that power LTGG and the portfolio's performance over sufficient periods of time.

There is one way that short-term correlated drawdown events can negatively weigh on long-term outcomes for our clients. That is if we decide to lock-in drawdowns by selling clients' holdings in a panic. To lose our stomach, especially on the emerging companies. To join the sudden faddishness and diverge from our process.

Twice in the past five years NIO gave us opportunity to lock in massive losses – 50 per cent and 70 per cent respectively. But we retained confidence in the fundamentals, stress tested our investment case and exercised our hold discipline. NIO has gone on to deliver multi-bagger returns so far. This logic applies to the portfolio as much as it does to holdings.

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The occasional response is that a 'long-term trade is a short-term one gone wrong.' This is to ignore that there might be a certain art of investing in growth companies for the long term, and that art has very little to do with judging the timing or cause of sudden shifts in market sentiment. In other words, long-term outcomes and short-term results are often uncorrelated, and requiring of totally different skill sets. We don't trust those who suggest they can 'do both.' We stick to our time horizon and we stick to our process. We do one thing. This is our strength.

We started nostalgically, so let's finish with one more from the archive. This one is courtesy of Edward Hocknell, a former partner of Baillie Gifford, writing 10 years ago in his *How to invest in equities and stay sane*.

'…It is much easier to behave rationally if we do not believe that a fall in prices betrays some hidden horror. Similarly, a rise in prices does not mean that Santa Claus is on his way… The point is not that everything is irrelevant, but that most investors are too exposed to random buffetings by forces that have no more influence on their portfolios than the gale outside their windows (this is written in Scotland). They should wrap up.'

Absolute drawdowns in excess of 10 per cent in the LTGG portfolio from 29 February 2004 to 31 December 2021:

	Absolute per cent Drawdown	Date of Trough	Date of Peak	Peak to Trough (# of Months)	Drawdown Recovery (# of Months)
1	-55.2	28/02/2009	31/10/2007	16	26
2	-21.3	30/09/2011	30/04/2011	5	16
3	-18.0	31/12/2018	31/08/2018	4	11
4	-15.3	29/02/2016	30/11/2015	3	6
5	-12.5	30/09/2015	31/07/2015	2	2
6	-10.9	30/04/2014	28/02/2014	2	4

Important information and risk factors

Annual Past Performance to 31 December Each Year (Net %)

	2017	2018	2019	2020	2021
LTGG Composite	54.0	-1.6	34.1	102.0	2.4
MSCI ACWI Index	24.6	-8.9	27.3	16.8	19

Annualised returns to 31 December 2021 (%)

	1 Year	5 Years	10 Years
LTGG Composite	2.4	33.3	22.9
MSCI ACWI Index	19.0	15.0	12.4

Source: Baillie Gifford & Co and MSCI. USD.

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CM17521 LTGG Reflections Feb 22 IC 0322
Ref: 15702 10007587