BAILLIE GIFFORD | *Sustainable Growth*

Sustainable Growth – monthly bulletin

July 2023

In the latest Sustainable Growth quarterly letter, we discussed the importance of diversification within the portfolio. Poor performance in 2022 was driven by having excess exposure to what we describe as 'rapid-growth' names. These are typically early-stage companies, providing fast, transformative growth opportunities and scaling quickly. Often, they are creating new or redefining traditional industries. They performed exceptionally well for your portfolio during the Covid-pandemic. At its peak, close to three-quarters of the portfolio was weighted in such companies – familiar names including Moderna, Tesla, Amazon and Zoom. However, market sentiment changed when interest rates started to rise and concerns over the impact of higher inflation on younger businesses mounted.

While we have sought to temper exposure to these rapid growth names, we remain enthused about their longer-term growth opportunities, and they still make up more than a third of the portfolio today. The competitive edge of many of these companies stems from a combination of first-mover advantage, the ambition and vision of their founders, and high investment into leading disrupting technologies. The market has been sceptical about this category of companies over the past 12-18 months. However, sentiment has slowly been improving. July saw continued optimism from the broader market, perhaps catalysed by a drop in developed market inflation. Over the month, the top contributors to relative returns featured some of these rapid-growth companies. Detractors were primarily companies that reported disappointing first-half results. As such, your portfolio performed roughly in line with the index.

Topping the contributors is the programmatic ad-buying platform, The Trade Desk, which has had a strong start with its share price up 98 per cent year-to-date. In challenging macro environments, advertising is usually an early cost to be cut by companies. However, The Trade Desk has reported strong results despite this, and revenues have been growing by more than 20 per cent annually, with earnings before interest, taxes, depreciation and amortisation (EBITDA) margins having expanded approximately 10 per cent from 2019–2022. We view this as supporting evidence of the value that The Trade Desk's platform offers its customers at a time when advertising budgets are under pressure. The Trade Desk is a critical gatekeeper in the digital advertising industry, enabling targeted advertising in a way that protects consumers and maximises transparency over how data is used, with strong ethical guidelines that influence many other actors in the system. It continues to launch new product lines and platforms every one to two years, creating a growing list of attractive solutions that its customer base values.

Another top contributor is biotechnology equipment manufacturer Sartorius Stedim Biotech. While results were slightly dampened over the first half of the year versus the same period in 2022, management guided towards a rebound in customer orders from late Q3. It also completed the acquisition of Polypus, the leading provider of innovative technologies for cell and gene therapies, further adding to its solutions offerings. We believe this area will be a key driver to growth from here.

Online grocery delivery company Ocado also had a strong month. Its share price strengthened after it was announced that a three-year-long patent battle with AutoStore would be settled, with Ocado receiving £200m in instalments over two years. Its technology business has also announced profitability for the first time, and we continue to believe that it has a significant opportunity to improve efficiency, reduce waste and relieve labour shortages in the industry.

On the other hand, one of the top detractors is leading provider of industrial robots, Fanuc. Results were disappointing, driven by weakened Chinese demand. Fanuc operates in a cyclical industry, and we are considerate of depressed results when entering a downturn. While this is a factor that we continue to discuss, we believe there remain structural drivers to the investment case. Fanuc's customers in the automotive sector need to retool as they switch from traditional internal-combustion engines to power trains used in electric vehicles. This should boost the robotics business, and Fanuc has invested heavily in cobots (industrial robots that work alongside humans), putting it ahead of many competitors in an area of future demand.

And finally, after a stronger start to the year (share price up circa 80 per cent), music streaming platform Spotify's results were mixed. It posted its highest monthly average user growth in any previous quarter, but revenues lagged. And with price increases not impacting the income statement until later in the year, the market focused on the short term. Despite that, revenues were up 11 per cent over the period, and we are encouraged by the company's focus on efficiencies such as consolidating its real estate footprint, exiting Soundtrap (music creation tool) and reducing its headcount. These actions should enable it to refocus its investment on further evolving its mission to allow creative artists to 'live off' their art and provide billions of fans with the ability to enjoy and be inspired.

We have recently intensified our focus on improving the portfolio's diversification. Not only does this mean looking for a variety of companies operating across a range of industries and sectors but also companies addressing different societal challenges. Today, we are excited about the diverse names that the portfolio is exposed to, from transformative healthcare companies such as STAAR Surgical and Exact Sciences to infrastructure solutions providers such as Advanced Drainage Systems and platforms lowering barriers to entrepreneurship such as MercadoLibre and Shopify.

Performance

Annual past performance to 30 June each year (net %)

	2019	2020	2021	2022	2023
Sustainable Growth Composite	5.2	29.7	53.4	-45.2	12.7
MSCI ACWI	6.3	2.6	39.9	-15.4	17.1

Annualised returns to 30 June 2023 (net %)

	1 Year	3 Years	5 Years	Since Inception*
Sustainable Growth Composite	12.7	-1.8	5.3	10.4
MSCI ACWI	17.1	11.5	8.6	10.0

Annualised returns to 31 July 2023 (net %)

	Composite Net (%)	Benchmark (%)	Relative (%)
July 2023	4.0	3.7	0.3
3 Months	9.5	8.7	0.9
One Year	8.0	13.5	-5.5
Three Years (p.a.)	-3.6	10.9	-14.5
Five Years (p.a.)	5.9	8.8	-2.9
Since Inception* (p.a.)	10.8	10.4	0.4

Source: StatPro, MSCI

Benchmark: MSCI ACWI Index

Based on the Sustainable Growth composite, in USD

Global Stewardship was renamed Sustainable Growth in 2023. *Inception date: 31/12/2015. Past performance is not a guide to future returns

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