Long Term Global Growth

Reflections

January 2023

Shifting shades of grey

'At night, all cats are grey.' So runs the aphorism variously attributed to John Heywood's 1547 book of proverbs and to Benjamin Franklin. The witticism remains popular in Russia today – a macabre reflection on history perhaps, or on that wonderful flair for dark irony at which the Russian language so excels. It could apply too, sadly, to the catastrophe of Ukraine – a crime perpetrated by a fading clique of KGB paranoiacs driven by a deep hatred of supposedly 'Western' values, greed, and indifference to human life.

This commentary, though, is not about Russia. Nor should it be. And just as we are not Kremlinologists, neither are we macroeconomists, professional Fed-watchers, epidemiologists, constitutional law professors, or overnight experts on ChatGPT. We do strive to learn patiently from subject matter specialists (we think these are more likely to be found in academia than on Wall Street.) And we remind ourselves to be humble about what we don't know. However, our task is to seek out exceptional growth companies and hold them long-term. Not to provide a running commentary on the news of the moment. In our age of The Current Thing, we believe that long-termism and being generalists have become more important than ever.

An abundance of grey cats also accurately describes the current situation for growth stocks. Companies where the rewards lie in the future, often at the expense of profit now, all look equally colourless to the average market participant today. A startling example is the LTGG holding Ginkgo Bioworks. This leading synthetic biology company has swung from stock market darling to pariah. After pulling off one of the largest biotech IPO ever in 2021 and being valued at a peak of $27bn, it has rapidly fallen to $3bn (we bought a holding at just under $5bn.) And yet we know that synthetic biology will likely be critical to decarbonising some sizeable industries – from fertiliser to textiles – as well as helping Ginkgo's large pharmaceutical customers to rationalise R&D spend (just as Amazon's AWS freed large companies from the need to build expensive IT infrastructure in house, replacing a fixed cost with a variable one). We also know that Ginkgo's formidable $1.3bn cash balance – nearly half its market cap – provides it with a large safety cushion. And we see the business nearly doubling its active programs year-over-year with healthy revenue growth of 45 per cent. But, as far as the stock market is concerned, potential profit at scale in the future is of little interest. Ginkgo simply blends in with the other grey cats.

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Ginkgo's predicament is mirrored by an LTGG holding at a more mature stage of development: the electric vehicle (EV) maker NIO. The company went public in September 2018 and received a positive reception despite having delivered no cars and possessing a mere 5,000 firm orders for its flagship ES8 SUV. Fast forward three-and-a-half years, and the company is now at a run rate of 180,000 vehicles per year across three product lines. It is growing volumes by over 50 per cent per year in a market where green transport is a central plank of Chinese government policy, 80 per cent of EV sales come from domestic brands, and NIO has carved out an aspirational, premium position. And as the founder William Li reflected in a recent meeting with us, if NIO can succeed in the most competitive auto market in the world, then his plans to enter the European market should have a fair prospect of success. He sees NIO's innovative battery-swapping stations as a unique selling point. Yet the business's value has fallen close to the IPO level. NIO is another grey cat.

This is an environment that should excite us as growth investors. True, the history of LTGG shows that the outlier returns we seek on your behalf often come from surprising areas regardless of prevailing market conditions. Consider the medical robotics company Intuitive Surgical for example (7x return over 12 years), or the category-of-its-own luxury brand Hermès (30x over 17 years). But history also reminds us that many of the finest opportunities arise when others are fearful. Oftentimes these look obvious with hindsight. Our colleague Mark Urquhart recently recounted the tale of how, on returning from parental leave at the height of the Global Financial Crisis, Apple's shares looked so cheap that he had to double-check whether a stock split had occurred. The company delivered an 8x return over the following six years from purchase (…and another 5x after the eventual sale: we often scold ourselves for selling it too soon.)

The point here is not that we will get every call right or, worse, somehow believe ourselves to be infallible. We have always believed that making mistakes is an important element of the quest for outliers. But it is only by adhering resolutely to our investment philosophy as others run frantically in the opposite direction – or are distracted by the perennial urge to sermonise on The Current Thing – that we will identify those rare flashes of colour amid the many grey shades of the stock market night.

Important information and risk factors

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

	2018	2019	2020	2021	2022
LTGG Composite	-1.6	34.1	102.0	2.4	-46.4
MSCI ACWI	-8.9	27.3	16.8	19.0	-18.0

Annualised returns to 31 December 2022 (Net %)

	1 Year	5 Years	10 Years	Since Inception*
LTGG Composite	-46.4	7.9	13.2	10.5
MSCI ACWI	-18.0	5.8	8.5	7.2

*Inception date 29 February 2004.

Source: Baillie Gifford & Co and MSCI. US Dollars.

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