BAILLIE GIFFORD | *Long Term Global Growth*

Reflections

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The following is based on this paper by Dave Bujnowski from the US Growth Team.

It had to end sometime, and it's brutal. Thirteen years of outperformance of growth stocks has ended abruptly. Events ranging from war, pandemic-induced supply chain constraints, labour shortages and rampant inflation have left us wondering what's next. Do great growth ideas even still exist? Where will we find the next engines of growth?

As students of economics, we know the essential variables are demand and supply. Growth happens when supply of a product/service meets demand.

But what drives growth in the first place? We see three engines:

— **Expansionary**, whereby demand grows, and supply rises to meet it

— **Disruptive** growth, where supply innovates to meet existing demand better

— **Replacement** growth, where new demand supersedes the old following changes in the system

Have the engines that have driven growth over the past decade stalled? Have they changed? What will take us into the next decade?

Expansionary growth is driven by increased demand and innovation. Over the past decade, this growth has been driven by favourable economic conditions, globalisation and innovation associated with new markets and new business models. These new models are democratising and awakening demand by offering affordable or free products. Think software as a service, social media or searching for knowledge. Has this engine stalled?

We believe this engine can still drive growth, but it seems unlikely that the macroeconomic and global forces that powered expansionary growth in the past decade will have as much impact in the next.

We need to look to new democratisers and to the platforms capable of adapting to provide new tools for new users to do new things. Some of these new democratisers can be found in the metaverse, healthcare and agile software development.

The metaverse offers a virtual world where social media, online gaming, and ecommerce coalesce while promising a new canvas for users to create content. If expanding the reach of mobile 15 years ago helped create massive new markets, then what might the emergence of a new digital world such as the metaverse open?

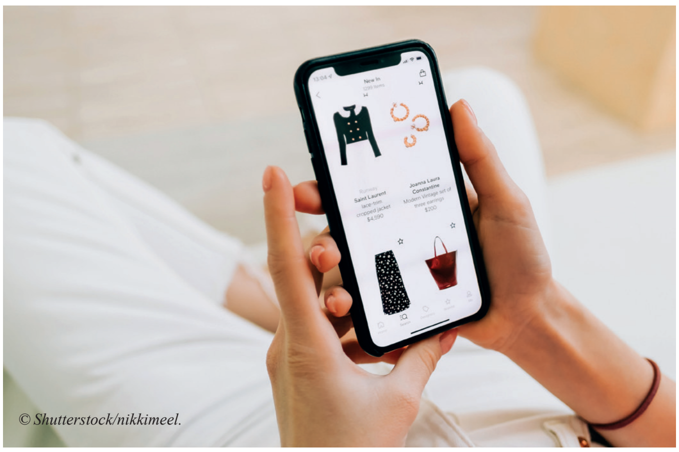
Data also represents a new tool that lets users do new things. Over the past decade, we have lived in a data-driven world, but now our relationship with data is changing. Much of the value had been confined to making existing businesses more efficient. Now its impact can be found in life sciences, healthcare and synthetic biology, where problems are solved increasingly by data, not science. These are examples of how expansionary growth is unleashing human creativity irrespective of globalisation and economic conditions.

In disruptive growth, it's not essential for demand to grow, but that supply innovates to meet it in new, better ways. We have seen this in ecommerce, cloud infrastructure and electrical vehicle adoption. Ecommerce has changed how we shop – a single click vs a trip to the shops. The shift has been dramatic, with ecommerce more than doubling as a percentage of retail in the past 10 years. We have seen cloud adoption begin to dwarf investment in traditional datacentres and electric vehicle sales increasing 50-fold in the past decade. This illustrates how technology-based shifts fuel disruptive growth.

Over the past decade, disruptive growth has contributed mightily to growth investors' portfolios and it is still going strong. Not inflation, the Fed, nor recession can put the disruption genie back in the bottle. Nothing can prevent more commerce going online; more IT migrating to the cloud, healthcare becoming personalised and transport more electrified. The broader point is that this growth engine is not dependent on the growth of the system itself. Dynamic disruption is the trigger.

The final engine is replacement growth, where demand is not growing but changing. A result of dynamism within a system, a paradigm shift among participants and demand appearing that we might not have previously imagined. An example here is the changing attitudes about climate change and sustainability – there is a demand for clean energy that simply didn't exist 20 years ago.

In times of economic adversity, contraction doesn't prevent growth opportunities from arising. However, as a system contracts, expansionary growth engines may stall, but the pain points within the system shift, and with those shifts come new opportunities. Value accrues to those who control the scarce resource or can supply alternatives. Not that the companies who thrived amid abundance have suddenly seen their growth prospects disappear, but that scarcity brings new opportunities. Over the next few decades, as was true of the past, it's the companies that can invent the future that will succeed.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