

**SHINING A LIGHT ON THE.....
Baillie Gifford Global Discovery Fund**

AT A GLANCE

Investment Objective
The Fund aims to outperform (after deduction of costs) the S&P Global Small Cap Index, as stated in Sterling, by at least 2% per annum over rolling five-year periods. The Fund will invest at least 90% in shares of companies. The Fund will be actively managed and will invest in shares of companies in any country and in any sector which typically at the time of initial purchase have a market capitalisation of US\$10 billion or less and that the ACD considers will offer excellent future growth prospects.

Fund Factsheet Link	https://www.morningstar.co.uk/uk/funds/snapshot/snapshot.aspx?id=F0GBR0506N
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Management	
Manager Name	Start Date
Douglas Brodie	3 May 2011
Luke Ward	1 January 2018
Svetlana Viteva	1 January 2018

FUND PERFORMANCE

Performance from 1st January 2016 to 31st July 2022:

	2016	2017	2018	2019	2020	2021	2022
Baillie Gifford Global Discovery Fund	9.81%	30.94%	3.97%	23.00%	75.44%	-21.20%	-32.29%
S&P Global Small TR USD	32.73%	13.51%	-9.05%	20.39%	12.57%	16.40%	-6.09%

Performance over 12 months, 3 years, 5 years and since lead fund manager:

	1 year	3 years	5 years	Since lead fund manager
Baillie Gifford Global Discovery Fund	-42.65%	-10.92%	33.42%	239.30%
S&P Global Small TR USD	-2.62%	22.42%	43.92%	191.05%

You should note that past performance is not a reliable indicator of future returns, and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced.

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Tracking Error	Information Ratio	Active Share	Upside Capture Ratio	Downside Capture Ratio	Batting Average	Beta	Alpha	Equity Style
22.90	-0.46	-	106.35	168.68	52.78	1.05	(8.94)	Growth / Small

Volatility Measurements	
3-Yr Std Dev (volatility)	29.57%
3-Yr Mean Return (average)	-3.78%

Investment Style Details	
Giant	2.43%
Large	7.48%
Medium	39.42%
Small	39.78%
Micro	14.90%

Top 5 Holdings – 101 Equity Holdings		
Anylam Pharmaceuticals Inc	Healthcare	6.42%
Staar Surgical Co	Healthcare	6.12%
Ocado Group PLC	Consumer Defensive	4.08%
MarketAxess Holdings Inc	Financial Services	3.23%
Upwork Inc	Industrials	2.97%

Top 5 Sectors	
Healthcare	41.60%
Technology	27.68%
Industrials	9.70%
Consumer Defensive	5.93%
Financial Services	5.68%

Top 5 Regions	
United States	67.98%
United Kingdom	13.97%
Asia - Emerging	5.73%
Europe ex Euro	2.68%
Japan	2.47%

UPDATE....

This fund has had a difficult 18 months and it has led to questions over whether it remains a viable investment. This update includes an update from the manager and two specific questions we raised with the team. There are two potential areas of concern for us. The first is the earnings position of the holdings, and the second is the “tail” of holdings. In terms of the tail, the fund has several holdings where the position is around 0.2%.

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The response to these questions is summarised below:

Tail

There are around 15 to 20 names where the position is less than 0.20%. They argue that having these holdings provides them a foothold in these businesses, and therefore can improve access to company management.

A key aspect of the philosophy is to be patient long-term investors. This means the strategy will hold early-stage, immature businesses which are using innovation to disrupt large markets or create new ones. The process can take years and therefore these holdings can be extremely volatile. They don't overly manage these positions, however they do formally re-assess the original investment case against recent operational progress and valuation. This can lead to them selling out of positions. The last review was in Q1 2022, and they removed 8 holdings where their conviction had lessened.

Our observation is that investors need to be aware that this is part of the process and therefore carries greater volatility and risk. The aim is that some of these will become key holdings in the future.

Earnings position of holdings

The concern raised by investors is that cash will be less plentiful in this new environment, and therefore if companies need to go back to markets for more they may struggle to do so.

The team have reviewed the current funding position of the companies they hold and around 70% have net cash on their balance sheets. They have also run cash burn rate analysis and they believe these companies have sufficient cash to sustain the businesses for a significant period.

Over 60% of the weighting of the portfolio is generating positive cashflow or earnings. This can change, but they believe this is a positive figure to focus on.

Of the 40% not generating positive earnings or cashflow, this is split into three categories:

Execution phase - the business's core offering is de-risked but not mature, and they may be considering additional adjacent or emerging opportunities. They have developed a solid revenue base (i.e. >\$400m annually). The balance sheet has reached a point of maturity and visibility that can tolerate decent levels of debt.

De-risking phase - the core proposition is emerging, and there is evidence of it resonating with users/consumers. However, the business still has meaningful de-risking events/ milestones to be navigated. The overall footprint remains small compared to the total addressable market. The business is likely generating some revenue (i.e. \$50m-\$400m), but required investment skews earnings and cashflows negative.

Fledglings - earliest stage companies. These are likely pre-material revenue, but intrigue on potential and progress hints at possible de-risking. They remain in a cash consuming stage of growth and will likely require further rounds of funding.

Around 30% of the portfolios holdings are at early stage, and may need further funding to maintain operations, and only a handful have net debt.

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Our observation is that investors should be aware that around 30% of the portfolio may need funding in the future. This could create volatility / risk if that funding is not forthcoming. However many of these holdings are likely to be in the tail which is reviewed so the hope would be that the team would identify concerns and remove before the issue becomes too acute.

In terms of the fund manager meeting, we have put some notes below.

The lead manager has been running this for ten years plus. Clearly the recent performance has been difficult for the team, and they are certainly keen to reassure investors that the future remains bright. The underperformance over the last 18 months has meant that its track record has gone from exceptional to poor. They highlighted in this period that they have been able to invest in companies they have wanted to hold, but the valuations were too high.

The strategy ultimately is looking to invest in companies that are looking to solve big problems. Early investments are likely to be experimental and often unproven. As a direct result of this approach around 20 / 30 ideas will deliver the bulk of the returns. They are happy to hold the winners so there will be some large cap exposure.

This period has been difficult for them and they stress that they are not economic forecasters. They focus on businesses that dictate their own future. These should weather different cycles because they are delivering solutions, and the issues they are tackling are not going to go away. Ultimately these businesses are delivering real structural growth and exploiting ways to make things improve. They should in theory succeed because they are delivering scalable efficient answers to challenges, we are all facing.

A brief summary of what the top-5 do:

Alnylam Pharmaceuticals Inc - biopharmaceutical company focused on the discovery, development and commercialization of RNA interference therapeutics for genetically defined diseases

Staar Surgical Co - designs, develops, manufactures and markets implantable lenses for the eye with companion delivery systems.

Ocado Group PLC - is a technology-led global software and robotics platform business providing a unique end-to-end solution for online grocery around the world.

MarketAxess Holdings Inc - is the leading fixed income electronic trading platform for institutional investors and dealers.

Upwork Inc - connects businesses with independent professionals and agencies around the globe.

In summary, the question is what an investor gets by investing in this fund, and ultimately are they rewarded for this? In terms of what they get, that is access to small and emerging companies that are tackling the big problems faced by the world today. This is not a "green" fund and therefore solutions go across different sectors and geographies. By the nature of the investments these are speculative and volatile.

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The aim is that some of the early-stage investments will become a significant part of the portfolio in the future but the journey to achieve that will be far from smooth. Our view remains that if an investor goes into this with open eyes and is prepared to have this as a long-term investment, then, in theory, they should be rewarded. However the journey will not be smooth and is likely to at points lead to investors questioning whether to continue holding.

The source of information in this note has been provided by Baillie Gifford and is correct as of August 2022. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to decide based on these notes we cannot take responsibility for this, and you should carry out your own research before making a decision. We would also recommend that you receive advice before following up on any decision.