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SUSTAINABLE GROWTH: OWNER'S MANUAL

TOBY ROSS AND KATHERINE DAVIDSON

For Sustainable Growth our principle is that investing in companies which deliver enduring good could also deliver enduring growth, write investment managers Toby Ross and Katherine Davidson



Many of the companies we most admire have a clear and simple purpose, an essential ambition that explains why they exist and guides how they will succeed.

As we set out as managers of the Sustainable Growth strategy, what is ours?

TWO FUNDAMENTAL BELIEFS

We believe that:

- companies capable of **sustaining profitable growth over a genuinely long time horizon** will make the best investments
- companies can be a force for good, **making a difference to society through what they do or how they do it**

These two beliefs underpin the purpose of Sustainable Growth: to invest in enduring growth companies that deliver enduring good.

MAKING A DIFFERENCE?

Typically, when people think about a company's influence on society, they think about its products and services, ie what it does. The companies that provide new and transformative medicines or technology that help cut costs and emissions.

But companies can also make a difference through their behaviours, the choices they make about how they run their businesses, ie how they do it. Firms that show leadership in addressing a challenge can help raise standards across their industry and the wider economy, making the world a better place. This is less obvious but can be just as significant.

Companies that make a difference, either through what they do or how they do it, will be long-term winners. Either their products will fulfil an unmet need and contribute to solving a global problem, leading to growing demand. Or their distinctive culture and behaviours will allow them to tackle problems more effectively than their competitors, leading to market share gains.

VIRTUOUS CIRCLES AND ENDURING GROWTH

How does this translate into shareholder value? Admittedly, in the short term, a company's societal impact is unlikely to make much difference to economic outcomes. At times there may be a direct conflict between what helps society and what helps short-term profits. Investing to reduce the environmental impact of your supply chain or increasing benefits for your staff will inevitably eat into today's earnings, prompting ire from many shareholders.

But over the longer term, a virtuous circle emerges. Businesses that show leadership in how they treat stakeholders will strengthen their competitive position and, thereby, their growth prospects. For example, they may become an employer of choice, command unusual customer loyalty, or experience a lower impact from carbon pricing. This economic success will, in turn, increase their ability to make a difference to society, both via their growing share and the likelihood of industry peers following their example.

But most investors don't stick around long enough to see this play out. Attention spans are getting shorter, with average holding periods measured in months rather than years. To benefit from these virtuous circles, we, too, need to do things differently. That's why we invest with a ten-year time horizon.

To buy and hold with a ten-year view requires a very high degree of conviction in our investee companies. This is where our focus on enduring growth comes in. What differentiates a great company from a merely good one is its potential over the genuinely long term, whether it is capable of delivering meaningful growth over five, ten years and beyond.

These great companies share some common traits: a significant market opportunity, a competitive edge that helps them to win in an increasingly complex world, the resilience to ride out cycles and shocks, and leadership that can take the long view and 'think around corners'.

That's the key to Sustainable Growth. We work hard to find the best opportunities, then stand back and let the wonder of compounding play out.

HOW WE DO IT: OUR PRINCIPLES

- **Long-term focus.** This is our most important advantage and is embedded in every aspect of our approach. We are privileged to be supported by an investment-led partnership and clients who share our time horizon.
- **Opportunity-driven.** The best investors are natural optimists. The core of our philosophy is to look for opportunities to improve the status quo.
- **Act as owners.** Our time horizon allows us to build genuinely collaborative relationships with investee companies. We will use this to support their success however we can – including by offering supportive challenges.
- **Materiality matters.** Our edge is in the quality of our research, analysis and debate and our desire to understand the businesses we invest in truly. We spend our time on issues material to the future success of investee companies, not seeking to tick boxes, which dictates our engagement.
- **Full transparency.** We will communicate to our clients in the same way that we would want from companies. We will be clear about how and why we make decisions and be honest when we get things wrong.

HOLDING US TO ACCOUNT

We ask clients to judge our progress in three ways:

- **Investment performance.** We believe that finding sustainable companies will help us to deliver returns that are meaningfully better than broad equity indices. We aim to outperform our benchmark by 2% net of fees over rolling 5-year periods.*

- **Whether portfolio companies are making a difference.** Our investment case always contains a ‘theory of change’, including evidence that would support or challenge our hypothesis. We won’t always be able to demonstrate this quantitatively, but we commit to appraising our investments with humility and integrity – and to sharing the results.
- **Whether we are making a difference.** Specifically, through our engagement activity. Again, this will be hard to quantify, and we will not confuse process (votes cast, letters written) with outcomes (a change in the real world).

SUSTAINABLE GROWTH, BEYOND ESG

Ultimately, what makes companies outstanding, and potentially great long-term investments, is when they do something different from the pack – to innovate, influence others, and shape their industries. When they make a difference.

Similarly, we won’t be able to deliver outperformance unless we do something different from our peers. We believe our approach is a more useful lens than the conventional approach to ‘ESG’, which is increasingly focused on compliance with minimum standards. We prefer a forward-looking approach that focuses on matters critical to a company’s success rather than trying to tick every box.

This is a road less trodden, but we believe it will make our journey more meaningful and rewarding for our clients.

Toby Ross & Katherine Davidson

*Sustainable Growth Benchmark = MSCI ACWI.

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Toby is an Investment Manager on the Sustainable Growth Team, and will become a Baillie Gifford Partner in May 2023. He first joined Baillie Gifford in 2006 as an analyst on the UK equities team. He joined the Global Income Growth team as an Investment Manager in 2013, and in this role he helped to develop the team's approach to responsible investment. He became the Joint Manager of The Scottish American Investment Company PLC (SAINTS) in 2017. In 2022, Toby assumed the leadership of the Sustainable Growth Team. He graduated MA in English Literature from the University of Cambridge in 2006 and is a CFA Charterholder.

KATHERINE DAVIDSON

Investment Manager

Katherine is an Investment Manager on the Sustainable Growth Team. Before joining Baillie Gifford in September 2022, she had spent her investment career on the Global and International Equity Team at Schroders. Katherine joined the Schroders graduate scheme in 2008 and held various sector and fund responsibilities while developing a growing interest and expertise in sustainable investing. Katherine was instrumental in the development and management of Schroders' Global Sustainable Growth Fund. She graduated with an MA in Philosophy, Politics and Economics from the University of Oxford in 2008 and is a CFA Charterholder.



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