

Baillie Gifford™

Global Alpha Paris-Aligned

Philosophy and Process



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Introduction

Global Alpha Paris-Aligned (GAPA) is a lower carbon variant of the established core Global Alpha Strategy. The portfolio offers a pathway for clients to align their assets with the objectives of the Paris Agreement, and namely the most stretching aspect of Paris, the 1.5C warming scenario (2050 net zero). It is managed by the same team as the core Global Alpha Strategy, with the same investment philosophy and performance objective.

However, GAPA has a guideline of having a carbon footprint lower than that of the MSCI ACWI EU Paris-Aligned Requirements index. This index, which maps the EU delegated acts on Paris-Aligned benchmarks, starts with a carbon footprint 50% less than that of the parent ACWI. It then decarbonises by at least 7% year-on-year – consistent with a trajectory for a 1.5C warming scenario outlined in the 2018 Intergovernmental Panel on Climate Change report.



Philosophy

GAPA is a long term global equity growth strategy that follows the same investment philosophy as the established Global Alpha Strategy. Stock selection is bottom-up with a focus on fundamental analysis. The portfolio, investing in approximately 90 stocks, is well diversified and boasts a high active share.

Our investment philosophy is to make long-term investments in well-managed businesses which enjoy sustainable competitive advantages. Our core belief is that share prices ultimately follow earnings. For this reason, we aim to select stocks that offer the prospect of sustainable, above average growth in earnings and cash flow. Our 'growth hurdle' is to look for companies which we believe have the potential to at least double over our five-year investment time horizon. We are patient investors; we believe we can deliver greater outperformance for our clients by assessing a company's prospects for sustainable growth rather than by predicting short-term share price movements or macroeconomic trends.

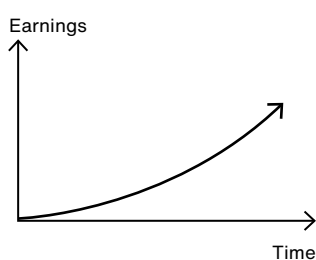
We have an open-minded approach to growth, recognising that companies can grow at different rates over different time lines. We are optimistic investors, seeking to embrace the diversity of growth opportunities available to us.

We place all the stocks in the portfolio in one of three 'growth profiles': compounders, disruptors and capital allocators. Our growth profile framework helps to ensure there is an appropriate diversity of growth across the portfolio. We expect companies in each profile to exhibit different characteristics and perform differently across the market cycle.

For each investment in the portfolio we construct a 'forward-looking hypothesis'. The purpose is to concisely lay out the core of the investment thesis and ensure a resolute focus on the progress of a company towards our long-term growth expectations. We continually retest the thesis as new information about a company arises and in context of the forward-looking hypothesis.

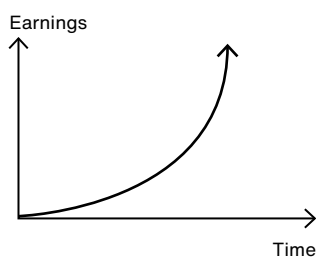
GAPA stock growth profiles

Compounders



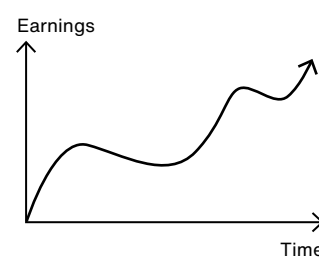
Durable franchise
Strong competitive advantage

Disruptors



Innovative disruptors
Vast opportunity

Capital Allocators



Skilled management
Structural growth

Process

The Global Alpha investment managers and analysts spend the majority of their time researching stock ideas. The team also leverages the work and experience of the wider Baillie Gifford research teams through our trusted advisor network, drawing on the stock ideas and insights generated by their individual teams. The advisors fall into two groups aligned with either disruptive or flexible growth strategies. Further research is then conducted on stocks which the Global Alpha Team believe may merit inclusion in the portfolio.

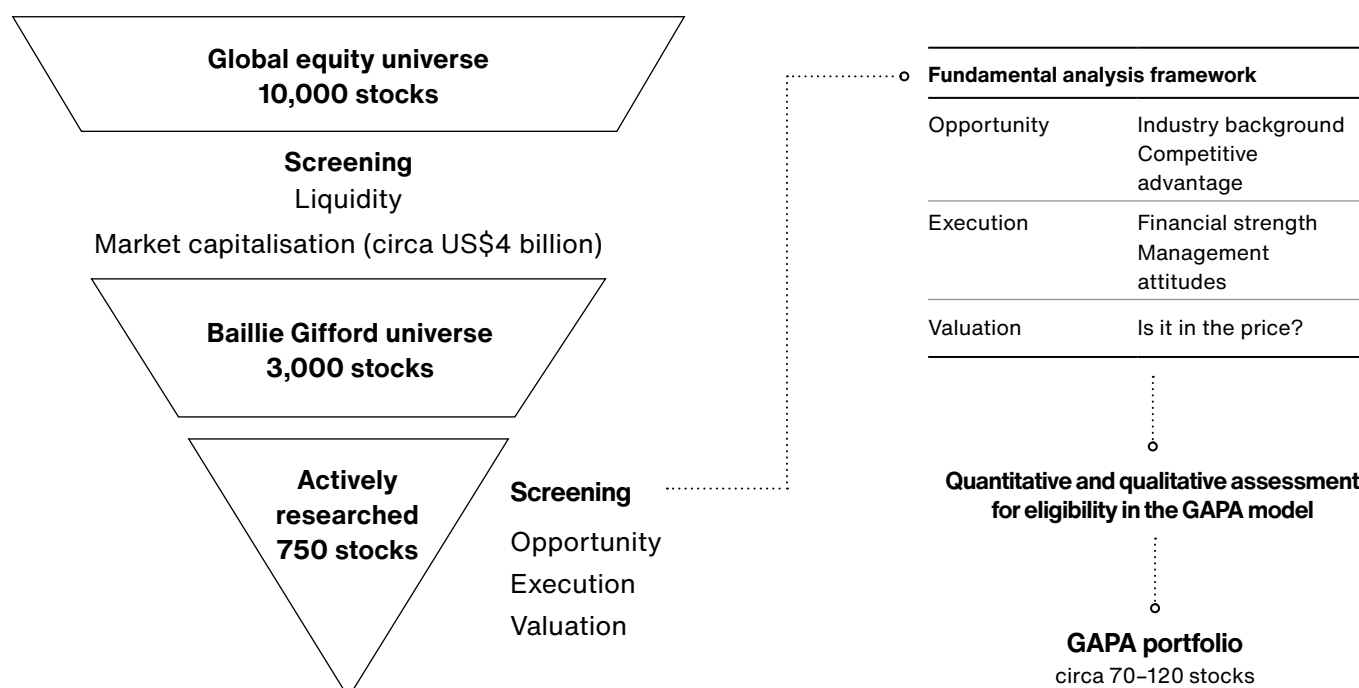
The Global Alpha Portfolio Review Group (PRG) consists of the three investment managers and dedicated analysts together with the trusted advisors. Occasionally, a topical guest from the broader Baillie Gifford investment floor may also attend to address specific areas of interest.

At the PRG meetings, which we alternate between the two growth groups and occur roughly every six weeks, all members show their enthusiasm for stock ideas by ranking the stocks that are currently in the portfolio and those that they think warrant inclusion in the future. Ideas are debated in a global context, and where more work needs to be done, the investment managers can either take this forward themselves or ask the advisors to undertake the work.

The qualitative examination of companies is critical to the company research and selection process. We have an extensive programme of company meetings and we aim to meet with all our major holdings at least once a year.

All the research undertaken at Baillie Gifford is generated internally, using a wide range of sources including the companies themselves. For every investment under consideration, we analyse three aspects – the opportunity available to the company, its ability to execute on that opportunity and the valuation of the business.

Research



Additional process for GAPA

GAPA applies a four-stage process to negotiate the pathway to net zero. The first stage is a quantitative screen that strips out companies engaged in both fossil fuel exploration and production as well as service provision to the sector.

This screen excludes companies that generate more than 10% of revenues from oil, coal and/or gas exploration, and those companies that generate more than 50% of revenues from services provided to those industries. Appropriate revenue thresholds are used to allow for the inclusion of businesses engaged in a transformational pivot to renewable energy.

As the portfolio is managed to support the goal of net zero GHG emissions, we go a step beyond applying a purely quantitative approach. Carbon intensive companies from other industries or sectors will remain within the possible investment universe, and as such, the strategy applies a qualitative screening process. The purpose is to identify those companies that, in our opinion, face significant challenges from the transition to a low-carbon future. The highest emitting holdings, or those involved in high emitting industries, are therefore subject to a further three-question analysis.

Does this company provide an essential product/service?

This question captures the idea of a carbon budget, accepting that not all emissions are equal. Some industries produce products and/or services that are essential, while others deliver products or services that are discretionary or only benefit a small group of people (e.g. cruise ships). Companies in the latter category are more exposed to climate risk.

Can emissions be mitigated in an economically viable way?

This question addresses whether products and services can be delivered in a better manner – specifically, if there are technologies which can significantly reduce the carbon intensity of a business in an economically viable way. Companies where green alternatives are readily available, feasible, and economic, are most at risk.

Is the company part of the problem or the solution?

We seek to understand how willing a company is to adapt and consider its part in the low-carbon transition. We take into consideration company policy, emissions reporting, and future targets. And we seek to understand how the company's carbon performance now and in the future might compare to others in the sector, as well as its alignment with the Paris Agreement.

We use frameworks such as the Financial Stability Board, Taskforce on Climate-related Financial Disclosures, and the Transition Pathway Initiative to assist our assessment.

Output

The outcome is a portfolio that is very similar to that of the core Global Alpha Strategy, with an overlap that ranges between 85-95%. However, this is a portfolio that is managed to support the goal of net zero GHG emissions by 2050.

Portfolio construction

The three investment managers, Malcolm MacColl, Spencer Adair and Helen Xiong, have ultimate responsibility for portfolio construction and performance.

Following debate within the PRG, the investment managers consider four questions of each potential holding when constructing the portfolio:

01

How does the stock compare globally?

Designed to assess how the business stacks up against its global peers. It may be the best investment in its home region, but could we do better by broadening our horizons?

02

Is it sustainable?

This question is deliberately broad, designed to identify any aspect of the investment case which may impact on a company's ability to compound growth many years into the future.

03

Where do we differ from the market?

Designed to establish whether the growth potential of the stock is already reflected in the share price.

04

What does it add to the portfolio?

Designed to seek out whether the stock is bringing a new theme to the portfolio (we are particularly keen to look for attractive diversifiers) or whether it is replicating an investment already held.

All three investment managers have an equal say in investment decisions, thereby ensuring that a majority decision is always reached. However, where one investment manager strongly disagrees with the other two, this will result in further work being undertaken in order to achieve broader agreement before any final decision is taken.

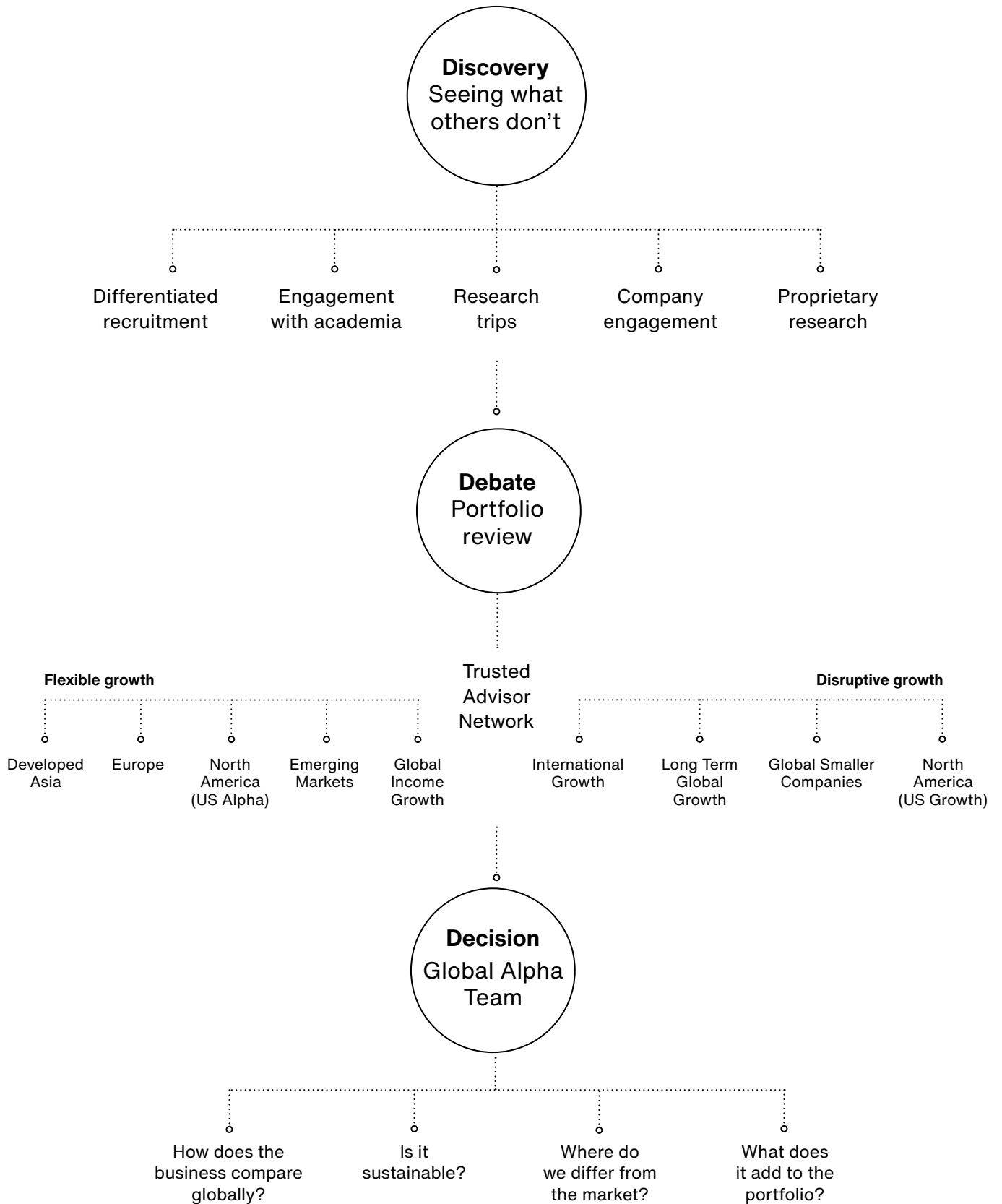
Careful consideration is given to the holding size of individual investments. We have three broad groups of holding size: circa 0.5% holdings, circa 1% holdings and circa 2%+ holdings. This is explained in more detail in the risk section of this document.

Our sell decisions are generated by frequent re-examination of our holdings. We particularly look for an adverse change in the fundamentals of the business, a loss of confidence in management or valuations where we think the market fully reflects our long-term view. Our 'growth profile' analysis also enables us to question whether a company is performing in line with our expectations and, if not, whether a sale is appropriate.

The structure of the PRG, which is strengthened by the knowledge of the trusted advisor network, ensures that we conduct timely reviews of stocks and that decisions can be implemented quickly and on an informed basis.

Asset allocation is stock driven on a bottom-up basis. As a result, asset allocation across the world's industries and regions is a function of where we identify the most attractive investment ideas. We have deliberately selected wide ranges for the portfolio relative to index weights at a regional level – the managers can hold up to 20% more than the index weight in a region. There is no minimum – we do not wish to be forced to invest in a region if we cannot find any attractive stocks in it.

Portfolio construction process



Risk management

Fundamental and portfolio risk

An understanding of company fundamentals

We recognise that one of the most significant risks within the portfolio is the permanent loss of our clients' capital and we therefore place significant emphasis in our investment management process on understanding the fundamentals of the companies in which we invest, and of the industries in which they operate.

Diversification

We ensure that we have a prudent level of diversification across stocks, industries and regions. Our investment guidelines, provided on the following page, are deliberately broad. This affords our investors the freedom to only invest where they see the very best opportunities for long-term value creation. Global Alpha is also diversified by growth type due to its three growth profiles.

Holding size

Careful consideration is given to the holding size of individual investments. We have three broad groups of holding size: circa 0.5% holdings, circa 1% holdings and circa 2% holdings. Only the highest conviction stocks are normally holdings above circa 2% of the portfolio. Companies in which there is a greater degree of risk or uncertainty are typically circa 1% or less. The circa 0.5% holding size, our 'incubator' holdings, enable us to bring a wide range of stocks into the portfolio where we believe there to be a higher risk/reward profile.

Valuations and correlation

Following the unusual environment in markets in 2022, we implemented two regular proprietary inputs into our risk framework.

1. Valuation heatmap. This tool uses valuation levels, growth expectations, and 30-plus years of global historic data on the distribution of returns outcomes to identify clusters of high valuations versus growth expectations. This enhances the context and challenge to investment teams, helping to improve decisions and disciplines for purchasing, holding, and selling positions.
2. Correlation and network analysis. Prioritising the importance of visual representation in our analysis of the data, this toolkit is used to prompt further discussion of portfolio balance and risk clusters.

Risk categories

We consider exposures to different risk categories such as commodity prices or inflation – these risk concentrations are not directly captured by reference to an index or benchmark but are important influences on return in the portfolio.

Trading risk

Our proprietary restrictions system is designed to prevent inappropriate transactions before dealing takes place. Systems also help to avoid excessive concentration of risk by identifying any stock, sector or country exposures that are outside internal guidelines. Segregated clients are sent an annual confirmation report to ensure the ongoing accuracy of their restrictions.

Risk team monitoring

Our dedicated Investment Risk, Analytics and Research Department is entirely independent of the Global Alpha Team. The department uses a range of tools and measures to analyse the risk within portfolios. Importantly, our Investment Risk, Analytics and Research Department is also experienced in assessing the methodology and limitations of the different tools, and how to interpret their output in different market conditions.

Overall, we believe that these tools can add value to the investment monitoring process if used intelligently and pragmatically. The Investment Risk, Analytics and Research Department reports formally every quarter to the investment managers, client service team and our Equity Investment Risk Committee, which is chaired by an investment partner.

Guidelines

Benchmark	MSCI All Country World Index (ACWI)
Performance objective*	To outperform the MSCI All Country World Index by 2–3% per annum over rolling five-year periods, gross of fees.
Number of stocks (guideline range)	70–120
Stocks	Maximum 6%, no minimum
Growth profile	Stop and think (with input from Investment Risk Committee) if: 45% in any one profile +/- 10% change in profile weight over rolling 12-month period
Industries	Minimum 15 industries Maximum 50% in top four
Regions	Maximum benchmark plus 20% No minimum

* Before management fees. The performance target is aspirational and is not guaranteed. We do not use it to compile the portfolio and returns will vary. A single performance target may not be appropriate across all vehicles and jurisdictions. We may not meet our investment objectives if, for example, our growth investment style is out of favour or we misjudge the long term earnings growth of our holdings.

Competitive advantages

People

Our people are fundamental to our success, and our partnership structure brings sustainable advantages in the recruitment and retention of staff.

Baillie Gifford's partnership structure has provided the foundation for an enviable record of corporate stability. It is also a significant factor in our success in attracting and retaining the very best investment talent. Our selection policy is based on intelligence rather than allegedly relevant specialisation, leading to recruitment of individuals from a wide range of academic disciplines. By training our analysts and investment managers in-house we manage to combine a common culture with an atmosphere that encourages vigorous debate. The firm's values and beliefs are clearly communicated and, coupled with low staff turnover and long service, the firm has been able to retain a team spirit while growing steadily in recent years.

Location

Having the majority of our decision makers in Edinburgh enables us to share views and ideas easily and efficiently. In addition to this, our common approach to research across departments helps provide an outstanding framework to allow us to select stocks effectively on a global basis.

Investment research information

We believe that while access to information is important to an investment manager, how we use that information is more so.

We recognise that all investment institutions have access to the same information and that it is our analysis of this information which adds value for our clients. In addition, the Global Alpha Team gain insights into business models and the competitive advantages of companies by attending around 350 company meetings each year. Company meetings are key to our idea generation, research and stock selection process as they help us understand a company in greater depth. We are cognisant of the pitfalls of confirmation bias and market noise. Rather than being guided by the mood of the market, we think independently and make more informed stock picking decisions for the long-term benefit of our clients.

People

Global Alpha key decision makers



Spencer Adair*

Spencer is an investment manager in the Global Alpha Team. He joined Baillie Gifford in 2000 and became a partner in 2013. He has been an investment manager in the Global Alpha Team since its inception in 2005 and for the Monks Investment Trust since 2015. He became an investment manager in the International Concentrated Growth Strategy in 2021. Spencer has also spent time working in the Fixed Income, Japanese, European, Emerging Markets and UK Equities teams. He graduated BSc in Medicine from the University of St Andrews in 1997.



Malcolm MacColl*

Malcolm is an investment manager in the Global Alpha Team. He has been involved in Global Alpha since the product's inception in 2005 and became a partner of the firm in 2011. In 2021 he became a managing partner with overall oversight for the investment department. Malcolm previously worked in the UK Small Cap and North American equity teams. He managed the North American portion of wider Global portfolios while in the North American Equity Team. Malcolm graduated MA in Economics and History in 1998 and MLitt in Economics, Politics and Management in 1999, both from the University of St Andrews.



Helen Xiong*

Helen is an investment manager in the Global Alpha Team. She joined Baillie Gifford in 2008 and became a partner in 2020. In addition to Global Alpha, Helen has spent time working in our Developed Asia, UK, US Equity Growth, and Emerging Markets equity teams. She graduated BSc (Hons) in Economics from the University of Warwick in 2007 and MPhil in Economics from the University of Cambridge in 2008.

*Partner.

Baillie Gifford

Clients

We are immensely proud of our supportive client base. Without them, our business could not exist.

Our primary goal is to build long-term relationships with aligned, like minded, clients. Our longest client relationship dates back to the early 1900s.

A core principle we have always upheld is prioritising our clients' interests above the firm's. In an industry that often puts financial gain over client outcomes, this focus is crucial. We aspire to be seen as more than merely the 'hired help', and aim to be recognised as a trusted, long-term partner, who can be relied on to give honest and objective advice at all times.

We are research-driven, patient and prepared to stand apart from the crowd. And because we're an independent partnership without outside shareholders, the long-term goals of our clients are genuinely our priority.

Partnership

Stability matters.

Since its inception in 1908, Baillie Gifford has proudly remained a private partnership. We have no intention of changing this. We have never had a merger or made an acquisition, nor do we seek to in the future. This is a rare level of stability in financial services.

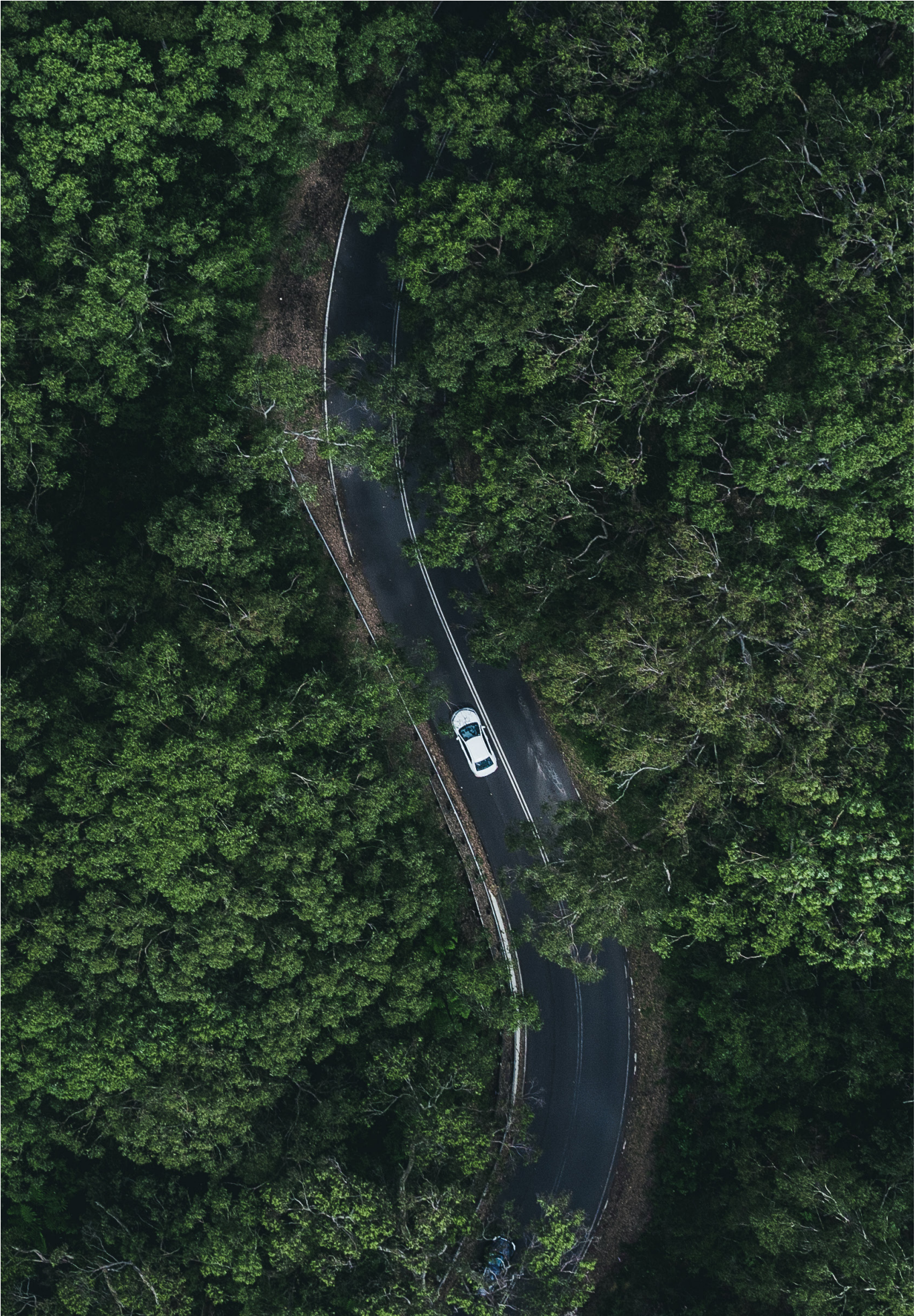
All of our partners work within the firm which provides a unique level of alignment between them as owners, and our clients. This is a key differentiator in comparison to a lot of our peers.

Focus

We have a clear unity of purpose – excellent long-term investment returns and unparalleled client service. Our interests and long-term objectives are completely aligned with those of our clients.

We are not short-term speculators, rather we deploy client's capital to run truly active portfolios that give exposure to exciting and lasting growth companies. We would argue that it is visionary entrepreneurs and company leaders that generate long-term profits and share price increases, not stock markets or indices.

When active management is done well it can add material value over the long term. We need to be willing to take a differentiated view. This is not easy. It requires dedication, independent thought and a long-term perspective. Our whole firm is built around this, and we will always remain resolutely investment and client outcome driven in our outlook.



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