

Baillie Gifford Investment Grade Bond Fund

30 September 2024

Baillie Gifford Update

Philosophy	Long-term investment horizon A growth bias Bottom-up portfolio construction High active share
Partnership	100% owned by 58 partners with average 20 years' service Ownership aligns our interests with those of our clients Enables us to take a thoughtful, long-term view in all that we do Stability, quality and consistency

Investment Proposition

The Fund seeks to maximise total return relative to an index comprised of sterling investment grade bonds. Performance is driven by stock selection. Ideas are sourced primarily from investment grade bonds and are driven by fundamental, bottom-up stock analysis. Our portfolio is well diversified, with exposure to between 50-90 companies typically. Holdings are sized according to our level of conviction in their prospects and the risks they pose.

Fund Facts

Fund Launch Date	30 November 2001
Fund Size	£973.2m
IA Sector	£ Corporate Bond
Current Number of Issuers	78
Typical Number of Issuers	50-90
Duration	5.9
Average Credit Rating	BBB
Tracking Error	0.8%
Tracking Error Range	0.5-2.5%
Redemption Yield	5.2
Running Yield	4.5

Fund Manager

Name	Years' Experience
Paul Dilworth	18
Nektarios Chatzilefteris Michalas	8

Fund Objective

To outperform (after deduction of costs) the ICE BofA Sterling Non-Gilt Index by 0.75% per annum over rolling three-year periods.

The manager believes this is an appropriate target given the investment policy of the Fund and the approach taken by the manager when investing. In addition, the manager believes an appropriate performance comparison for this Fund is the Investment Association Sterling Corporate Bond Sector.

There is no guarantee that this objective will be achieved over any time period and actual investment returns may differ from this objective, particularly over shorter time periods.

Periodic Performance

	3 Months	1 Year	3 Years (p.a.)	5 Years (p.a.)
Class B-Inc (%)	3.1	11.1	-2.7	-0.9
Index (%)*	2.3	9.7	-2.9	-1.0
Target (%)**	2.5	10.5	-2.2	-0.4
Sector Average (%)***	2.5	10.9	-1.8	0.0

Source: FE, Revolution, ICE Data Indices. Total return net of charges, in sterling.

Share class returns calculated using 10am prices, while the Index is calculated close-to-close.

Baillie Gifford operates a single swinging price for the Fund and, therefore, may apply a dilution adjustment to the price to protect long-term investors from the costs associated with buying and selling underlying investments that result from other investors joining or leaving the Fund. This adjustment will affect relative performance, either positively or negatively.

*ICE BofA sterling Non-Gilt Index.

**ICE BofA sterling Non-Gilt Index plus +0.50% to 16 September 2022; thereafter ICE BofA sterling Non-Gilt Index plus +0.75% per annum, over rolling three-year periods. The indices have been chain-linked for performance figures above.

***IA £ Corporate Bond Sector.

Discrete Performance

	30/09/19- 30/09/20	30/09/20- 30/09/21	30/09/21- 30/09/22	30/09/22- 30/09/23	30/09/23- 30/09/24
Class B-Inc (%)	3.6	0.3	-22.1	6.5	11.1
Index (%)*	3.9	-0.3	-22.2	7.4	9.7
Target (%)**	4.4	0.2	-21.9	8.2	10.6
Sector Average (%)***	4.2	1.3	-20.5	7.3	10.9

Source: FE, Revolution, ICE Data Indices. Total return net of charges, in sterling.

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Market environment

Market environment

With inflation now close to target levels in the developed world, three of the world's major central banks – the US Federal Reserve (the Fed), Bank of England (BoE) and European Central Bank (ECB) – were among those cutting interest rates during the third quarter of 2024. In the US, the Fed's first interest rate cut of the cycle was by half a percentage point, with a softer labour market providing more conviction that policy rates are too high for current levels of inflation. Moving earlier, the BoE was much more tentative as services inflation remained high. In the Eurozone, the ECB also cut by a quarter percentage point in response to signs of slowing growth in the bloc's core economies.

Credit markets performed well over the quarter, responding positively to continued lower inflation and falling interest rates. While growth is slowing, importantly, developed market economies continue to grow. There are signs of deteriorating company fundamentals but weakness starts from a very robust starting point. Overall, these are strong market conditions for corporate credit and, in this context, high yield corporate bonds outperformed their investment grade counterparts. Valuations, as measured by credit spreads (the additional yield provided by corporate bonds compared to government bonds), remain high relative to the past. 'All-in' yields continued to look attractive as interest rates remained near their highest levels in 15 years. This supported corporate bond returns as evidenced by the high demand for corporate bonds, most visibly in the buoyant new issues market – a further sign of a healthy market.

However, there was a short-lived "rout" in August which provided evidence of the fragility of market sentiment. The perception of a higher risk of recession combined with the unwinding of the yen carry trade (investors had been taking advantage of the significant yield differential between US and Japanese bonds but this began to narrow) led to a selloff in risk markets. While this settled quickly, reflecting the strong market backdrop, it served as a reminder that any economic scenario which does not reflect the market's base case is likely to be met with significant volatility.

Performance

Investment grade corporate bonds delivered a healthy return over the quarter. Credit spreads ended the quarter at a similar level to the start. However, underlying government bonds yields fell and combined with steady income generation, absolute returns were positive.

Relative to the index benchmark the Fund outperformed. Security selection was the main driver

of returns, most notably in the water sector. Thames Water has been in the news for some time due to concerns about its future solvency and during the quarter it was heavily downgraded by credit rating agencies. The Fund does not hold Thames bonds, nor Southern Water which also has concerning finances – relative to the index, avoiding these bonds was a positive. The bond prices of other water companies were hurt due to broad negative sentiment. The Fund holds what we consider to be the stronger companies in the sector and, relatively speaking, Welsh Water and Lunar Funding (a securitisation of bonds issued by Northumbrian and Wessex Water) made positive contributions to performance.

Elsewhere, from a more positive angle International Workspace Group, a company providing flexible workspaces, was one of the top contributors over the quarter. We participated in a new issue earlier in the year at a valuation we felt was especially compelling and the market has quite quickly become aligned to our positive view of the company – we have already trimmed the position to manage risk as the valuation has increased. There were a broad range of positive contributors across other sectors including financials, and no major concerns in the portfolio.

Over 12 months the Fund is comfortably ahead of its target return, again driven by security selection. Property companies have been among the top contributors, with Eastern European office and residential operator CPI the standout performer. Over three years the Fund has outperformed the index net of fees but not met its target. We underestimated the speed and scale of interest rate rises as inflation soared following the pandemic, and this detracted from performance due to exposure to sensitive sectors such as real estate – as noted above, in some cases bonds have recovered strongly since.

Positioning

We continued to reduce risk in the Fund during the quarter, reflecting our desire to protect against unexpected events or a deterioration in the economic backdrop – current valuations leave little room for error. We took out some insurance against a rise in corporate bond spreads through credit default swaps (CDS) and increased the Fund's exposure to higher quality and shorter-dated bonds.

That said, we are seeking to maintain enough yield in the Fund to keep pace with positive market momentum – or at least one which does not deteriorate – in line with our base case scenario. The new issue market continues to provide opportunities to add interesting and attractively valued bonds to the Fund. Examples included: Great Portland Estates, a FTSE 250 property company owning £2.5 billion of central London offices, providing an opportunity to invest in a high-quality name in an unloved sector; and,

Pearson, a global learning and assessment company which is a highly cash-generative business with leading positions in various sectors and diversified revenue streams. We sold a few bonds which had performed strongly and carry more risk if volatility increases, including Lonza, a supplier to the pharmaceuticals industry and Unite, a student accommodation provider.

Market outlook

The economic outlook is finely poised at this stage. There were various signs of a slowdown in the US economy during the third quarter, including weaker data on labour markets, manufacturing and consumer confidence. Very recently, some of those data points have been subject to positive revisions, and the latest US labour market data showed strong job growth and a decline in the unemployment rate.

Looking ahead, the upcoming US presidential election is considered too close to call, and this could bring market volatility in the very short term. Rising tensions in the Middle East could escalate further still, with spillover effects into the wider global economy, which have been limited thus far. For example, disruption in the oil market could cause inflation to rise from current benign levels.

This presents a challenge for central banks. While interest rates in many countries appear too high today given current growth and inflation rates, policymakers have indicated a wariness of cutting rates too quickly and risking a rebound in inflation. On the other hand, they will be cognisant of the potential for high interest rates to restrict economic growth.

We continue to believe a soft landing is the most likely outcome. In addition, company fundamentals remain broadly resilient although pockets of deterioration are emerging in some cyclical sectors as higher financing costs start to impact demand. There is no sign that the market's insatiable hunger for corporate bonds is likely to deteriorate in the short term. However, valuations remain high and, as recent events have shown, sentiment is fragile leaving the market vulnerable to bad news.

Distribution of Portfolio by Asset Class

	Fund Weight*(%)
Sterling	
Conventional Sovereign	7.3
Conventional Non Sovereign	79.4
Index Linked	0.0
Total Sterling	86.7
Cash & Derivatives ***	
Total Cash & Derivatives ***	5.1
Foreign Currency	
Conventional Sovereign	0.0
Conventional Non Sovereign	8.1
Index Linked	0.0
Total Foreign Currency	8.1
Total	100.0

*Shows exposure to bonds in the currency before any hedging is applied

Distribution of Portfolio by Credit Rating Band

	Fund Weight (%)
AAA	9.1
AA	13.8
A*	7.5
BBB*	57.2
BB*	6.5
B	0.7
Cash & Derivatives	5.1

*Includes BG internally-rated bonds where there is no official rating.

Top Ten Issuers

	Fund Weight (%)
UK Treasury	3.9
National Grid	3.4
EIB	3.3
Banco Santander	3.1
Telereal Securitisation PLC	2.8
NatWest Group plc	2.6
AT&T	2.6
HM Treasury	2.6
Annington Finance	2.4
Nationwide Building Society	2.4

Distribution of Portfolio by Industry

	Fund Weight (%)
Banking	16.5
Utility	9.6
Asset Backed	8.3
Real Estate	7.8
Financial Services	7.0
Insurance	6.8
Sovereign	6.5
Supranational	5.1
Government Guaranteed	4.2
Commercial Mortgage Backed	4.1
Telecommunications	4.1
Retail	2.7
Technology & Electronics	2.5
Agency	2.2
Others	7.5
Cash & Derivatives	5.1

Distribution of Portfolio by Region

	Fund Weight (%)
United Kingdom	57.6
Europe	15.3
North America	13.1
Supranational	5.1
Emerging Markets	2.5
Developed Asia	1.4
Cash & Derivatives	5.1

Company Engagement

Engagement Type

Company

Governance

Burberry Group plc, The Weir Group PLC

For further details on company engagement please contact us. You can also find further information on how we integrate environmental, social and governance (ESG) matters into our investment approach, [here](#).

Asset Name	Fund %	Asset Name	Fund %
Sterling Bonds		Sterling Bonds	
Conventional Sovereign		Conventional Sovereign	
LCR Finance 4.5% 2028	0.85	E.ON 5.875% 2037	0.34
Long Gilt Future 10yr Dec 24	-0.01	E.ON 6.75% 2039	0.44
UK T Bill 28/10/2024	2.46	EDF 5.5% 2037	0.54
UK Treasury 3.5% 22/10/2025	1.22	EDF 5.5% 2041	0.32
UK Treasury 4.125% 29/01/2027	0.20	EDF 6% 2114	0.46
UK Treasury 4.25% 07/12/2049	0.98	EDF 7.375% 2035 Perp	0.93
UK Treasury 4.5% 07/12/2042	0.92	EIB 0.125% 2026	0.51
UK Treasury 5% 07/03/2025	0.73	EIB 1.375% 2025	0.62
Total Conventional Sovereign	7.32	EIB 4.5% 2044	0.74
Conventional Non Sovereign		EIB 4.625% 2054	0.39
Abrdn 5.25% 2026 Perp AT1	0.31	EIB 6% 2028	1.02
Admiral Group 8.5% 2034 T2	1.00	Ford Motor Co 5.625% 2028	0.99
Amgen 4% 2029	0.69	Gatwick Funding 5.5% 2040	0.66
Anglian Water 6% 2039	0.26	Great Portland Estates 5.375% 2031	0.38
Anglian Water 6.25% 2044	1.01	Heathrow Finance 5.75% 2025	0.73
Annington Funding 2.308% 2032	0.49	HSBC Bank 5.844% 2031 Perp	0.35
Annington Funding 2.924% 2051	0.81	IBRD 0.25% 2026	1.27
Annington Funding 3.935% 2047	0.47	IBRD 5.75% 2032	0.52
Annington Funding 4.75% 2033	0.67	Inchcape 6.5% 2028	1.24
AT&T 4.25% 2043	0.38	ING Groep 5% 2025/26	0.91
AT&T 4.875% 2044	0.40	Intesa Sanpaolo 6.5% 2028/29	0.96
AT&T 7% 2040	1.86	Investec 1.875% 2027/28	0.75
Banco Santander 3.125% 2025/26	0.97	Investec 10.5% 2030 Perp AT1	0.29
Banco Santander 5.5% 2029	1.22	Investor 5.5% 2037	0.42
Barclays 3.75% 2025/30 T2	0.25	KFW 0.875% 2026	0.99
Barclays 7.09% 2028/29	0.51	KFW 5% 2036	0.50
Barclays 8.407% 2027/32 T2	0.83	KFW 6% 2028	0.92
Berkeley Group 2.5% 2031	0.83	Legal & General 5.375% 2025/45 T2	1.16
Blackstone Private Credit 4.875% 2026	2.18	Lunar Funding 1 5.75% 2033	0.50
Burberry 1.125% 2025	1.49	Mitchells & Butlers FRN (AB) 2033	1.51
CaixaBank 6.875% 2028/33 T2	0.74	Motability 3.625% 2036	0.48
Canada Pension Plan 1.25% 2027	0.48	Motability 5.625% 2035	0.93
Canada Pension Plan 1.625% 2071	0.48	National Gas Transmission 1.375% 2031	1.00
Center Parcs 5.876% 2027	0.95	National Grid 5.625% 2025 Perp	0.37
Center Parcs 6.136% 2031	0.21	National Grid ED plc 3.5% 2026	0.83
Centrica 6.5% 2030 Perp	0.40	National Grid ED S Wales 5.35% 2039	0.51
Centrica 7% 2033	0.33	National Grid ED W Midlands 6% 2025	0.68
CK Hutchison Telecom 2.625% 2034	1.01	Nationwide 5.875% 2024 Perp AT1	1.53
CPI Property 2.75% 2028	0.69	Nationwide Building Society 6.125% 2028	0.88
DNB Bank 4% 2026/27	0.73	NatWest 2.875% 2025/26	0.94
		NatWest 3.622% 2025/30 T2	0.93
		NatWest 5.642% 2034	1.72
		Network Rail 4.75% 2035	0.96

Asset Name	Fund %	Asset Name	Fund %
New York Life Insurance 4.875% 2031	1.09	Conventional Sovereign	
New York Life Insurance 4.95% 2029	0.96	Euro-Bobl Future Dec 24	0.00
Ontario Teachers' Pension Plan Board 1.125% 2026	0.47	Euro-Bund Future Dec 24	0.00
Pearson Funding 5.375% 2034	0.67	US 10yr Note Future Dec 24	0.00
Pension Insurance 4.625% 2031 T2	1.01	US 5yr Note Dec 24	0.01
Pension Insurance 7.375% 2029 Perp RT1	0.25	US Ultra 10yr Note Future Dec 24	0.01
Pension Insurance Corp 8% 2033 T2	0.15	Total Conventional Sovereign	0.00
Phoenix 5.75% 2028 Perp RT1	0.26		
Phoenix Group 7.75% 2033/53 T2	0.58	Conventional Non Sovereign	
Pinewood Gp 3.625% 2027	1.03	BEL SA 4.375% 2029	0.73
Realty Income 1.875% 2027	0.27	Burford Capital 6.25% 2028 (144a)	0.43
Realty Income 5% 2029	0.40	Burford Capital 9.25% 2031 (144A)	0.56
Santander UK 7.098% 2026/27	0.93	CDIB ITRX Crossover SAS	-3.08
Schroders 6.346% 2029/34 T2	1.00	CPI Property 1.5% 2031	1.02
SNCF Reseau 5.25% 2035	0.37	Fraport 4.25% 2032	0.18
South West Water 6.375% 2041	0.85	Iberdrola 1.874% 2026 Perp	0.49
Sovereign Housing 4.768% 2043	0.49	International Workplace Group 6.5% 2030	1.64
Swedish Export Credit 0.125% 15/12/2025	0.48	Kyndryl Holdings 6.35% 2034	1.45
Telereal 1.3657% 2031 (A6)	0.14	Rabobank 6.5% Perp	0.42
Telereal 1.9632% 2031 (B2)	0.96	TAG Immobilien 4.25% 2030	1.24
Telereal 3.5625% 2031 (A3)	1.04	Teleperformance 5.75% 2031	1.04
Telereal 5.634% 2031 (B3)	0.28	Teva 7.875% Pharma 2031	0.59
Telereal FRN 2031 (B7)	0.41	Teva Pharma 7.375% 2029	0.39
Temasek 5.125% 2040	0.39	Voestalpine 3.75% 2029	1.03
Tesco Property Finance 1 7.6227% 2039	0.39	Total Conventional Non Sovereign	8.12
Tesco Property Finance 4 5.801% 2040	0.83	Total Foreign Currency Bonds	8.12
Vodafone 3% 2056	0.48		
Weir Group 6.875% 2028	1.19	Cash & Derivatives	
Wellcome Trust 2.517% 2118	0.30	Forwards	
Welsh Water 1.625% 2026	0.48	EUR Fwd Asset 21-Nov-2024 S	-8.60
Welsh Water 2.375% 2034	0.64	GBP Fwd Asset 21-Nov-2024 P	11.35
Welsh Water 5.75% 2044	0.87	USD Fwd Asset 21-Nov-2024 S	-2.47
Yorkshire Building Society 3.375% 2027/28 T2	0.39	Total Forwards	0.29
Yorkshire Building Society 6.375% 2027/28	1.26		
Yorkshire Power 7.25% 2028	1.07	Swaps	
Yorkshire Water 2.75% 2041	0.24	CDIB ITRX Crossover SAS	2.82
Yorkshire Water 5.5% 2035	0.14	IRS GBP PAY FLT 19/09/27	-12.66
Yorkshire Water 6.375% 2034	0.51	IRS GBP PAY FLT 21/03/27	-7.47
Yorkshire Water 6.601% 2031	0.28	IRS GBP REC FIX 19/09/27	12.65
Total Conventional Non Sovereign	79.40	IRS GBP REC FIX 21/03/27	7.48
Total Sterling Bonds	86.72	Total Swaps	2.81
Foreign Currency Bonds		Cash	

Asset Name	Fund %
Collateral Account Memo	-0.06
EUR Futures Initial Margin Account	0.11
EUR Uncommitted Cash	0.01
GBP BNY Revenue Uncommitted Cash	-0.40
GBP CCP Initial Margin	0.61
GBP CCP Variation Margin	-0.01
GBP Futures Initial Margin Account	0.28
GBP Uncommitted Cash	1.47
USD Futures Initial Margin Account	0.04
Total Cash	2.05
Total Cash & Derivatives	5.15
Total	100.00

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Share Class	Share Class Inception Date	ISIN	SEDOL	Annual Management Fee (%)	Ongoing Charge Figure (%)	Distribution Yield (%)	Underlying Yield (%)
Class B-Inc	26 March 2002	GB0030816481	3081648	0.25	0.28	5.20	4.90
Class B-Acc	01 April 2016	GB00BYQCYS34	BYQCYS3	0.25	0.28	5.20	4.90

The table displays the primary shares classes. Other share classes may be available for those investors who have a separate arrangement. Charges will reduce the value of your investment. Please refer to the Prospectus and Key Investor Information Document for further details. The Ongoing Charges Figure ('OCF') may be lower than previous declarations as a result of a revision to how the indirect fees associated with closed-ended investment companies need to be shown. This does not necessarily mean that fund expenses have gone down rather that we have reverted to how they have been calculated until 30 June 2022 to reflect the revised Investment Association's Guidance on Disclosure of Fund Charges and Costs (July 2020, updated January 2022, revised November 2023). A more detailed Costs and Charges disclosure is available upon request.

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Additional Geographical Location Information

Israel: This Report, as well as investment in the Fund described herein, is directed at and intended for Investors that fall within at least one category in each of: (1) the First Schedule of the Israeli Securities Law, 1968 (“Sophisticated Investors”); and (2) the First Schedule of the Investment Advice Law (“Qualified Clients”).

The Fund’s share price can be volatile due to movements in the prices of the underlying holdings and the basis on which the Fund is priced.

As with any investment, the clients’ capital is at risk. Past performance is not a guide to future returns.

Throughout the report all figures are rounded, so any totals may not sum. Not all stocks mentioned may be held by the portfolio.

All information as at 30 September 2024 and source is Baillie Gifford & Co unless otherwise stated.