LWM Consultants Ltd

Meeting the Fund Manager

Baillie Gifford Emerging Markets Bond Fund – Sally Greig

In reviewing the portfolios we spent some time looking at the fixed interest part, we have decided to increase the weightings in the Standard Life GARS Fund as the central foundation, and move away from fixed interest exposure in the developed markets although we will still have a small holding.

We have therefore turned to the emerging markets as a region where we see potential for growth in the future. The thought of investing in emerging markets conjures up risk – the fact is that emerging market bonds have lower volatility or risk than global bonds.

We met with one of the fund managers Sally Greig to understand more about these types of funds and the opportunities they offer long term. Two facts struck me as important:

1. Strong potential growth – the average growth potential in emerging markets is 5.8% p.a. compared to just 1.6% in the developed markets
2. Low debt levels – the average debt in emerging markets is 33% of GDP, compared to 104% in the developed markets

Often when we consider emerging markets we might consider Argentina, India, China et al but the fund works from the JP Morgan GBI-EM Global Diversified Index which includes countries from Europe (Russia, Hungry, Poland etc), Asia (Malaysia, Thailand etc) Africa (South Africa) and Latin America (Brazil, Peru, Chile etc). This provides diversification across 14 investible and liquid countries.

We will expand on this when we look at how the fund invests.

What does the fund look to achieve?

The fund looks to outperform the JP Morgan GBI-EM Global Diversified Benchmark by 2.5% per annum over rolling three year periods. It does this by diversifying the portfolio by country and also can move in and out currency depending on their thoughts. So the fund is a local currency fund i.e. the debts are in local currency rather than dollars. However, they can switch to dollar based debt if this is likely to provide stronger returns.

Introducing the fund manager

The fund is managed by Sally Greig and Steven Hay. Sally started her career as an economist with the Bank of England before moving to Baillie Gifford where she has been for seven years. Baillie Gifford unlike many fund houses operate on a partnership basis where the partners are personally responsible should the firm fall into trouble, this sense of corporate responsibility rests not only with the partners but also with all members of staff. This clearly shows through in the way the fund managers approach the management of their funds and Sally is no exception. Sally and Steven are supported by a team of analysts and each member of the team has responsibility for a particular country.

How the fund is managed?

The fund is well managed and we liked the approach described by Sally, they take their responsibility to money very seriously this is reflected by the unique structure of the business. When looking to invest they look to find investments where there is a difference between long-term value and the market price they do this through in-depth research and quantative analysis.

There were a number of discussions which we found fascinating this included the theme analysis, this looks at various events and then considers what the likelihood of this is and then what impact this would have on the fund. So for example, what would the likelihood of very low global growth be, so if they rated this as say 70% then this would influence certain holdings.

We talked about about how this would impact on holdings and Sally talked about how they are not afraid to take big country bets compared to the index and lessen exposure so for example they have a greater exposure to Czechoslovakia compared to Hungry. The reason being threefold:

1. Fiscal sustainability – Czech prudence v Hungarian fudge
2. All about growth – Hungary cannot rise above stall speed
3. Debt vulnerability – external debt is 134% of GDP fir Hungary v 46% for Czech Republic

So it is important to have the flexibility to move away from the benchmark to drive long term growth.

On the country allocation this does change and countries can be added and removed from the index, we were interested to see the likes of India and China were not included. The reason for this is that they are not investable at the moment. You can buy into Chinese debt but it is fraught with danger and therefore is not considered.

Finally the fund is relatively small which enables it to move quickly if needed but fundamentally Baillie Gifford are long-term fundamental investors, not speculators and this fits well with our philosophy.

Conclusion

We have always liked the Baillie Gifford style to investing and this fund is no different. We are adding the Threadneedle Emerging Market Bond Fund as well and the two will complement each other within the portfolios.

The source of information in this note has been provided by Baillie Gifford and is correct to the end of March 2012. These are notes from meeting the fund manager and should not be seen as a recommendation to purchase this fund. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision. You should also note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise.