LWM Consultants Ltd

Meeting the Fund Manager

Scottish Mortgage – Tom Slater

The Scottish Mortgage Investment Trust is a holding in a number of portfolios and this is unlikely to change in the next review. We have met the fund manager, James Anderson, on several occasions and Tom is the deputy manager on the fund. Tom has recently been made a partner at Baillie Gifford which demonstrates both his commitment to the business and their commitment to him. There are currently 37 partners and it is an unlimited partnership.

What does the fund look to achieve?

This quote sums up the style very well "please don't own Scottish Mortgage shares if you cannot afford a five year time horizon or want high correlation to the market". The fund invests globally, looking for strong businesses with above-average returns and aims to achieve a greater return than the FTSE All-World Index (in sterling terms) over a five year rolling period. We agree that this holding should not be seen as short term.

Introducing the fund manager

Tom Slater is the deputy manager of the Scottish Mortgage Investment Trust and is a partner of Baillie Gifford. This unique structure means that partners have full liability for losses suffered by the firm and therefore by its nature installs a sense of corporate responsibility. Tom joined Baillie Gifford in 2000 as an analyst before being appointed as an investment manager in 2003, he is also a member of the Long Term Global Growth Team.

How the fund is managed?

There are around 80 equity investments in the portfolio chosen from around the world for their long-term potential. The portfolio bears little resemblance to the benchmark index which is only used for performance measurement over a five year rolling period. Achieving adequate diversification is a requirement but an unconstrained approach is taken with no fixed limits of geographical and sector exposures.

Companies are analysed using questions that aim to assess: strength of management, competitive position, customer perspective, prospects for sales and margins, current and potential valuation, how the market and their view differs and what will happen in five years.

We expanded on this when we talked about Google, Amazon, Apple and Facebook and how we are experiencing with these companies significant market domination and share values which defy the laws of large numbers (although Facebook shares have not come out). Effectively these companies now own the internet and rather than clashing with each other they command different aspects of it.

Focusing on Amazon, the reason why this is one of the largest holdings is simply that it is a business building for the long term. The model makes sense, high street prices can only go one way which is up (cost of shops etc) whereas Amazon can drive down prices. Its model is hugely destructive and we can see this as high streets struggle to compete. We talked about price margins but the feeling is that as more people turn to Amazon for shopping price becomes less of an issue. The business is not the normal stock market led business, the management are renowned for their customer focus and long term approach preferring to sacrifice short term margins to invest for future growth. The business is growing into new markets including cloud as well as Kindle and now Kindle Fire, these developments are why the company has long term potential.

On a plus side the shares could be seen as cheap even at today's level and could growth substantially over the next five years. However, there are risks – the business depends on the growth of e-commerce and if this growth is much lower than predicated then this could have a negative impact as could competition in places like Brazil and China, all of this could stifle potential growth of the share price and potentially reduce it significantly.

We discussed other shares that they held but we found this example interesting as it shows the process of analysing a stock and looking at the positives and negatives and then predicting where the share prices can go depending on different scenarios.

On a geographical level we turned to China and what the thoughts were around this. Tom seemed very positive in his outlook for China in the long-term. Some of the factors he mentioned:

1. The growth in 2008 was perhaps aggressive but monetary tightening has seen inflation put under control and robust growth at around 9% p.a.
2. The ruling party recently put together a 5 year plan, in reality this was a 20 year plan. The point being that China is looking over a 20 year horizon
3. There are still opportunities to be had through Chinese industrialisation and there are still quality innovative businesses coming through

Interestingly when you look at the volatility of emerging market shares these stand at 23.7% compared to UK shares which are 21.1%. When you consider the difference with debt and growth and that emerging markets have the potential to drive long term returns this difference is not great.

Conclusion

We have always liked the Baillie Gifford style to investing and this trust is no different. As long term investors this philosophy sits well with the way we look at investments. We believe this is a good long term global fund which offers the potential for strong returns over the next five years.