



The Scott Trust Endowment Fund Performance Report 2018/2019

Statement by the Chairman of the Scott Trust, Alex Graham



The Scott Trust Endowment Fund and our other investment assets are central to securing the long-term future of the Guardian.

The genesis of the Endowment Fund was the disposal in mid-2007 of a minority stake in Trader Media Group. This allowed us to invest a portion of these proceeds (£200m) in a diversified investment portfolio. We commenced investment in mid-2008, the heart of the financial crisis, and this was of course challenging. However, the investment portfolio weathered the storm well, and has subsequently flourished. The Endowment Fund has increased in scale since 2008 through a combination of organic growth and other cash injections as Guardian Media Group has disposed of non-core assets over time.

The investment objectives of the Fund were (and still are) three-fold - to generate long-term returns to secure the financial and editorial independence of the Guardian in perpetuity; to provide diversification in economies other than that of the UK, and to provide diversification in sectors other than the media industry, which has been undergoing substantial change over the past decade. We believe investing in a global, diversified, multi-asset portfolio is an appropriate investment strategy, in terms of risk and return.

In this performance report we detail how the Endowment Fund has evolved over the past nine years, the successes it has achieved, our approach to socially responsible investment, including the Fund's alignment with the Guardian's fossil fuel divestment campaign 'Keep it in the Ground', and how the Fund is currently positioned.

The Endowment Fund is now a unique and critical part of the Guardian's make up, and it is essential that those of us charged with overseeing its investment and its work take a long view, and bear in mind its ultimate purpose: to secure the Guardian's financial and editorial independence, in perpetuity. That is the guiding principle for every decision we make around the Fund.

We are delighted to share with Guardian staff and other stakeholders some detail on our assets, with a particular focus on the Endowment Fund, its evolution, composition and performance over the past twelve months.

A handwritten signature in black ink, consisting of a stylized 'A' followed by a series of loops and a long horizontal stroke.

Report on the Endowment Fund

1. Structure of Endowment Fund

At 31 March 2018, the Endowment Fund's aggregate investment assets were in excess of £1.01bn. The split between the different components and their respective roles is as follows:

Endowment Asset	Balance	Role of Investment Asset
Long-Term Investment Fund (LTIF)	£784.7m	The LTIF aims to generate strong risk-adjusted financial returns over the long term to support the Scott Trust's mission.
Medium-Term Investment Fund (MTIF)	£148.4m	The MTIF is invested in investment grade bonds and money market funds to provide near-term spending requirements for GMG's business operations.
GMG Ventures	£42m	GMG Ventures contributes financial returns and supports GMG's strategy by investing in early stage businesses focussed on developing the next generation of media technology.
Money Market Funds & Cash	£39.4m	As for the MTIF.
Total	£1.01bn	

This report relates to the LTIF. Details of GMG Ventures activities can be found at its website <http://www.gmgventures.co/>

2. Performance

Since inception in mid-2008 to 31 March 2018, the Long-Term Investment Fund (LTIF) has generated an annualised return of +6.3%, ahead of its portfolio benchmark (+4.9%). This portfolio benchmark reflects the LTIF's Strategic Asset Allocation (SAA), i.e. the combination of assets which over the long-term should enable us to meet our investment objectives.

For the twelve month period to 31 March 2018 (in line with our fiscal year end period), the LTIF generated a return of +3.7%, ahead of the benchmark (+3.1%).

3. Governance of the Endowment Fund

For practical purposes the Scott Trust has delegated authority for most decisions relating to the management of the assets to the Scott Trust Investment Committee ("Investment Committee"). The Investment Committee meets on a quarterly basis to review the performance and strategy of the aggregate Endowment Fund assets.

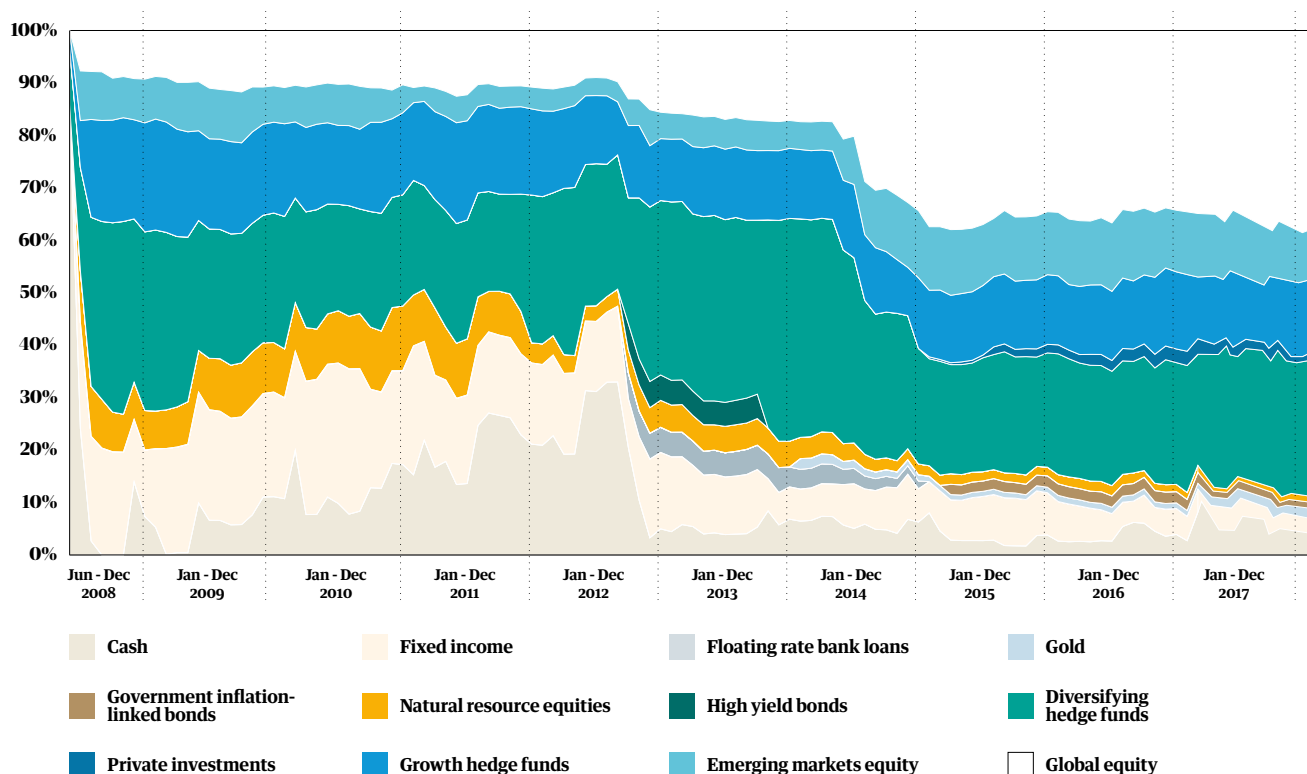
The Investment Committee comprises both Scott Trust and GMG plc Board members - the current membership is as follows:

- Neil Berkett (Chair)
- Catherine Howarth
- Ole Jacob Sunde
- Coram Williams
- Nils Pratley
- Sir Anthony Salz

The Scott Trust has retained Cambridge Associates as an advisor to work with the Investment Committee and Executive Team on strategic and tactical asset allocation, and management of day to day aspects of the LTIF.

4. Review of Investment Activities

Evolution of the LTIF's Asset Allocation



The table above shows the evolution of the LTIF's asset allocation since mid-2008 to 31 March 2018.

In the aftermath of the 2008 financial crisis, we would highlight the defensive positioning of the portfolio. It was necessary at that time to draw meaningful amounts of capital from the portfolio to fund on-going business needs.

In more recent years, the LTIF has adopted a more return-seeking stance - reflected in the greater exposure to equity assets from 2014 onwards. The Medium-Term Investment Fund (MTIF) and Money Market Funds & Cash investments are intended to meet the business' short to medium term financing requirements, meaning that no spending has yet been necessary from the LTIF. The LTIF is currently invested in eleven asset classes.

4. Review of Investment Activities (cont.)

Overview of LTIF Performance

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018 TD	Ann. since inception
Scott Trust Total Assets (with currency overlay)	-9.3%	+17.5%	+10.7%	-2.8%	+4.5%	+10.6%	+8.2%	+0.2%	+17.6%	+9.5%	-1.7%	+6.3%
Scott Trust Portfolio Benchmark (hedged)	-12.1%	+12.8%	+7.8%	-2.4%	+4.6%	+7.8%	+7.1%	+0.4%	+17.4%	+9.7%	-2.5%	+4.9%
Value Added	+2.8%	+4.6%	+2.9%	-0.4%	-0.1%	+2.9%	+1.1%	-0.2%	+0.1%	-0.3%	+0.8%	+1.4%

Note: returns above for calendar year end periods to December. 2018 TD relates to the period to 31 March 2018.

¹2008 returns reflects period from 30 June 2008 to 31 December 2008.

The table above shows the LTIF's performance since inception on both a calendar year (to December) and annualised basis ("Ann. Since Inception"). The LTIF has outperformed its portfolio benchmark since inception (net of fees). The fund's relative performance has been positive in both rising and falling equity markets.

Diversification

The LTIF invests across multiple asset classes through third party fund managers. These managers are subject to rigorous initial and ongoing review. The LTIF is highly diversified, with allocation to any single active manager limited to 5% of the overall portfolio at the time of investment. The LTIF also has passive allocations to both equities and bonds to help control costs as part of a broad-based effort to minimize the costs associated with managing the aggregate Endowment Fund.

Managers

While fossil fuel divestment is a central objective for the LTIF, we have also been working to identify investment strategies which offer proactive solutions to a range of social and environmental issues. Below we provide examples of managers in which the LTIF has invested in the past 12 months:

- **Global Equity: Lansdowne Clean Energy**

This strategy invests in companies that are well placed to take advantage of the transformational change occurring in energy generation, distribution, and consumption as both technology and regulation drive the shift to a lower-carbon economy. The strategy aims to back the long-term structural winners from this transition.

- **Global Equity: Ownership Capital**

This strategy focuses on sustainable long term investing, with an impressive combination of rigorous fundamental and ESG analysis and an exceptional level of constructive and tangible engagement with companies. ESG (environmental, social and governance criteria) is not pursued as a theme, but because it is believed such extra-financial analysis leads to better long term investment decisions.

- **Natural Resources Equities: GMO Climate Change**

This strategy invests in companies expected to benefit from the trend towards climate change mitigation and adaptation to clean energy (wind, solar), energy efficiency, agriculture, water sectors etc. Also, we negotiated formal exclusion of fossil fuel stocks as defined by the **Carbon Underground 200**.

- **Private Investments: Dementia Discovery Fund (DDF)**

This fund will invest in seed and early stage therapeutics and diagnostic companies specifically targeting the clinical area of Dementia. Managed by SV Health Advisors (SV), the fund has been formed in partnership with the UK Department of Health, leading pharmaceutical companies and United Kingdom charity Alzheimer's UK. The DDF will invest in 40-50 projects and companies based primarily in the UK and US.

- **Illiquid Diversifiers: Vision Ridge Sustainable II**

This fund will invest in asset-based growth opportunities that increase the efficiency and sustainability of real assets across four sectors: energy, water & agriculture, transportation and land.

4. Review of Investment Activities (cont.)

Risk

The objective of the LTIF is to maximize returns for a given level of risk. At the asset allocation policy level, the LTIF has four distinct components, as shown below.

		Macroeconomic hedges		
Four key roles	Growth dividers	Diversifiers	Inflation sensitive	Deflation hedge
	Goal: Generate growth to support longer - term objectives	Goal: Mitigate equity risk while attempting to improve overall risk/return profile	Goal: Provide protection in a period of sharp unexpected inflation	Goal: Provide protection in a period of economic contraction
Example asset classes	● Global developed equities ● Emerging market equities ● High yield credit ● Equity - oriented hedge funds ● Private equity and venture capital	● Balanced/multi - asset manager ● Investment grade credit ● Less directional hedge fund strategies ● Private credit	● Commodities ● Natural resource equities ● Private property ● Property equities ● Gold	● Government bonds ● Cash

The Growth Drivers allocation is focused on generating long-term growth for the LTIF and, as such, is focused on listed and private equity assets. The allocation to Diversifiers is intended to mitigate the volatility inherent in an equity-orientated portfolio. This portfolio component plays a particularly important role given the extended valuations we see in government bonds, which have historically served to dampen volatility effectively. The final two components of the portfolio, Inflation Sensitive and Deflation Hedging serve as insurance against two macro-economic risks that can undermine the purchasing power of the LTIF over the long-term, namely inflation and deflation. This long-term policy ensures that we take enough risk to meet our long-term investment objectives, but also limits potential drawdowns over shorter periods.

Over shorter periods we monitor risk in a number of ways, for example at the total portfolio level, the monitoring of beta (i.e. sensitivity to the broad equity market) and volatility (as measured by standard deviation) offer insight into the positioning of the portfolio.

We also consider the geographic and sector positioning of the listed equity allocations to ensure that portfolio positioning is in line with our view on relative valuations.

Another important consideration is the monitoring of currency risk. With future spending from the LTIF to be predominantly in sterling, there is a mismatch with the currency exposure of a globally diversified portfolio, where the dollar is the dominant currency, along with, to a lesser extent, the euro. We therefore use a passive currency overlay to hedge back the portfolio's currency to a sterling range of 40-70%.

5. Socially Responsible Investment

The Scott Trust believes that long-term sustainable investment returns are dependent on stable, well-functioning and well-governed social, environmental and economic systems. As a result, environmental, social and governance (ESG) considerations are fully integrated in the investment approach, in addition to the specific decision taken in 2015 to divest from fossil fuels over the medium term and re-invest in solutions to a low carbon economy.

Beyond this focus on climate change mitigation and adaptation, we also seek investments more broadly aligned with real world social and environmental norms since we believe these issues are both financially material and aligned with our own values. These policies are applied to the Endowment Assets in five key pillars:

1. **UN PRI:** proactively pursue commitments under United Nations Principles for Responsible Investment.
2. **Engagement:** we will engage with our investment managers on all aspects of responsible investment.
3. **ESG integration:** we aim to invest in managers taking a proactive approach to integrating ESG in a material way in their investment process.
4. **Proactive investments :** we are seeking to invest in areas delivering an environmental or social solution or impact.
5. **Divestment:** our investment fund has pledged to divest from fossil fuels over the medium term.

We aim to improve behaviour in the investment industry, disclosure, and the provision of new sustainable and responsible investment products. We are also developing our own collaborations, in order to engage with portfolio companies directly. We have joined both ShareAction's Charities Responsible Investment Network (CRIN) and the Institutional Investors Group on Climate Change (IIGCC).

GMG has achieved significant progress on all five areas of its plan as illustrated by the table below:

	UN PRI	Engagement	ESG integration	Proactive investments	Divestment
Progress made 2017/2018	Completed third annual report and receiving A or A+ for all modules. Completed the new 2018 voluntary module climate-related investment considerations.	Collaborated with managers and helped seed innovative new ESG products. Engaged with all asset managers in the portfolio, and reviewed all voting and engagement records.	Substantial re-allocations were made over the last year and a half of the portfolio is now invested in ESG integrated managers, well exceeding the initial 10% target.	Commitments to Proactive investments, delivering an environmental or social solution or impact comprise 5% of the portfolio.	Exposure of fossil fuels have been reduced by three quarters since divestment decision, well ahead of the target to halve by the end of 2017. Other decisions taken will continue to reduce remaining exposure.

5. Socially Responsible Investment (cont.)

In 2018 we have received A and A+ ratings for our UN PRI modules, the latter for the listed equity module, which is the largest single allocation for the Endowment Fund and where peers score B. We also completed a new voluntary pilot module (currently unassessed) focusing on climate-related indicators for investors based on the Taskforce for Climate Related Disclosure (TCFD) recommendations. We welcome this further innovation from UN PRI, given our focus on reducing climate related risk in our portfolio.

We have been one of the largest funds globally to divest from fossil fuels and reinvest in solutions to a low carbon economy. We are focused on doing this without sacrificing financial returns. We have been successful in changing investment managers' behavior and driving the creation of new products, which have subsequently attracted new capital. For example, in 2018 we seeded a new UCITS fund investing in companies aligned with climate change adaptation and mitigation launched by Grantham Mayo Van Otterloo & Co. (GMO). More generally, half of the portfolio is now invested in managers integrating ESG in a material way, well above our original 10% target.

Particularly noteworthy has been the growing availability of proactive investment opportunities offering commercial rates of returns while also having a positive impact.

We have now made commitments to seven different strategies in this area across multiple asset classes. Examples of new proactive commitments include a pan European private equity fund targeting businesses having a positive environmental impact, a venture capital strategy targeting dementia treatments, and sustainable private infrastructure fund investing across four sectors: energy, water and agriculture, transportation, and land. Themes targeted by this manager have included renewable power and energy storage, water trading and storage, energy efficiency and electric vehicle charging infrastructure.

We have been able to broaden the scope of our proactive investments pillar beyond investments in low carbon solutions and target broader social and environmental impact. Our investment team has devoted considerable time to this area over the last year and we have made great progress.