Baron Mid Cap Growth Strategy

BARON CAPITAL

September 30, 2019

Dear Investor:

Performance

Stocks experienced heightened volatility during the third quarter, as trade tensions between the U.S. and China dominated headlines. In addition, mixed global economic data combined with the inversion of the U.S. yield curve weighed on investor sentiment. Investors sought safety in perceived defensive sectors, such as Utilities and Consumer Staples. Real Estate also held up well, driven by yield-oriented REITs, which benefited from a declining interest rate environment. Energy was down the most in the quarter because of the continued decline in oil prices. Health Care was also under pressure because of rising support for Democratic presidential candidates who support Medicare for All, as well as uncertainty regarding other potential health care policy changes, such as measures to lower prescription drug prices.

Investors gravitated towards larger capitalization stocks for the third consecutive quarter. Among mid-caps, value stocks outperformed growth stocks. Against this backdrop, Baron Mid Cap Growth Strategy declined 2.33% while the Russell Midcap Growth Index (the "Index") fell 0.67%, and the S&P 500 Index gained 1.70%.

Table I.
Performance
Annualized for periods ended September 30, 2019

	Baron Mid Cap Growth Strategy (net)[1]	Baron Mid Cap Growth Strategy (gross)[1]	Russell Midcap Growth Index[1]	S&P 500 Index[1]
Three Months[2]	(2.33)%	(2.09)%	(0.67)%	1.70%
Nine Months[2]	29.32%	30.27%	25.23%	20.55%
One Year	8.19%	9.25%	5.20%	4.25%
Three Years	17.94%	19.11%	14.50%	13.39%
Five Years	13.31%	14.44%	11.12%	10.84%
Ten Years	14.56%	15.70%	14.08%	13.24%
Fifteen Years	10.77%	11.90%	10.53%	9.01%
Since Inception[3] (June 30, 1998)	8.73%	9.81%	8.16%	6.65%

Investments in Industrials and Financials, higher exposure to strong performing REITs within Real Estate, and lack of exposure to the lagging Energy sector added the most value. Favorable stock selection in Industrials was driven by data and analytics vendor **Verisk Analytics, Inc.** and

For Strategy reporting purposes, the Firm is defined as all accounts managed by Baron Capital Management, Inc. ("BCM") and BAMCO, Inc. ("BAMCO"), registered investment advisers wholly owned by Baron Capital Group, Inc. As of September 30, 2019, total Firm assets under management are approximately $29.1 billion. The Strategy is a time-weighted, total return composite of all mid-cap accounts greater than $1 million using our standard investment process. Since 2010, accounts in the Strategy are market-value weighted and are included on the first day of the month following one full month under management. Prior to 2010, accounts were included on the first day of the quarter after one full quarter. Gross performance figures do not reflect the deduction of investment advisory fees. Actual client returns will be reduced by the advisory fees and any other expenses incurred in the management of the investment advisory account. A full description of investment advisory fees is supplied in our Form ADV Part 2A. Valuations and returns are computed and stated in U.S. dollars. Performance figures reflect the reinvestment of dividends and other earnings. The Strategy is currently composed of one mutual fund managed by BAMCO and separately managed accounts managed by BCM. BAMCO and BCM claim compliance with the Global Investment Performance Standards (GIPS®). To receive a complete list and description of the Firm's Strategies or a GIPS-compliant presentation please contact us at 1-800-99BARON.

Performance data quoted represents past performance. Current performance may be lower or higher than the performance data quoted. Past performance is no guarantee of future results.

[1] The indexes are unmanaged. The Russell Midcap™ Growth Index measures the performance of medium-sized U.S. companies that are classified as growth and the S&P 500 Index of 500 widely held large-cap U.S. companies. The indexes and the Strategy are with dividends, which positively impact the performance results. Russell investment Group is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell is a trademark of Russell Investment Group.

[2] Not annualized.

[3] The Strategy has a different inception date than its underlying portfolio, which is 6/12/87.

consumer credit bureau **TransUnion**. Both companies saw their stock prices rise after reporting strong earnings results. Real estate information and marketing services company **CoStar Group, Inc.**, landscaping equipment manufacturer **The Toro Company**, and nuclear components and fuel supplier **BWX Technologies, Inc.** also performed well within the sector. Strength in Financials came from specialty insurer **Arch Capital Group Ltd.**, whose stock price rose over 13% during the quarter, driven by improving market conditions for commercial insurance and continued strength in mortgage insurance.

Investments in Health Care, Information Technology (IT), and Communication Services as well as the lack of exposure to the defensive Consumer Staples sector detracted the most from relative performance. Within Health Care, higher exposure to poor performing life sciences tools & services stocks through sizeable positions in **Mettler-Toledo International, Inc.** and **Illumina, Inc.** hurt relative results. Weakness in IT was driven by syndicated research provider **Gartner, Inc.**, which fell after reducing its full-year earnings guidance. Additionally, lack of exposure to semiconductor equipment stocks, which were up more than 25% in the Index, and underperformance of internet services & infrastructure companies **Wix.com Ltd.** and **Verisign, Inc.** hampered relative results. Communication Services holdings underperformed, with real estate website operator **Zillow Group, Inc.** leading the decline. Zillow's shares were down sharply due to expanded testing of the company's new Flex commission model, whereby the company takes a percentage of agents' commissions. While the new model will likely weigh on profitability in the short-to-medium term, we believe Flex will be accretive to long-term shareholder value.

Table II.
Top contributors to performance for the quarter ended September 30, 2019[1,2]

Verisk Analytics, Inc.
Arch Capital Group Ltd.
ANSYS, Inc.
Equinix, Inc.
TransUnion

Shares of **Verisk Analytics, Inc.**, a leading data and analytics vendor, gained after the company reported solid quarterly earnings results. Verisk's Insurance segment continued its strong performance, and both its Energy and Financial Services segments showed encouraging signs of improvement. We remain positive about the company's competitive positioning, defensive business model, long-term growth prospects, margin expansion potential, and its ability to effectively deploy its capital.

Arch Capital Group Ltd. is a specialty insurance and reinsurance company based in Bermuda. Its shares outperformed, as general market conditions for commercial insurance improved and the mortgage insurance market continued to perform well. Management took advantage of higher insurance rates to selectively underwrite additional new business. In addition, Arch reported solid earnings results, highlighted by 19% growth in its book value per share.

ANSYS, Inc. is a leading provider of physics-based simulation software used to evaluate how products will perform under various real-world environments. Its shares rose after ANSYS held its first analyst event in two years. Investors' overall takeaways were positive around changes in its go-to-market strategy. There was also optimism that a growing product line will enable the company to become a more strategic vendor for clients and increase its average selling price. The company's continued healthy sales growth has allowed it to keep generating substantial cash despite making prudent reinvestments into its business.

Equinix, Inc. is a global operator of network-dense, carrier-neutral colocation data centers. Shares increased because of its robust second quarter results, management's increase of full-year guidance, and the company's investment grade debt upgrade. The lower interest rate environment benefited REITs broadly as well. We retain conviction in Equinix because of the ongoing demand for cloud adoption and IT outsourcing. We believe that Equinix's unique position as one of the only operators that can offer a global platform is an important competitive differentiator.

TransUnion is a consumer credit bureau that helps businesses make credit and marketing decisions. Its shares performed well after the company reported quarterly results that beat street forecast and raised its full-year guidance. Revenue grew 18% and EBITDA grew 20%, with organic, constant-currency revenue growth accelerating to 10% as its bank customers resumed spending on marketing, health care demand improved, and year-over-year comparisons eased. We continue to own the stock because we expect TransUnion to generate industry-leading growth while diversifying into additional information services segments.

Table III.
Top detractors from performance for the quarter ended September 30, 2019[1,2]

Mettler-Toledo International, Inc.
Gartner, Inc.
Illumina, Inc.
FactSet Research Systems, Inc.
SmileDirectClub, Inc.

Shares of weighing instruments manufacturer **Mettler-Toledo International, Inc.** detracted from performance. The company reported quarterly financial results that fell slightly short of investor expectations because of weakness in its non-core food retailing business. Given Mettler's large presence in China, the President's intense trade war rhetoric during the quarter compounded the stock's weakness. We continue to believe Mettler is a good business with stable growth, strong pricing power, robust free cash flow, and shareholder-friendly management.

Shares of **Gartner, Inc.**, a provider of syndicated research, detracted from performance after the company reduced its full-year guidance. Although forward-looking metrics in Gartner's traditional IT research business decelerated modestly, they remain at a robust low-teens growth rate. The company also chose to discontinue several non-subscription products, which will hurt profitability this year but are not core to its long-term

1 Top contributors, top detractors, and top 10 holdings are based on a representative account. Such data may vary for each client in the Strategy due to asset size, market conditions, client guidelines, and diversify of portfolio holdings. The representative account is the account in the Strategy that we believe most closely reflects the current portfolio management style for the Strategy. Representative account data is supplemental information.

2 Based on the gross performance results of the representative account.

strategy. Finally, the company was more successful than expected in filling its open sales force positions, which should reduce this year's earnings while driving faster revenue growth in 2020.

Shares of **Illumina, Inc.** fell after the market-leading manufacturer of next generation DNA sequencing systems and consumables reported a revenue miss and lowered revenue guidance for the year. The shortfall was due to delays in population genomics programs, slower growth in the consumer genomics market, and a slowdown in sales of certain low throughput sequencing instruments. We continue to believe Illumina has a long runway for growth driven by expanding applications and utilization of DNA sequencing technologies.

Shares of **FactSet Research Systems, Inc.**, a leading provider of investment management tools, declined during the quarter after the company reported weak guidance for 2020 while also announcing a new three-year investment plan to accelerate revenue growth. This hurt the stock because it led analysts to presume that corporate margins will not increase for a couple of years.

We were excited by the business prospects for dental aligner company **SmileDirectClub, Inc.**, including its large addressable market, first mover advantage, unique vertically integrated business model, and commanding direct-to-consumer presence. However, the company's IPO performed poorly, with shares opening below deal price and trading down sharply from there. It became apparent to us that shares had been mispriced and poorly placed by underwriters who greatly misjudged demand for the company stock. We felt it was best to limit our losses and exit the position.

Portfolio Structure

At September 30, 2019, Baron Mid Cap Growth Strategy held 58 positions. The Strategy's 10 largest holdings represented 38.9% of assets, and the 20 largest represented 60.8% of assets. The Strategy's largest weighting was in the IT sector at 26.8% of assets. This sector includes software companies, IT consulting businesses, data processing firms, and internet services and infrastructure companies. The Strategy held 22.8% of its assets in the Health Care sector, which includes investments in life sciences, health care equipment, health care supplies, health care technology, and biotechnology companies. The Strategy held 17.9% of its assets in the Industrials sector, which includes investments in research and consulting companies, industrial conglomerates, and machinery companies. The Strategy also had significant weightings in Financials at 12.1% of assets and Consumer Discretionary at 8.4% of assets.

Table IV.
Top 10 holdings as of September 30, 2019[1]

IDEXX Laboratories, Inc.
Gartner, Inc.
Verisk Analytics, Inc.
Mettler-Toledo International, Inc.
Guidewire Software, Inc.
Vail Resorts, Inc.
ANSYS, Inc.
Verisign, Inc.
CoStar Group, Inc.
TransUnion

[1] Based on the representative account

Recent Activity

During the past quarter, the Strategy established 4 new positions and added to 14 others. The Strategy eliminated 7 positions and reduced its holdings in 4 others.

Table V.
Top net purchases for the quarter ended September 30, 2019[1]

Clarivate Analytics Plc
Alexandria Real Estate Equities, Inc.
argenx SE
Amphenol Corporation
Gartner, Inc.

[1] Based on the representative account

Clarivate Analytics Plc provides comprehensive intellectual property and scientific information that allow various types of clients (including academia, governments, corporations, and the legal community) to discover and commercialize new ideas, while also helping to protect content, patents, and brands. Clarivate operates several brands that are well known in the broad scientific community, including Web of Science (scientific and academic research), Cortellis (pharmaceutical and biotechnology intelligence), Derwent Innovation (patent analytics), CompuMark (trademark protection), and MarkMonitor (domain brand protection).

We believe that Clarivate has an attractive business model, similar to that of other leading companies in the information services sector. The company's key assets are its highly valuable proprietary databases–Clarivate is the #1 or #2 player in nearly every market in which it operates. Its databases are combined with analytical tools that help users apply the underlying data to everyday business problems. The proprietary data and accompanying analytics become an important part of the end users' daily workflow, creating a sticky and predictable business model (>80% subscription revenue) with high levels of recurring revenue (>90% revenue retention). In addition, we are particularly impressed by CEO Jerre Stead, who was previously the longtime CEO of IHS Markit (a $27 billion company) and has served on more than 30 corporate boards during his career.

Since much of the company's required investment is in collecting the underlying data and creating the analytical tools, we believe that Clarivate should have high operating leverage ("build it once, sell it many times"), with sales of new subscriptions carrying high incremental margins. This natural operating leverage along with targeted cost synergies should help increase its margins during the next couple of years. Customers typically pay Clarivate up front on an annual basis and the business has low capital requirements; both these factors should result in strong free cash flow generation.

We believe that Clarivate is poised to accelerate its revenue growth. After its recent history of low single-digit organic growth, the company is planning to exit 2020 with a 4% to 6% organic growth rate. This growth acceleration will be driven by a number of factors, including positive tailwinds around the growth of predictive analytics and data, product and pricing enhancement strategies, growth in the Asia Pacific region, an increased focus on subscription revenue, cross/up-selling across the existing client base, and an overall improvement in the management of the business. Once the company reduces its leverage, M&A is also likely to be a driver of incremental growth, as management sees a robust pipeline of potential acquisition targets. We believe that Clarivate will be a steady earnings compounder, which should drive solid returns for the stock over a multi-year period.

Table VI.
Top net sales for the quarter ended September 30, 2019

Align Technology, Inc.
Fastenal Co.
First Republic Bank
FactSet Research Systems, Inc.
A. O. Smith Corporation

We exited our position in **Align Technology, Inc.**, the manufacturer of Invisalign-brand orthodontic devices, over concerns increased competition in the market for teeth-straightening solutions. We exited our position in industrial distributor **Fastenal Co.** over concerns about e-commerce firms entering the distribution industry. We reduced our stake in **First Republic Bank** because of concerns about its ability to grow its profitability given an increasingly unfavorable interest rate environment for banks. We reduced our stake in **FactSet Research Systems, Inc.** because of concerns about slowing growth in certain of its end markets. We exited our position in **A. O. Smith Corporation**, a manufacturer of water heating and treatment devices, over concerns about problems in the company's important Chinese market.

Outlook

Throughout the past decade's bull market, prominent market commentators and strategists have offered various reasons to sell equities. However, investors that have ignored "short-term noise" in the stock market while pursuing a long-term "buy and hold" strategy have generally been richly rewarded. We believe this straightforward method remains the best approach for investors to follow.

We continue to remain optimistic that the prospects for U.S. equities are bright. We believe that the U.S. economy remains generally robust and that the outlook for continued earnings growth from the companies in our portfolio is solid. The U.S. unemployment rate remains at historically low levels, and most leading economic indicators remain encouraging. Inflation is muted, and the Federal Reserve seems poised to ensure that interest rates remain at historically low levels.

We believe that our portfolio of well-managed, competitively advantaged, fast growing companies will continue to perform well, although we cannot guarantee that they will. We continue to believe that high-quality, mid-sized growth stocks represent a compelling long-term investment opportunity.

Sincerely,

Andrew Peck
Portfolio Manager

The performance of accounts in the Strategy may be materially different at any given time. Differences that may affect investment performance include cash flows, inception dates, and historical prices. Positions may not be the same or may be traded at different times. In addition, accounts in the Strategy may be pursuing similar investment strategies, but may have different investment restrictions.

The Adviser believes that there is more potential for capital appreciation in mid-sized companies, but there also may be more risk. Specific risks associated with investing in mid-sized companies include that the securities may be thinly traded and they may be more difficult to sell during market downturns. Prior to February 15, 2007, the Strategy invested primarily in small and mid-sized growth companies. Since then, the Strategy invests in mid-sized companies. The Strategy may not achieve its objectives. Portfolio holdings are subject to change. Current and future portfolio holdings are subject to risk.

The discussions of the companies herein are not intended as advice to any person regarding the advisability of investing in any particular security. The views expressed in this report reflect those of the respective portfolio managers only through the end of the period stated in this report. The portfolio manager's views are not intended as recommendations or investment advice to any person reading this report and are subject to change at any time based on market and other conditions and Baron has no obligation to update them.