Baron Emerging Markets Strategy

September 30, 2020

Dear Investor:

Performance

Baron Emerging Markets Strategy gained 12.98% (net of fees) for the third quarter of 2020, while its principal benchmark index, the MSCI EM Index, appreciated 9.56%. The MSCI EM IMI Growth Index gained 14.11% for the quarter. The Strategy outperformed its principal benchmark index, while trailing the all-cap growth proxy, in a quarter that was in many ways an extension of the previous one, as global equities delivered solid returns with broad-based participation. Emerging market ("EM") and international equities largely kept up with their U.S. counterparts, while various sectors exhibited pockets of intermittent leadership with no clear change in the market's overall tone. Progress continued with clinical trials for vaccines and therapies to address the COVID-19 health crisis, though some uncertainty remains as to when large-scale vaccination may be achievable and whether adequate scale of fiscal support will be forthcoming in the interim. Though a market correction began late in the third quarter, in our view related to uncertainty regarding a U.S. "Phase 5" fiscal stimulus package as well as the upcoming election, we remain optimistic. Looking forward, we have increasing conviction that COVID-19 will prove to have been the catalyst that pushed global policymakers through the portal of "Modern Monetary Theory," or what we call "populist QE." We believe this, together with the emergence of government-directed lending programs, credit guarantees and grants, may well usher in a regime change for market leadership, favoring equities over fixed income, and sparking a sustainable period of outperformance for EM and international equities. Further, we reiterate our view that the changing tone of relations between the U.S. and China presents compelling opportunities for long-term and bottom-up fundamental investors. As always, we are confident that we have invested in many well-positioned and well-managed companies on a bottom-up basis, which are poised to benefit from several long-term and attractive investment themes.

Table I.
Performance
Annualized for periods ended September 30, 2020

	Baron Emerging Markets Strategy (net)[1]	Baron Emerging Markets Strategy (gross)[1]	MSCI EM Index[1]	MSCI EM IMI Growth Index[1]
Three Months[2]	12.98%	13.24%	9.56%	14.11%
Nine Months[2]	7.44%	8.19%	(1.16)%	11.58%
One Year	17.72%	18.83%	10.54%	26.37%
Three Years	3.50%	4.47%	2.42%	6.76%
Five Years	9.65%	10.71%	8.97%	12.11%
Since Inception[3] (January 31, 2011)	5.92%	6.68%	2.13%	4.54%

For the third quarter of 2020, we outperformed our primary benchmark, the MSCI EM Index, while trailing our all-cap EM growth proxy. We continue to comfortably outperform our primary benchmark for the year-to-date period. We had very solid performance and stock selection results across the portfolio. From a sector or theme perspective, our Digitization (**Alibaba Group Holding Limited**, **Meituan Dianping**, **Reliance Industries Limited**, and **Tata Communications Limited**) and China value add/localization (**S. F. Holding Co., Ltd.**, **China Tourism Group Duty Free Corporation Limited, Midea Group Co., Ltd.**, and **Hangzhou Hikvision Digital Technology Co., Ltd.**) themes contributed the most. In addition, strong stock selection in the Energy sector, led by our large overweight position in **Reliance Industries Limited** was a key contributor to relative outperformance. We think classifying Reliance in the Energy sector is a misnomer, as we remain excited about the company not so much for its energy assets but for it being a play on "Digital India." Reliance is well positioned to emerge as the "Amazon/Facebook/Netflix" of India, and we believe its digital and retail businesses already represent a solid majority of

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, 2020, total Firm assets under management are approximately $38.2 billion. Gross performance figures do not reflect the deduction of investment advisory fees and any other expenses incurred in the management of the investment advisory account. 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 the Firm's 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, a Collective Investment Trust, a multipartner SICAV fund, and a subadvised account managed by BAMCO; and a separately managed account and a private offshore fund managed by BCM. The Strategy invests mainly in non-U.S. companies of all sizes. The majority of investments are in companies domiciled in developing countries. The Strategy may invest up to 20% in companies in developed and frontier countries. 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 MSCI EM (Emerging Markets) IMI indexes cited are unmanaged, free float adjusted market capitalization weighted indexes reflected in U.S. dollars. The MSCI EM (Emerging Markets) IMI Growth Index Net USD and the MSCI EM (Emerging Markets) IMI Index Net USD are designed to measure equity market performance of large-, mid- and small-cap securities in the emerging markets. The MSCI EM (Emerging Markets) IMI Growth Index Net USD screens for growth-style securities. The indexes and Baron Emerging Markets Strategy include reinvestment of dividends, net of foreign withholding taxes, which positively impact the performance results.

[2] Not annualized.

[3] The Strategy has a different inception date than its underlying portfolio, which is December 30, 2010.

the company's value. Our Fintech (**StoneCo Ltd.**) theme and India wealth management and consumer finance investments (**Bajaj Finance Limited**, **Max Financial Services Limited,** and **JM Financial Limited**) also contributed to strong relative performance. From a country perspective, strong stock selection across the board in China (China Tourism Group, **Xiaomi Corporation**, S. F. Holding Co., Ltd., and **Shenzhou International Group Holdings Ltd.**), as well as in Brazil, Taiwan, and Russia, contributed the most. Our overweight position in India also added value as equities in the country responded well to an uptick in economic activity after the national lockdown was lifted. While the breadth of portfolio performance was very good during the quarter, weak stock selection in Korea (**Korea Shipbuilding & Offshore Engineering Co., Ltd.**) and the UAE (**Network International Holdings Ltd.**), and our modest cash position in a rising market, both detracted from relative performance.

Table II.
Top contributors to performance for the quarter ended September 30, 2020

	Percent Impact
Alibaba Group Holding Limited	1.95%
Taiwan Semiconductor Manufacturing Company Ltd.	1.30
Reliance Industries Limited	0.91
Xiaomi Corporation	0.75
China Tourism Group Duty Free Corporation Limited	0.67

Alibaba Group Holding Limited is the largest retailer and e-commerce company in China. Alibaba operates shopping platforms Taobao and Tmall and owns 33% of soon-to-be publicly traded Ant Financial, which operates Alipay, China's largest third-party online payment provider. Shares of Alibaba were up on a sustained recovery in e-commerce driven by an increase in purchase frequency and spend per order. We believe Alibaba's core business remains highly profitable, complemented by rapid growth in the cloud business and inflection in the Cainiao logistics and New Retail segments.

Taiwan Semiconductor Manufacturing Company Ltd. had another outperforming quarter as demand for its leading-edge processing technology remained robust, driven by visible end market growth in 5G and high performance computing applications. Taiwan Semi continued to gain share in top tier clients. Intel's decision to possibly outsource its next generation chip manufacturing to Taiwan Semi further demonstrated its superior competitive advantages. We believe Taiwan Semi is likely to outpace its long-term growth target of 5%-10% topline CAGR in the next five years.

Reliance Industries Limited contributed to performance. As India's leading conglomerate, with business interests in telecom, digital services, retail, and oil refining, the company is benefiting from accelerated adoption of 4G connectivity and digital services. The company raised more than $20 billion from strategic (Facebook/Google) and financial investors in its "Jio Platforms" and "Reliance Retail" business verticals. We retain conviction as we believe Reliance is a key beneficiary of a "Digital India" with potential to emerge as the "Amazon/Facebook/Netflix" of India.

Xiaomi Corporation, a Chinese electronics company, contributed to performance on profits from its smartphone shipment and services division that beat Street expectations. Xiaomi gained share in both China and overseas markets as a result of competitor Huawei's inability to obtain chip supplies and damaged brand image. We continue to believe in Xiaomi's long-term growth prospects as it improves its product mix toward high-end models and expands its services and IoT segment.

China Tourism Group Duty Free Corporation Limited, the largest operator of duty free shops in China, contributed to performance on strong pent up demand and favorable government policy. During the period, the company also successfully rolled out online duty free shopping to complement the existing offline presence. We retain conviction as duty free penetration rates increase in China coupled with the company's ability to drive growth from expansion, product mix improvement, and value-added services.

Table III.
Top detractors from performance for the quarter ended September 30, 2020

	Percent Impact
Bharti Airtel Limited	–0.20%
Network International Holdings Ltd.	–0.18
LexinFintech Holdings Ltd.	–0.16
Sino Biopharmaceutical Ltd.	–0.16
Rumo S.A.	–0.14

Bharti Airtel Limited detracted from performance as a result of passive selling pressure due to sizable rebalancing in major indexes such as MSCI and FTSE. We retain conviction. As a leading mobile services operator in India, Bharti continues to gain market share as the Indian telecom sector transitions into a quasi-duopoly. We also believe Bharti will benefit from a likely government-mandated data pricing floor. Finally, we think mobile tariffs can double over the next five years, which should generate meaningful upside for shareholders.

Network International Holdings Ltd. is a leading payment processor in the Middle East and Africa. Weakness in the share price was driven by first half financial results that were negatively impacted by the pandemic. Revenue fell 12% and EBITDA fell 31% due to a rapid drop in spending and tourism. The company also announced an acquisition that received a mixed reaction from investors and required an equity raise. We remain invested because we believe the pandemic's impact on performance is temporary and the company should benefit from increasing adoption of electronic payments.

LexinFintech Holdings Ltd. is an online consumer lending platform in China. Shares fell after China's Supreme People's Court announced guidelines effectively capping the court-protected interest rate charged on loans. The guidelines do not apply to licensed financial institutions and are not supported by the banking regulator, so it remains unclear what the impact to the company will be. Nevertheless, the stock reacted negatively to the announcement. We have identified regulation a key risk in our thesis for Lexin but believe the current valuation already discounts such risk.

Sino Biopharmaceutical Ltd. detracted from performance following an earnings miss. We retain conviction. As China's leading pharmaceutical player, the company is well-positioned to benefit from growing demand for health care services in the country. The company's focus on R&D and robust product pipeline should generate double-digit earnings growth for the next three to five years, in our view. A fast-changing government regulatory landscape should also favor established innovative pharmaceutical companies such as Sino Bio.

Rumo S.A. is the largest independent rail concessionaire in Brazil, transporting largely agricultural commodities and fertilizers across Brazil to export markets in Europe and Asia. The shares have been weak after Rumo raised capital to make advance payments in concession fees. We still like the company. Rumo is now well-capitalized to continue executing on the plan to expand its throughput on its existing network by at least 50% over the next three years in addition to new concessions. We also expect continued progress in lowering the company's fixed cost per ton moved.

Portfolio Structure

Table IV.
Top 10 holdings as of September 30, 2020[1]

	Percent of Net Assets
Alibaba Group Holding Limited	6.4%
Tencent Holdings Limited	4.2
Taiwan Semiconductor Manufacturing Company Ltd.	3.5
Samsung Electronics Co., Ltd.	3.4
Reliance Industries Limited	3.1
Zai Lab Limited	2.1
Dr. Reddy's Laboratories Ltd.	1.7
Techtronic Industries Co. Ltd.	1.7
China Conch Venture Holdings Ltd.	1.7
Midea Group Co., Ltd.	1.5

Exposure By Country

Table V.
Percentage of securities by country as of September 30, 2020

	Percent of Net Assets
China	42.6%
India	20.6
Brazil	7.7
Taiwan	4.9
Korea	4.3
Russia	3.1
Mexico	3.0
Hong Kong	2.4
Philippines	1.0
Japan	0.9
South Africa	0.8
Thailand	0.5
United Arab Emirates	0.3
Norway	0.3
Hungary	0.1

Exposure by Market Cap: The Strategy may invest in companies of any market capitalization, and we have generally been broadly diversified across large-, mid-, and small-cap companies, as we believe developing world companies of all sizes can exhibit attractive growth potential. At the end of the third quarter of 2020, the Strategy's median market cap was $16.3 billion, and we were invested 50.1% in giant-cap companies, 35.1% in large-cap companies, 5.8% in mid-cap companies, and 1.3% in small- and micro-cap companies as defined by Morningstar, with the remainder in cash and private securities.

Recent Activity

During the third quarter of 2020, we added several new ideas toward existing themes while also increasing position sizing on recent investments reduce the number of positions in the portfolio while adding concentration to our high-conviction ideas. that were made earlier in the year. We continue our endeavor to modestly

During the quarter, we initiated a position in **Yum China Holdings Inc.**, the master franchisee and operator of KFC and Pizza Hut restaurants in China, which was spun out of its U.S.-listed franchisor, Yum! Brands Inc., in 2016. In our view, Yum China is one of the best restaurant operators globally. It has the most well-known and most-localized brand among western restaurant concepts in China, having entered the market before any of its peers in the late 1980s. In a highly competitive industry being disrupted by new technologies and delivery aggregators, we believe at-scale operators that have invested aggressively in technology and have actively reconfigured their businesses around digital and delivery will emerge as long-term winners. These are exactly the traits that we believe characterize Yum China. The company benefits from a best-in-class in-house food service supply chain and years of front-footed investments in digital ordering capabilities, loyalty, and an in-house delivery fulfillment network that is unparalleled among restaurant operators. Unit economics at KFC, which represents 90% of operating income, are best-in-class, with new units yielding a two-year payback, a number that has improved as Yum China has developed smaller units configured around ever greater delivery and off-premise consumption. A laser focus on efficiency is evident in Yum China's continued margin expansion over the last five years, despite persistent wage inflation. The company's ability to innovate on store sizing and double its KFC unit openings from about 350 in 2015 to over 700 in 2019 on a similar capex budget is commendable. The business is highly cash generative and capital allocation has been solid with management returning over 50% of free cash to shareholders in recent years. We believe this will continue or accelerate in the coming years as the balance sheet is overcapitalized. We believe Yum China can double its unit count from roughly 10,000 today over the next decade with potential acquisitions and/or return of capital augmenting investor returns over that time period.

As part of our China value add/localization theme, we re-initiated a position in **Han's Laser Technology Industry Group Co., Ltd**, a leading integrated laser equipment manufacturer in China. In our view, the company's earnings will continue to recover and expand over the next several years driven by form factor change in 5G smartphones, localized production of PCBs, general demand acceleration post COVID-19, and long-term investment in advanced technologies. The company is accelerating R&D efforts in mission critical segments such as EuV machines to help drive China's technology localization efforts. We maintain conviction in Han's Laser's competitive positioning as one of the best direct plays in China's manufacturing upgrade theme.

[1] Top 10 holdings, percentages of securities by country, and recent activity 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.

We recently participated in the IPO of **Li Auto Inc.**, which is one of China's leading electric vehicle ("EV") companies. We believe that Li Auto is well positioned to capture a large share of the premium EV/SUV market in China and later expand into mass market EVs, which is a large addressable market. We have looked at a number of EV companies outside of the U.S. and have largely passed on them due to questions over the long-term business model and/or execution related risk, but we think Li Auto is different. We are impressed by the management team, the founder's successful track record at Autohome, and in particular their targeted approach based on a sophisticated understanding of Chinese auto consumers. We think that Li Auto's unique EREV hybrid technology positions it well against both incumbent conventional ("ICE") vehicles and other new entry EVs by offering the competitive pricing of ICE vehicles while also delivering attractive range efficiency, driving performance and smart features inherent in EVs. The company has strong vehicle gross margins and a lean and efficient sales and R&D structure that differentiates it from most Chinese peers. Finally, we believe the company is investing for the future in several advanced technologies, including automated driving, suggesting a long runway for potential growth.

Finally, we increased several newer positions during the quarter, notably **XP Inc.**, **Hong Kong Exchanges and Clearing Limited**, **Muthoot Finance Ltd.**, **Localiza Rent a Car S.A.**, and **Beijing Oriental Yuhong Waterproof Technology Co., Ltd**.

During the quarter, we opportunistically exited several positions, most notably **WH Group Limited**, **PT Telekom Indonesia (Persero) Tbk**, and **PT Tower Bersama Infrastructure, Tbk**. In our endeavor to increase concentration in holdings where we have highest conviction in quality and return potential, while eliminating lower conviction or smaller holdings over time, we also exited positions in **Sunny Optical Technology Group**, **Globant, S.A.**, **Ginko International Co., Ltd.**, **KB Financial Group, Inc.**, and **Eclat Textile Co., Ltd.**

Outlook

The third quarter of 2020 was in many ways an extension of the second, with global equities delivering solid returns with broad-based participation. EM and international equities largely kept up with their U.S. counterparts, while various sectors exhibited pockets of intermittent leadership with no clear change in the market's overall tone. Progress continued with clinical trials for vaccines and therapies to address the COVID-19 health crisis, though some uncertainty remains as to when large-scale vaccination may be achievable and whether adequate scale of fiscal support will be forthcoming in the interim.

The market's message through much of the past quarter, however, has been clear. The global economy is progressing towards reopening and normalization. In most countries, consumer spending and utilization measures of public and private transportation are recovering substantially, while certain activities such as travel remain subdued. With few signs of troubling credit issues and a fair portion of record stimulus still in the pipeline, markets are largely looking through ongoing COVID disruption in favor of long-term earnings potential and full normalization over a reasonable time frame.

Late in the quarter, a global market correction emerged, in our view largely a result of the failure of the U.S. Congress to pass a meaningful "Phase 5" stimulus package, uncertainty regarding Brexit and economic growth in Europe, as well as the U.S. election, its integrity, and how the immediate post-election period will play out. Finally, as the fourth quarter began, indications of a potential second wave of virus began to emerge in various countries. While we see this market consolidation as part of the ongoing ebb and flow of the interplay between the path of the virus, the near-term outlook for the economy, interest rates and inflation, and the U.S. election and related politics, we remain believers that global authorities will continue to underwrite adequate policy support to provide a bridge to a full recovery, and that most publicly traded businesses will ultimately arrive at earnings potential without the need for dilutive capital issuance. In other words, notwithstanding some near-term noise, policymakers have rolled out a shiny bazooka, and we remain optimistic, particularly with regard to the companies in which we are invested.

In last quarter's letter we described how we had strategically approached COVID beneficiaries, COVID-impacted and COVID-impaired businesses. We are confident that adjustments to our holdings along this logic has been additive to our returns, with several newer positions among our higher percentage return investments during the quarter. In addition, higher-quality growth companies with strong market positions and healthy balance sheets are consolidating markets and gaining share. This is a global phenomenon benefitting many of our portfolio companies which also helps reconcile the performance of many publicly traded equities with COVID-challenged economic growth. We also suggested last quarter that rising geopolitical tension between the U.S. and China was creating significant opportunities for investors in domestic Chinese businesses and their supply chains seeking to displace profit share from Western multi-nationals in a variety of value-added industries. We believe this has been a material driver of the leadership and success of our China-related investments in the year-to-date period, and we believe we are in the early innings of substantial value creation.

Finally, we reiterate our view that the COVID crisis has vaulted the world's policymakers through the portal of "Modern Monetary Theory," or fiscal expansion funded by money printing and central bank balance sheet expansion. More recently, we appear to have entered the early stages of politicians hijacking the levers of monetary policy through targeted and subsidized lending, credit guarantees and government grants. This "populist QE" will likely prove to be a very different type of stimulus, one that could challenge consensus views on inflation expectations and sustainable nominal economic growth, and ultimately lead to a change in capital allocation and market leadership favoring equities over fixed income, and in particular EM and international equities and currencies. We are increasingly confident, that as the end of COVID disruption eventually comes into view, we are likely to enter a sweet spot for EM equities.

Sincerely,

Michael Kass
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.

In addition to the general stock market risk that securities may fluctuate in value, investments in developing countries may have increased risks due to a greater possibility of: settlement delays; currency and capital controls; interest rate sensitivity; corruption and crime; exchange rate volatility; and inflation or deflation. The Strategy invests in companies of all sizes, including small and medium sized companies whose securities may be thinly traded and more difficult to sell during market downturns. 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 manager 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.

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