Baron Emerging Markets Strategy

June 30, 2020

Dear Investor:

Performance

Baron Emerging Markets Strategy gained 26.71% (net of fees) for the second quarter of 2020, while its principal benchmark index, the MSCI EM Index, appreciated 18.08%. The MSCI EM IMI Growth Index gained 22.76% for the quarter. The Strategy handily outperformed its principal benchmark index, as well as the all-cap growth proxy, for the quarter as markets recovered strongly after substantial COVID-19-related declines during the first quarter. In our first quarter letter, we suggested that markets should at a minimum stabilize as greater clarity emerges regarding a peak in case counts, availability of testing, therapeutic options, and progress towards a vaccine. We also noted evidence that the unprecedented and global policy response was achieving its desired effect, and could act as a bridge to the restart of economies and the normalization of corporate earnings. After lagging early in the quarter, we were encouraged that emerging market ("EM") equities finished quite strong and largely kept pace with U.S. and global equity benchmarks for the period. Looking forward, we continue to believe that COVID-19 will be the catalyst that likely confirms a policy shift through the portal of Modern Monetary Theory, or what we call populist quantitative easing ("QE"), which we expect will lead to a shift in relative performance in favor of non-U.S. equities, as well as a U.S. dollar bear market. We have taken advantage of recent market events to further concentrate our portfolio in attractive long-term themes and companies that are well positioned to prosper from significant catalysts, reforms, and trends that we believe will remain in place for many years. Also, we believe the evolving and complex relationship between the U.S. and China represents a tectonic shift in geopolitics that is by no means a reason to disfavor investing in China or EM more broadly, rather it is creating exciting long-term investment opportunities for forward looking and bottom-up investors such as ourselves.

Table I.
Performance
Annualized for periods ended June 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]	26.71%	27.01%	18.08%	22.76%
Six Months[2]	(4.90)%	(4.46)%	(9.78)%	(2.21)%
One Year	0.74%	1.69%	(3.39)%	8.32%
Three Years	2.62%	3.60%	1.90%	5.30%
Five Years	3.78%	4.78%	2.86%	5.28%
Since Inception[3] (January 31, 2011)	4.71%	5.46%	1.21%	3.21%

For the second quarter of 2020, we comfortably outperformed our primary benchmark, the MSCI EM Index, as well as the all-cap EM growth proxy, and we have now outperformed our primary benchmark for the year-to-date period. From a broad market perspective, second quarter performance was largely a reversal of first quarter performance. Under the surface, however, second quarter performance was marked by broad swings in relative performance between groups we define as COVID beneficiaries, COVID-impacted, and COVID-impaired businesses, countries, and currencies. Early in the quarter COVID beneficiaries staged impressive rallies, while the impacted and impaired businesses began to catch up late in the quarter. We were pleased to deliver a strong quarter of absolute and relative performance with broad-based participation across several themes, and we added to several high-quality positions even though COVID disruption impacted them in the short term. In addition, we sold some COVID-

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 June 30, 2020, total Firm assets under management are approximately $32.5 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 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.

The performance data quoted represents past performance. Past performance is no guarantee of future results.

The Strategy's 1-year historical performance was impacted by gains from IPOs and/or secondary offerings. There is no guarantee that these results can be repeated or that the Strategy's level of participation in IPOs and secondary offerings will be the same in the future.

[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.

impaired investments, such as airlines, late in the quarter on strength, thereby upgrading the overall portfolio quality in a post-COVID context. While we had solid performance and stock selection across the portfolio, from a sector perspective our Information Technology investments, led by our mobile e-commerce and cloud/SaaS software themes (**Glodon Company Limited**, **Kingdee International Software Group Co. Ltd.**, and **Kingsoft Corporation Ltd.**) and Brazilian fintech (**PagSeguro Digital Ltd.** and **StoneCo Ltd**.) contributed the most. In addition, strong stock selection in the Financial sector, led by our India wealth management and consumer finance theme (**Max Financial Services Limited**, **Bajaj Finance Limited**, and **Edelweiss Financial Services Limited**), as well as our capital markets-related investments in Brazil (**B3 S.A. – Brasil, Bolsa, Balcao** and **XP Inc.**), contributed to strong relative performance. From a country perspective, strong stock selection in China, driven by our China value-added/localization theme (**Zai Lab Limited**, **China Tourism Group Duty Free Corporation Limited**, **Hua Hong Semiconductor Limited**, **Sino Biopharmaceutical Ltd.**, and **GDS Holdings Limited**), as well as in India and Brazil, our two largest overweight countries, contributed the most. Our underweight position in the Materials sector and our modest cash position in a strong market detracted from relative performance.

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

	Percent Impact
Tencent Holdings Limited	1.38%
Zai Lab Limited	1.30
Reliance Industries Limited	1.18
China Tourism Group Duty Free Corporation Limited	0.99
PagSeguro Digital Ltd.	0.96

Tencent Holdings Limited operates the leading social network and messaging platforms in China (QQ, WeChat), the largest online entertainment and media business in China, and the largest online PC and mobile gaming business in China. Shares of Tencent were up on strong first quarter results as the pandemic drove increased time spent on Tencent platforms and strong performance in smartphone gaming. Long term, we believe Tencent can grow each of its large business segments for years to come given its track record of execution, scale, and unique and diversified online assets.

Zai Lab Limited is a Chinese biotechnology company in-licensing drugs from developed countries to introduce to the Chinese health care market. Shares increased given a favorable reception to its recent in-licensing deal with Regeneron. The deal continues to cement Zai as a partner of choice for Western medicines in the China market. Recent commercial launches of two drugs for cancer treatment by Zai and a strong China health care market broadly should also help drive positive sentiment toward the company, in our view.

Reliance Industries Limited is India's leading conglomerate, with business interests that include oil refining, petrochemicals, media, telecommunications, and retail. Shares increased after the company sold a 25% stake in Jio Platforms for more than $15 billion to a number of strategic and financial investors including Facebook, KKR, and Silver Lake. This is a very large capital raise for an Indian company, and we see it as a vote of confidence by outside investors in Reliance's e-commerce growth opportunity in India. We believe earnings can grow 15%-18% CAGR over the next five years.

China Tourism Group Duty Free Corporation Limited, the largest operator of duty-free shops in China, contributed to performance in the quarter on reports of new policies that support the province of Hainan in becoming a free trade center and easing duty-free purchasing restrictions. As the market leader in the duty-free sector, China Tourism Group is poised to capture significant incremental growth, underpinned by domestic travel and consumption upgrade, in our view.

PagSeguro Digital Ltd. is a merchant acquirer and digital payments solution provider in Brazil catering primarily to the micro-merchant segment. Shares increased as the company experienced a rebound in payment volumes within its core segment that exceeded investor expectations, demonstrating that the company's clients were more resilient to COVID-19-related business interruptions. We retain conviction in PagSeguro as a leading player in the growing market for electronic payments in Brazil.

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

	Percent Impact
Guangzhou Automobile Group Company Limited	–0.24%
Haitong Securities Co., Ltd.	–0.09
Infraestructura Energetica Nova S.A.B. de C.V.	–0.05
China Conch Venture Holdings Ltd.	–0.05
Golar LNG Ltd.	–0.05

Guangzhou Automobile Group Company Limited detracted from performance due to the COVID-19 pandemic's negative impact on auto sales and industry profitability in China. Although Guangzhou remains one of the top automakers in China with a strong brand portfolio, we believe increasing competition and a potentially long recovery path will continue to weigh on the stock sentiment. We decided to exit the position.

Haitong Securities Co., Ltd. is a securities firm in China primarily focused on brokerage, asset management, and investment banking. Shares declined due to a weaker outlook for brokerage and investment income as suggested by interim operating figures. The announced removal of Haitong from the Hang Seng China Enterprises Index also weighed on shares. We exited our position, as the benefits of China's capital markets reform are taking longer than we anticipated, and company earnings remain tied to market volatility and cyclical factors.

Infraestructura Energetica Nova S.A.B. de C.V. is a Mexico-based energy infrastructure firm. It owns natural gas pipelines, an LNG storage and regasification terminal, a gas distribution utility, an electricity generation plant, and renewable energy assets. Shares came under pressure after a regulatory decision to significantly curtail the use and development of renewable electricity generation. We decided to exit our investment due to regulatory uncertainty, which in our view negatively impacts broader business development for both utilities and LNG exports in Mexico.

China Conch Venture Holdings Ltd. is an emerging leader in hazardous/solid waste treatment through its cement co-processing and waste-to-energy projects in China. Shares fell due to weakness in cement prices and a decline in the value of its stake in Anhui Conch Cement. We retain conviction. We think these issues are transitory and related to record heavy rains impacting construction activity in China. We expect the core business, cement co-processing, to grow at a over 20% CAGR and triple in value by 2025, becoming bigger than the company's stake in Anhui Conch.

Golar LNG Ltd. is engaged in transportation and regasification of liquefied natural gas. Golar also operates floating liquefaction unit Hilli (FLNG). Shares fell due to continued weakness in the shipping market. We retain conviction.

Golar has announced plans to spin off its shipping business, and we expect Golar to convert more vessels into FLNG units at attractive returns. We believe Golar is trading below its asset value and can create significant equity value going forward.

Portfolio Structure

Table IV.
Top 10 holdings as of June 30, 2020

	Percent of Net Assets
Alibaba Group Holding Limited	5.8%
Tencent Holdings Limited	5.0
Samsung Electronics Co., Ltd.	3.4
Taiwan Semiconductor Manufacturing Company Ltd.	3.0
Reliance Industries Limited	2.7
Zai Lab Limited	2.4
GDS Holdings Limited	1.7
Techtronic Industries Co. Ltd.	1.6
PagSeguro Digital Ltd.	1.6
China Conch Venture Holdings Ltd.	1.6

Exposure by Country

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

	Percent of Net Assets
China	43.4%
India	20.0
Brazil	7.9
Taiwan	4.6
Korea	4.6
Russia	3.5
Mexico	3.2
Hong Kong	2.0
Philippines	1.5
South Africa	1.3
Japan	1.0
Indonesia	0.9
Thailand	0.7
United Arab Emirates	0.6
Argentina	0.4
Norway	0.4
Hungary	0.2

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 second quarter of 2020, the Strategy's median market cap was $12.0 billion, and we were invested 46.3% in giant-cap companies, 40.7% in large-cap companies, 7.0% in mid-cap companies, and 2.0% in small- and micro-cap companies as defined by Morningstar, with the remainder in cash and private securities.

Recent Activity

During a quarter of continued market volatility, we added several new ideas toward existing themes while also increasing portfolio concentration in favor of our highest-conviction investments. Given the economic uncertainty related to COVID-19, we opportunistically exited positions whose earnings potential we deemed impaired for an unquantifiable time owing to disruption in global travel and other related services. We continue our endeavor to modestly reduce the number of positions in the portfolio.

As part of our China value-added theme, we initiated positions in **ZTO Express (Cayman) Inc.**, **S. F. Holding Co., Ltd.**, **Venustech Group Inc.**, and **Beijing Oriental Yuhong Waterproof Technology Co., Ltd.** These companies add to our exposure to China software/e-commerce-related investments and broadly to businesses that are innovating and transforming into local champions. ZTO is the largest express delivery company in China (by parcel volume) and is part of the Alibaba Cainiao logistics ecosystem. In our opinion, secular growth in e-commerce and new retail formats will support robust parcel demand over the next decade. ZTO's superior scale, automation, and routing efficiency will also lead to market share gains in a fragmented industry and deliver 20% to 30% earnings growth over the next three years. S. F. Holding is the leading white glove, next-day business express delivery company in China. We believe structural growth in the Chinese services industry will underpin sustained demand for high-quality, time-sensitive parcel delivery services. S. F. Holding's new e-commerce segment, leveraging its best-in-class service, brand, and operating efficiency will drive 20% incremental earnings growth annually in the next three years. Venustech is a leading software services provider focusing on cybersecurity in China. In our opinion, China is in the early stage of a decade-long growth trend in Software-as-a-Service, currently only 10% of the equivalent market penetration versus the U.S. Specifically, cybersecurity is a focus area in China's initiative to localize and be self-sufficient in software development. We believe Venustech, a market leader in providing intrusion detection, firewall, and real-time monitoring solutions, will benefit from favorable government policies and upgrade requirements under the MLPS 2.0 standard and achieve 20% to 30% annual growth over the next five years. Beijing Oriental Yuhong is China's leading producer of waterproofing and other advanced building materials, catering to the real estate and infrastructure sectors. The company has been rapidly gaining market share in a fragmented industry and is now bigger than the next 10 competitors combined. We expect structural growth in the waterproofing industry to accelerate as China pushes for higher-quality standards and increased regulations for building and construction-related activities. Beijing Oriental Yuhong, the industry pioneer, has by far the best product quality, track record, and pricing power among competitors. We believe the company is well positioned to sustain 30% earnings growth and double its market share to 20% in three to four years.

We also initiated a position during the quarter in **Hong Kong Exchanges and Clearing Limited** ("HKEX"), which operates the only stock exchange, futures exchange, and related clearinghouses in Hong Kong. In our view, and largely due to rising geopolitical tension between the U.S. and China, HKEX will gain relative attractiveness versus U.S. peers as a primary listing destination for major Chinese ADRs and primary offerings. U.S.-listed China ADRs currently account for a significant percentage of daily trading value on U.S. exchanges, and the migration of such liquidity to HKEX would drive a material enhancement to its earnings power. We see this trend likely accelerating given the recent passing of the Holding Foreign Companies Accountable Act in the U.S., which places new requirements on foreign ADRs and is directed at China. In addition, new product opportunities such as the listing of MSCI Index futures and potential inclusion of A-share derivatives will drive higher volumes and revenue growth at HKEX, beyond base case market expectations.

Related to our India consumer finance theme, we initiated a position in **Muthoot Finance Ltd.**, which is the largest gold-based non-bank financial company in India. Muthoot primarily serves under-banked borrowers in semi-urban/rural areas, which resonates with our keen interest to invest in businesses that support financial inclusion. The company is witnessing a surge in demand for gold loans owing to increased risk aversion by banks and other lenders in the aftermath of the IL&FS credit crisis and more recently due to COVID-19-related disruption/liquidity squeeze. We believe Muthoot is well positioned to generate 20% to 25% earnings growth over the next several years and will also benefit from rising gold prices that will support higher loan growth and operating leverage and lower credit costs.

We also established a position in **Localiza Rent a Car S.A.**, which is the largest car and fleet rental operator in Brazil. The company has pioneered an integrated business model from car purchase, to car and fleet rental, to used car sales. Localiza enjoys competitive advantages in buying and selling vehicles, while retaining the highest residual value. The company has been a key beneficiary of ongoing industry consolidation and should continue to gain market share due to its scale and cost structure. After a COVID-19-related disruption, we believe demand for car rentals and ride sharing will recover faster than other forms of transportation such as buses, rail, and air travel. We also expect further traction in fleet outsourcing among Brazilian corporates driven by a growing preference among younger employees to use rental and rideshare alternatives versus public transportation.

During the quarter, we opportunistically exited several positions, most notably **Azul S.A.** and **Copa Holdings, S.A.** We believe the COVID-19-related impact to global airlines and travel-related companies has impaired their earnings trajectories indefinitely, and we do not have visibility into traffic and revenue normalization trends. In our endeavor to increase the weightings of holdings in which we have highest conviction in quality and return potential while simultaneously eliminating lower conviction or smaller holdings over time, we also exited positions in **Cogna Educacao SA**, **Guangzhou Automobile Group Company Limited**, **Haitong Securities Co., Ltd.**, **Lenovo Group Limited**, and **Sinopharm Group Co. Ltd.**

Outlook

In our first quarter letter, we suggested that as COVID-related liquidity strains were likely abating, equities should, at a minimum, stabilize, and that as COVID cases peaked, testing capacity increased, and focus shifted to potential therapies, vaccines, and economic reopening, the policy stimulus in the pipeline would likely shift from defense to offense. We suggested at the time that the lack of confidence in the ability of EM countries to manage the COVID crisis likely led to a market mispricing, and speculated that investors were overlooking several positives such as younger populations and a history of balancing health, mortality, and economic risks, while noting that China, an EM barometer, was one of the best-placed countries to return to economic normalcy. While much of the above came to pass and EM equities recovered strongly, the second quarter remained volatile and bifurcated during much of the period.

During the peak of the global market crisis in March, global equity correlations neared 1.0, with most equities rapidly moving towards distressed levels given uncertainties regarding employment, consumer spending, corporate and personal bankruptcies, real estate occupancy, and bank solvency. However, as the U.S. Federal Reserve ("Fed"), Congress, and a chorus of global policymakers moved in unison to construct a fiscal and liquidity bridge to economic reopening, a hierarchy of performance in the recovery began to take hold. As policymakers effectively underwrote the largest insurance policy we have ever seen, capital began to flee towards the explicitly underwritten assets. This included various credit markets and assets targeted directly by the Fed, which had effectively countered the forced deleveraging and asset deflation that was well underway in mid-March. Countries with room for fiscal expansion, or with current account and FX reserve surpluses, and industries or companies with strong credit quality, were also early beneficiaries. By mid-April, it was becoming clear to us that investors were discerning between certain industries and companies as perceived beneficiaries of COVID-disruption such as those associated with *e-commerce/logistics, remote access/working from home, digitization beneficiaries (internet data centers, online education, and cloud software providers), essential consumption, home improvement, health care/pharmaceuticals/diagnostics*; COVID-survivors (industries and companies that were adversely impacted but likely to remain going concerns); and a third group was considered COVID-impaired, which maintained an extraordinarily high risk premium given liquidity and solvency risks such as businesses associated with *airline/travel, physical real estate, retail/restaurants, and banks*. Like most equity managers, our portfolio had exposure to each category, and our strategy was to hold our COVID-impaired investments given what we viewed as steep and overly-punitive discounts, with a goal of exiting should they return to our assessment of fair value or higher on enthusiasm over reopening or vaccine/therapy developments (the viability of which currently remain unpredictable, in our view). During the quarter, we assessed opportunities to add to COVID-impacted investments, given our view that they would eventually return to normal conditions with earnings power intact, and analyzed COVID-beneficiaries on a case-by-case basis, to determine whether we perceived the benefit as being long-term, permanent, or transitory. Similarly, markets also assigned a hierarchy of performance by country, depending on perceived ability to manage the health care, economic, and liquidity crises, with certain EM countries at the short end of the stick. In our communications during the quarter, we suggested that selling COVID-impacted or COVID-impaired EM equities, particularly those with long-term appeal, such as those domiciled in India or Brazil, would turn out to be poor decisions. Given that capital markets and currencies had *already been repriced*, capital chasing assets carrying the greatest insurance premium had created an attractive arbitrage opportunity for investing in the perceived riskier securities and businesses. To us, either the insurance policy would perform, providing a bridge to vaccinations/therapies and economic normalization, in which case buying/holding more steeply discounted COVID-impacted companies, countries, and currencies would lead to very attractive returns, or the insurance policy would fail as fiscal resources became exhausted, and the underwritten assets would likely have more downside in such a scenario than those already trading at discounted or distressed levels.

As the second quarter progressed global economies increasingly pursued reopening, businesses and world health agencies announced progress towards various potential vaccines, and the lagging COVID-impacted and impaired equities and currencies began to outperform. Capital finally began to migrate from the consensus underwritten and beneficiary assets. This drove high volatility and significant mean reversion in performance within the capital markets. Strong performance by our COVID beneficiaries throughout the quarter, combined with the subsequent significant recovery across the rest of our portfolio, led to a strong quarter of performance for our strategy, while also allowing us to opportunistically upgrade the quality of our holdings as appropriate in a post-COVID environment.

Looking forward, we cannot predict the duration of COVID-related impact on economic activity. However, we believe we have taken advantage of recent market events to further concentrate our portfolio in attractive long-term themes and companies that are well positioned to prosper from significant catalysts, reforms, and trends that we believe will remain in place for many years. Examples include mobile e-commerce, artificial intelligence, digitization and cloud migration, fintech disruption, China's shift in emphasis to value-added economic activity, wealth management and consumer finance in India, and attractive productivity-enhancing reforms in Brazil and India, to name a few. We believe the evolving and complex relationship between the U.S. and China represents a tectonic shift in geopolitics that is creating significant long-term investment opportunities across many of the markets in which we invest. The scaling back of globalization and the localization of supply chains, technology standards, and capabilities are not reasons to avoid investing in China and the emerging markets; rather they are catalysts for potentially enormous value creation. Our research team has been focused on these evolving themes and we have already made several related investments. Finally, we remain optimistic that the COVID crisis will prove to be the event that pushes the world's policymakers through the portal of Modern Monetary Theory, or fiscal expansion funded by printing money and central banks expanding their balance sheets. This populist QE should prove to be a very different type of stimulus, one that we believe will likely provoke a dollar bear market, which typically would suggest an extended period of EM equity outperformance.

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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