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Impact of Evergrande on China's Economy

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The economic situation in China continues to evolve. The most recent concerns that the Evergrande restructuring may trigger contagion to related sectors and markets raises the likelihood that local policymakers and officials will soon begin to act to contain such contagion and calm markets. However, it is also true that President Xi believes longer-term stability requires more market discipline with tighter regulatory guidelines and less government bailout. Thus, the playbook for this credit stress could prove less predictable, with more volatility, or a “lower v”, in the v-shaped bottom that we anticipate.

We cannot predict when this will come or how forceful the initial messaging will be, but we are confident authorities have the wherewithal to restore order and confidence to markets. We further believe that Chinese equities have been in the process of discounting a credit and regulatory tightening for many months and view the related correction as well-advanced.

The high cost of property and home ownership is one of the 2 primary concerns of the middle class in China. Xi has laid out various reforms to contain property and land price appreciation in China, but this will represent a new direction and adjustment for a key economic sector, the related entrepreneurs, and most municipalities that historically have relied on land sales as a key component of fiscal revenue.

The most leveraged players, with Evergrande being the most levered, are feeling this adjustment now and we believe additional property developers are likely to incur some level of bond haircuts and equity loss. We believe the government's plan is to manage losses largely to the holders of speculative high-yield bonds and equity of the most leveraged players, while safeguarding at par the value of bank debt and liabilities while also supporting the market price/bids for underlying finished properties.

This will inflict discipline on those seen as engaged in too much speculation, leverage or growth, while maintaining stability for many developers with acceptable operating protocols, as well as the financial sectors. There will be some investment pools holding the high-yield bonds of Evergrande or others that will suffer mark to market losses, but the large majority of this will be borne by the relatively wealthy holders of “wealth management products”, where the government has been warning for years that such products do not offer guaranteed returns. Losses here will also reduce moral hazard – an objective of the Party on the road to greater social, economic, and financial stability.

Baron Emerging Markets Fund

Baron Emerging Markets Fund has never owned Evergrande or any other China property/real estate developer. We have always viewed this sector as too leveraged, political, and cyclical. While we have zero exposure to the China real estate sector, we do hold a 0.9% position in a building materials manufacturer, the largest and highest quality advanced waterproofing technology company in China, Beijing Oriental Yuhong Waterproof Technology Co., Ltd, whose stock price has corrected in the past couple weeks in sympathy with Evergrande.

Oriental Yuhong cut off supplies to Evergrande and has no accounts receivables exposure to Evergrande. Oriental Yuhong has also been diversifying its revenue base and non-property development represents roughly 50% of revenue and is likely to benefit as policymakers will introduce infrastructure stimulus measures to counteract a private sector property slowdown.

Baron Emerging Markets Funds has zero exposure to Chinese banks or insurers. We generally believe Chinese banks lack market discipline and transparency and are at risk of “state service”. We sold our position in Ping An, the leading domestic private sector insurance underwriter, earlier this year because of an acquisition they made that we believed may have been encouraged by the State and not based on attractive financial returns. That decision indeed proved prescient.

Investors should consider the investment objectives, risks, and charges and expenses of the investment carefully before investing. The prospectus and summary prospectuses contain this and other information about the Funds. You may obtain them from the Funds’ distributor, Baron Capital, Inc., by calling 1-800-99BARON or visiting www.BaronFunds.com. Please read them carefully before investing.

Risks: 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 Fund 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.

BARON EMERGING MARKETS FUND

TOP 10 HOLDINGS 9/21/2021

Holding	% of Net Assets
Taiwan Semiconductor Manufacturing Company Ltd.	3.8%
Bajaj Finance Limited	3.2%
Samsung Electronics Co., Ltd.	3.0%
Tencent Holdings Limited	2.9%
Alibaba Group Holding Limited	2.7%
Reliance Industries Limited	2.3%
Novatek PJSC	2.0%
Sberbank of Russia PJSC	2.0%
Korea Shipbuilding & Offshore Engineering Co., Ltd.	1.7%
Max Financial Services Limited	1.7%
	<hr/> 25.2%

As-of 9/21/2021, 0.9% of the Fund’s assets were invested in Beijing Oriental Yuhong Waterproof Technology Co., Ltd.

Portfolio holdings are subject to change. Current and future portfolio holdings are subject to risk.

The discussion of market trends is not intended as advice to any person regarding the advisability of investing in any particular security. The views expressed in this document reflect those of the respective writer. Some of our comments are based on management expectations and are considered “forward- looking statements.” Actual future results, however, may prove to be different from our expectations. Our views are a reflection of our best judgment at the time 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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