Baron Mid Cap Growth Strategy

BARON CAPITAL

March 31, 2024

Dear Investor:

Performance

U.S. equities continued their strong run to begin the year, with major market indexes achieving new all-time highs during the first quarter. The rally was supported by robust economic data and relatively strong corporate earnings, which fueled investor hopes for a *soft landing*. Investors appeared unfazed by concerns about persistent inflation, the uncertain timing of Federal Reserve (Fed) interest rate cuts, record consumer and government debt, and potential government shutdowns.

Most sectors closed higher in the period, led by Communication Services, which was bolstered by double-digit gains from Meta and Netflix. Cyclical sectors, such as Energy, Information Technology (IT), Financials, and Industrials, were also among the leaders thanks to strong gains from integrated oil & gas, semiconductor, property & casualty insurance, and machinery stocks, respectively. Real Estate was the only sector to decline in the period, as REITs were pressured by the prospect of interest rates staying higher for longer. Defensive sectors, including Health Care, Utilities, and Consumer Staples, underperformed amid the ongoing *risk-on* market environment. Small and mid-cap stocks benefited from improving market breadth in March but still trailed large caps for the quarter. Growth stocks dominated their value counterparts in January and February to begin the year on the front foot.

Table I.
Performance for annualized periods ended March 31, 2024 (Figures in USD)[1]

	Baron Mid Cap Growth Strategy (net)[2]	Baron Mid Cap Growth Strategy (gross)[2]	Russell Midcap Growth Index[2]	S&P 500 Index[2]
Three Months[3]	6.04%	6.30%	9.50%	10.56%
One Year	18.11%	19.27%	26.28%	29.88%
Three Years	2.11%	3.10%	4.62%	11.49%
Five Years	10.05%	11.12%	11.82%	15.05%
Ten Years	11.12%	12.22%	11.35%	12.96%
Fifteen Years	15.01%	16.15%	15.64%	15.63%
Since Inception (June 30, 1998)[4]	8.86%	9.94%	8.83%	8.12%

Table II.
Calendar Year Performance 2019-2023 (Figures in USD)

	Baron Mid Cap Growth Strategy (net)[2]	Baron Mid Cap Growth Strategy (gross)[2]	Russell Midcap Growth Index[2]	S&P 500 Index[2]
2019	38.08%	39.43%	35.47%	31.49%
2020	33.59%	34.88%	35.59%	18.40%
2021	14.26%	15.37%	12.73%	28.71%
2022	(25.90)%	(25.18)%	(26.72)%	(18.11)%
2023	17.41%	18.56%	25.87%	26.29%

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 March 31, 2024, total Firm assets under management are approximately $43.0 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 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 Report please contact us at 1-800-99-BARON. GIPS® is a registered trademark owned by CFA Institute. CFA Institute does not endorse, promote or warrant the accuracy or quality of the report.

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 With the exception of performance data, most of the data is based on a representative account. Such data may vary for each client in the Strategy due to asset size, market conditions, client guidelines, and diversity 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 The **Russell Midcap® Growth Index** is an unmanaged index that measures the performance of small to medium-sized companies that are classified as growth and the **S&P 500 Index** measures the performance of 500 widely held large-cap U.S. companies. All rights in the FTSE Russell Index (the "Index") vest in the relevant LSE Group company which owns the Index. Russell® is a trademark of the relevant LSE Group company and is used by any other LSE Group company under license. Neither LSE Group nor its licensors accept any liability for any errors or omissions in the indexes or data and no party may rely on any indexes or data contained in this communication. The Strategy includes reinvestment of dividends, net of foreign withholding taxes, while the **Russell Midcap® Growth Index** and the **S&P 500 Index** includes reinvestment of dividends before taxes. Reinvestment of dividends positively impacts performance results. The indexes are unmanaged. Index performance is not Strategy performance. Investors cannot invest directly in an index.

3 Not annualized.

4 The Strategy has a different inception date than its representative account, which is 6/12/1987

Table III.
Top contributors to performance for the quarter ended March 31, 2024

	Percent Impact
Arch Capital Group Ltd.	0.88%
Gartner, Inc.	0.57
CoStar Group, Inc.	0.45
Mettler-Toledo International Inc.	0.41
Veeva Systems Inc.	0.34

The *risk-on* market environment resulted in a continuation of many of last year's trends. Bitcoin reached new highs, as did a narrow group of perceived AI winners. The types of stocks that performed best included higher beta, cyclical, and lower quality companies. The momentum factor also maintained an outsized impact on stocks. The Health Care sector, which is Baron Mid Cap Growth Strategy's (the Strategy) second largest weighting, continued to lag in this environment. As the economy stabilizes and interest rates inevitably come down, we expect the types of companies that the Strategy favors to outperform – leading companies that benefit from secular growth drivers, secure competitive positions, and talented management teams.

The Strategy appreciated 6.04% in the first quarter, trailing the Russell Midcap Growth Index by 3.46% due to stock selection and headwinds from the Strategy's longtime style biases. The Strategy was hurt most by its underexposure to securities with robust short-term momentum and elevated idiosyncratic volatility, which were strong performers in the period.

Investments in Industrials, Financials, Health Care, and IT were largely responsible for the relative shortfall in the period. Within Industrials, data and analytics vendor **Verisk Analytics, Inc.** reported solid quarterly earnings. Still, we believe the stock lagged as part of a broader market rotation away from steady-growing, compounding stocks. We maintain conviction in its competitive positioning, long-term growth, margin expansion, and capital deployment prospects for the business. Human capital management (HCM) software leader **Dayforce, Inc.** fell on concerns that slowing employment growth will reduce the company's growth rate in the near term. Although Dayforce has some direct exposure to employment levels, it also benefits from powerful secular trends around the modernization of HCM software and the growing adoption of SaaS.

FactSet Research Systems Inc., a leading investment management tool provider, hindered Financials performance. The company revised its fiscal year 2024 growth in annual subscription value downward, given ongoing challenges in its financial services end-market. While there is some near-term uncertainty, we maintain long-term conviction in the company's large addressable market, consistent execution on both new product development and financial results, and robust free cash flow generation.

Modest declines in veterinary diagnostics leader **IDEXX Laboratories, Inc**. and life sciences tools developer **Bio-Techne Corporation** challenged Health Care. IDEXX's shares fell as foot traffic to veterinary clinics in the U.S. remained uneven, modestly hampering aggregate revenue growth. IDEXX's competitive trends are outstanding, and we expect new proprietary innovations and field sales force expansion to meaningfully contribute to growth this year. Bio-Techne was hurt by a slowdown in its business in China and ongoing biotechnology funding constraints.

Weakness in IT was led by a disappointing performance from internet infrastructure company **VeriSign, Inc.** and physics-based simulation software leader **ANSYS, Inc**., whose shares pulled back for reasons noted below. Syndicated research provider **Gartner, Inc.** also underperformed in the period, relinquishing a portion of last year's strong relative gains. The company's core subscription research businesses continued to compound at attractive rates, and we believe that growth is poised to accelerate over the next several quarters. We think Gartner will emerge as a key decision support resource for every company evaluating the opportunities and risks of AI on its business, providing a tailwind to volume growth and pricing realization.

Somewhat offsetting the above was a solid stock selection in Communication Services, where internet advertising demand-side platform **The Trade Desk** delivered a solid quarter after experiencing some softness related to macroeconomic uncertainty in late 2023. This year appears promising for Trade Desk as the company continues to benefit from tailwinds stemming from the secular growth of Connected TV. Given its technology, scale, and estimated 10% share in the $100 billion programmatic advertising market, a small and growing subset of the $700 billion global advertising market, we remain positive about the company.

Specialty insurer **Arch Capital Group Ltd.** contributed to performance after reporting strong financial results that exceeded Wall Street expectations. In the most recent reported quarter, operating ROE was 24% and book value per share rose 44% as underwriting profitability remained excellent. Pricing trends in the property and casualty insurance market are favorable, and elevated interest rates are driving higher investment income. Insurance stocks broadly rebounded from weakness in the prior quarter as interest rates stabilized. We believe Arch's exceptional management team will continue to grow earnings and book value at attractive rates.

Shares of **Gartner, Inc**., the leading provider of syndicated research to the IT sector, contributed to performance. Fourth quarter financial results were mixed, with declines in net income and EPS. However, solid increases in contract value and strong full-year performance, including a 9% increase in net income and an 11% rise in diluted EPS, helped boost the company's share price. In addition, a 19% increase in free cash flow for the quarter and 6% for the full year underscored Gartner's operational efficiency. Gartner's core subscription research businesses compounded at attractive rates, and we believe growth is poised to accelerate. We think Gartner will emerge as a key decision support resource for every company evaluating the opportunities and risks of AI on its business, providing a tailwind to volume growth and pricing realization. We expect Gartner's sustained revenue growth and focus on cost control to drive continued margin expansion and enhanced free-cash-flow generation. The company's balance sheet is in excellent shape and can support aggressive repurchases and bolt-on acquisitions, in our view.

Shares of real estate marketing and data analytics provider **CoStar Group, Inc.** contributed to performance after posting strong quarterly and year-end results, including 2023 revenue of $2.46 billion, a 13% year-over-year increase, and above-consensus estimates. It was CoStar's 13th consecutive year of double-digit revenue growth. We remain enthusiastic about CoStar's growing traction in the residential home market. CoStar began to monetize its new Homes.com platform in February 2024, and it is targeting close to $100 million in run-rate revenue by year end. We believe momentum can be amplified by the recent class action settlement with the National Association of Realtors, which has the potential to disrupt the residential brokerage industry and enhance the return on investment for brokers advertising on Homes.com. CoStar plans to invest almost $1 billion in its residential business in 2024, which, while a significant upfront commitment, represents the peak level of annual spending, in our view. We think success in the residential segment has the potential to double the size of CoStar's overall revenue stream.

Table III.
Top detractors from performance for the quarter ended March 31, 2024

	Percent Impact
Bio-Techne Corporation	–0.24%
ANSYS, Inc.	–0.22
VeriSign, Inc.	–0.17
FactSet Research Systems Inc.	–0.17
IDEXX Laboratories, Inc.	–0.16

Bio-Techne Corporation is a leading developer and manufacturer of reagents, instruments, and services for the life sciences research, diagnostics, and bioprocessing markets. The stock detracted from performance after the company reported weak fourth-quarter financial results, including a 2% decline in organic growth, driven by a slowdown in China and ongoing funding constraints for biotechnology customers. While management noted that business in China has stabilized and the funding environment has started to recover, it did not forecast marked improvement until later in 2024. We believe these headwinds are cyclical, and we are encouraged by some signs of stabilization in the company's business. We continue to believe Bio-Techne is well positioned for long-term growth.

ANSYS, Inc. is a leading provider of physics-based simulation software. By accurately mimicking real world physics with software, simulation tools help customers reduce costs and accelerate their time to market. In December 2023, shares rose on news that several entities were interested in acquiring the company. In January 2024, Synopsys officially announced its intent to acquire ANSYS in a deal valued at nearly $35 billion, marking one of the largest software acquisitions in history. While the stock price remained above levels seen before the acquisition reports, the official announcement spurred a somewhat unfavorable market reaction given an implied price per share slightly below market expectations, a relatively long period between the announcement and anticipated closing date, heightened risk perception stemming from a substantial portion of the deal's value being proposed to ANSYS shareholders in the form of Synopsys shares, and perceived regulatory hurdles. We believe ANSYS is well positioned to benefit from multi-year contracts, its strategic relationships with its large and diversified customer base, and secular trends such as growing product complexity and the adoption of simulation technology.

VeriSign, Inc., a global provider of internet infrastructure and domain name registry services, manages the .com and .net domains. Shares of VeriSign declined because of continued weakness in new domain registrations, stemming largely from weaker demand in China. We believe that VeriSign maintains an exceptional competitive position and the contractual ability to raise prices. Longer term, we are encouraged by VeriSign's opportunity to win the rights to administer the ".web" domain, produce substantial free cash flow, and generate attractive capital returns as it continues to prioritize share buybacks.

Portfolio Structure

As of March 31, 2024, the Strategy held 53 positions. The Strategy's 10 largest holdings represented 47.2% of net assets, and the 20 largest represented 70.1% of net assets. The Strategy's largest weighting was in the IT sector at 28.6% of net assets. This sector includes software companies, IT consulting firms, technology distributors, and internet services companies. The Strategy held 22.9% of its net assets in the Health Care sector, which includes investments in life sciences companies and health care equipment, technology, and supplies companies. The Strategy held 17.2% of its net assets in the Industrials sector, which includes investments in research and consulting companies, aerospace & defense companies, and human resource and employment services companies. The Strategy also had significant weightings in Financials at 13.7% of net assets and Consumer Discretionary at 7.8% of net assets.

As the table below shows, the Strategy's largest investments all have been owned for significant periods – we have owned 8 of the 10 largest holdings for over a decade. This is consistent with our approach of investing for the long term in companies benefitting from secular growth trends with significant competitive advantages and best-in-class management teams.

Table IV.
Top 10 holdings as of March 31, 2024

	Year Acquired	Market Cap When Acquired (billions)	Quarter End Market Cap (billions)	Quarter End Investment Value (millions)	Percent of Net Assets
Gartner, Inc.	2007	$ 2.9	$37.2	$445.4	9.8%
IDEXX Laboratories, Inc.	2006	2.5	44.9	296.2	6.5
CoStar Group, Inc.	2016	5.0	39.5	217.2	4.8
Mettler-Toledo International Inc.	2008	2.4	28.5	209.2	4.6
Verisk Analytics, Inc.	2009	4.0	33.8	205.4	4.5
Arch Capital Group Ltd.	2003	0.9	34.6	187.8	4.1
FactSet Research Systems Inc.	2006	2.5	17.3	155.7	3.4
Guidewire Software, Inc.	2013	2.8	9.7	153.0	3.3
Fair Isaac Corporation	2020	12.1	31.1	151.2	3.3
Roper Technologies, Inc.	2011	7.4	60.0	133.6	2.9

Recent Activity

Table V.
Top net purchases for the quarter ended March 31, 2024

	Quarter End Market Cap (billions)	Net Amount Purchased (millions)
Procore Technologies, Inc.	$11.9	$27.0
Spotify Technology S.A.	52.3	23.1
Hilton Worldwide Holdings Inc.	53.8	6.5

We initiated an investment in **Procore Technologies, Inc.** Founded in 2002, Procore provides cloud-based construction management software that helps general contractors, subcontractors, and asset owners manage every step of the construction process. Procore's product suite includes project execution (storing and updating blueprints, designs, work orders, and project schedules in a single system of record), pre-construction (managing bids, permitting, and approvals), workforce management (scheduling worker hours and recording safety compliance), financial management (budgeting and invoicing), and data analytics. Together, these products help contractors execute projects more efficiently, plan more accurately, avoid costly rework, improve worker safety, and generate better margins. This has led to very low customer churn.

Procore serves a large and growing addressable market – annual construction volume exceeds $2 trillion in the U.S. alone – that is still in the early stages of digitization and technology adoption. The company has a leading market share in the sector, with more than 16,000 construction firms and asset owners using its software to manage billions of dollars of annual project volume. Yet, Procore has penetrated just 12% of U.S. construction volume and 2% of international volume. We believe the company has several competitive advantages that will drive further share gains and revenue growth. First, Procore is the only cloud-native technology vendor that addresses all stages of the project life cycle with a single, integrated interface and data model. Second, Procore was the first vendor to price its platform using a *take-rate* model, charging a percentage fee against its customers' total construction volume. Compared to seat-based license models offered by many competitors, this approach has encouraged far more industry practitioners to trial and use Procore products. As of last year, more than 500,000 collaborator companies were interacting with its product, driving a strong pipeline for new customer wins.

We see a long runway for growth through new customer additions and expanded usage within existing accounts. Recent product innovations like Procore Pay (managing payments for the various vendors and subcontractors on a given project) and geospatial mapping (for larger civil engineering projects) should improve the company's prospects. Procore's cash flow is positive today, and its margins have been increasing meaningfully during the past two years. We think the business can continue to grow at a healthy rate while further expanding free cash flow margins in excess of 20%, as it benefits from greater market share, higher take rates, and operating leverage. We believe this should result in good earnings growth and bodes well for the stock long term.

Another new addition was **Spotify Technology S.A.**, a leading global digital music service, offering on-demand audio streaming through paid premium subscriptions and an ad-supported free option. Spotify was among the originators of paid streaming music after the downloads/Napster era, with the Spotify app launching broadly in the early 2010s. Since then, streaming music has grown at a 20%-plus CAGR, and Spotify has been the leading streaming music service both in the U.S. and globally, with more than 600 million monthly average users. We believe that Spotify offers a compelling user experience, which includes algorithmic recommendations and podcasts.

While we have monitored Spotify for some time because of its product leadership and large market opportunity, we believe the last few months have signaled a meaningful positive inflection point for the company. First, Spotify has continued to show that its market is far from penetrated – subscriber net adds accelerated in 2023, even as the product has been widely available for years, thanks to targeted marketing in various countries and new product features. Next, Spotify's gross margin profile continues to improve thanks to the impact of its artist promotions marketplace, growth in its advertising business, and improved profitability in its podcast offerings.

In addition, management has recently become much more focused on operating discipline, with 2024 expected to be Spotify's first meaningfully profitable year after operating losses in 2021 and 2022. This has entailed material staff layoffs, restructuring the podcast division, and hiring a new operationally focused CFO. Furthermore, Spotify increased its pricing structure while seeing minimal customer loss, demonstrating the pricing power of its product and the broader streaming music industry. Finally, Spotify has continued to innovate its product roadmap, introducing audiobooks and features like AI DJ that differentiate it from other music streaming providers. We believe that Spotify has the potential to reach more than one billion monthly active users as its global market share increases and music listening habits mature internationally, and we expect its profitability to continue to improve.

Table VI.
Top net sales for the quarter ended March 31, 2024

	Net Amount Sold (millions)
ANSYS, Inc.	$68.2
Gartner, Inc.	41.1
IDEXX Laboratories, Inc.	36.6
VeriSign, Inc.	35.1
Mettler-Toledo International Inc.	20.3

We made some profits from **ANSYS, Inc.** after the announcement that it would be acquired by Synopsys, a software company focused on electronic design automation. We also took some profits and managed the position size of long-term holdings **Gartner, Inc.**, **IDEXX Laboratories, Inc.**, and **Mettler-Toledo International, Inc.** We reduced our position in **VeriSign, Inc.** as its growth in new internet domains has slowed.

Outlook

The market has been roiled by the largely unanticipated increase in interest rates throughout 2024. Inflation has proved more stubborn than most expected, and the Fed has continued to delay interest rate decreases. As a result, a higher discount rate is being applied to the future earnings streams of all companies. We believe this phenomenon has had an outsized impact on many of the businesses we favor – companies that benefit from long-term secular growth drivers with highly visible and growing earnings streams. Although we don't have particular insight into the timing of the Fed's actions, we believe it is inevitable that it will eventually cut rates, and we believe our investments should benefit.

In addition, the market has been especially focused on a relatively narrow group of companies that are perceived to be the beneficiaries of breakthroughs in AI. We believe that many of our holdings are well positioned to utilize AI to expand their product offerings and competitive differentiation, increase their growth rate, and, in some cases, reduce their cost structure. We expect the market to eventually appreciate these opportunities and see them reflected in these businesses' valuations.

It is also worth noting that the Benchmark has dramatically underperformed the Russell 1000 Growth Index, a key benchmark for large-cap growth stocks, during the past five years – by 6.70% annualized over this period. This has reduced the relative valuation for mid-cap growth stocks, as they usually trade at a premium to large-cap growth stocks, but that is not the case presently. We believe it presents an attractive opportunity to invest in this area.

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.

Risks: Past performance is not a guide to future performance. The value of investments and income from them may go down as well as up. Your capital is at risk. Specific risks associated with investing in smaller companies include that the securities may be thinly traded and more difficult to sell during market downturns. Even though the Strategy is diversified, it may establish significant positions where the Adviser has the greatest conviction. This could increase volatility of the Strategy's returns. 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.