Keeping an Eye on Long Term Fundamentals During a Market Crisis

This is an edited version of a June 4, 2020 Q&A with Ron Baron, Michael Baron, and David Baron. Ron is CEO of Baron Capital and portfolio manager of Baron Partners Fund and Baron Focused Growth Fund. Michael is co-portfolio manager of Baron Partners Fund and David is co-portfolio manager of Baron Focused Growth Fund.

To access the full recording, please dial 866-595-5357, passcode 5052296#.

Key Discussion Points

Overview

Baron Focused Growth Fund
Fund performance, management of the portfolio, current outlook for the market and the Fund

Baron Partners Fund
Fund performance, management of the portfolio, volatility, SpaceX, final thoughts

Overview

Ron Baron: Baron Partners Fund and Baron Focused Growth Fund are both outperforming their benchmarks year-to-date through May 31, 2020. Both funds are non-diversified, which means they invest in a relatively small number of companies.

Our process is relatively simple: invest for the long term in growth companies that are competitively advantaged with what we believe are great management teams. We also have relatively low turnover because we're allowing the companies we've discovered to grow. Even if they don't grow quite as fast as we hoped initially, we will still hold them as long as our investment thesis remains intact.

We like to buy companies early on when they are penalizing earnings by investing in their business to become much larger in the future. A number of our companies were already producing significant revenue prior to the pandemic. When the economy shut down, some of these businesses, particularly in travel and leisure, saw their revenue drop to zero basically overnight. We believe these companies, which were hurt the most in the pandemic, will help us the most as the economy recovers.

Baron Focused Growth Fund

How has the Fund performed during the crisis?

David Baron: Baron Focused Growth Fund has had strong performance year-to-date,[1] outperforming the Russell 2500 Growth Index by 963 basis points. However, how it got there has been quite volatile as the Fund was up almost 26% at the mid-February market peak and then declined 44% from peak to trough before recovering 52% from the trough to date.

Most of that volatility has been driven by outsized exposure to travel and leisure stocks, which comprised 37% of the portfolio as of the end of 2019, versus just 2% for the index. Despite recovering from their lows, these stocks have underperformed year-to-date. They're down about 18%, versus the index, which is down about 1.6% during the same period. However, we believe most of these stocks will outperform going forward, as we think the bad news is already priced in, and all of them have enough liquidity to survive the pandemic. These

[1] All year-to-date figures are through May 31, 2020 unless otherwise noted.

stocks currently comprise about 27% of the portfolio, and we think they will bring earnings back to 2019 levels over the next two to three years.

Names we think will rebound quickly include **Red Rock Resorts, Inc. (RRR)** and **Penn National Gaming, Inc. (PENN),** two regional gaming companies whose visitors typically drive rather than fly to their locations. In addition, we believe Penn Gaming's recent purchase of 36% of online sports betting company BarStool is a major opportunity for growth as more states legalize online gambling and sports betting as a source of funding to help fill large budget deficits. Penn has forecast that its online and sports betting segment could double EBITDA over the next five years.

Hotel franchiser **Choice Hotels International, Inc. (CHH)** is a low capital-intensive, fee-based business. It still throws off cash, even during downturns, and should also be among the first to recover given its lower-end leisure segments. **Vail Resorts, Inc. (MTN)** should also do well as it already has about half of its earnings locked in through season pass sales.

Tesla, Inc. (TSLA)'s stock has doubled year-to- date. The company continues to take share of the electric vehicle market. It has ramped production at its factory in Shanghai and has begun construction of a factory in Berlin. Lastly, **FactSet Research Systems, Inc. (FDS)**, a provider of financial data to the investment community, is up 15% year-to-date.

How have you been managing the portfolio during this period?

David Baron: We are taking the same proven long-term approach to investing that we've applied successfully over the last four decades. We invest in what we believe are high-quality companies with superior growth opportunities, significant competitive advantages, and great management. We regularly speak with all the companies in which we invest and review their business models and balance sheets to assess their long-term viability. We have low turnover, which has been a positive for the Fund, as we've been able to generate alpha of 694 basis points over the past three-year period as of March 31, 2020 with beta of just 88.

From a process perspective, we have spent these past few months talking to the CEOs and other members of the management teams of our companies to understand how they are dealing with the current situation. These discussions have been invaluable, especially given the sizable investments we have in these companies. We were able to confirm to ourselves that these companies have the means to survive and potentially emerge even stronger and we've added to some positions whose stock price had fallen sharply.

Ron Baron: As an example, Penn National Gaming's stock went from $38 in mid-February to below $10 when the pandemic forced it to shut its casinos. This is a business that ordinarily does $5 billion of annual revenues and makes $1.5 billion before it pays rent. In addition, it pays another $5 billion in state taxes. States are doing everything they can to reopen the casinos so they can recapture those taxes. Penn will also benefit from its BarStool partnership once sports teams are back off the sidelines. The stock's already back up to $33. We think it has plenty of room left to grow.

As another example, **Hyatt Hotels Corp. (H)** has had to close its hotels during the pandemic. Suddenly, it had zero revenue coming in on its owned assets although, of course, it still had overhead. The stock fell from $93 at the mid-February peak to $37 in less than a month. We added to our position at the low. The stock is now back to $60. We're not focused on what's happening right now; we're looking at what the business will earn when the economy recovers. Hyatt's hotels are normally quite profitable and we think its assets are tremendously underpriced. It's selling at half price now in our view, so we think there is the possibility that the stock will grow significantly over time. Would I rather take advantage of that possibility or have my money sit in the bank earning zero interest?

What is your current outlook for the economy, the markets, and the Fund?

David Baron: While there is obviously still considerable uncertainty regarding COVID-19 and its impact to the economy, we're confident in the prospects for the companies in the portfolio. I think our holdings will rebound as the pandemic subsides, testing ramps, and a vaccine is developed. In addition, the impact of massive fiscal stimulus should begin to kick in once the economy reopens. We believe valuations are attractive and already reflect the downsides from the disruption. Historically low interest rates should also help valuations and are a bullish sign for stock multiples. The Fund has had strong year-to-date performance, yet we still see significant upside in the years to come.

Baron Partners Fund

How has the Fund performed during the crisis?

Michael Baron: We have been quite pleased with Baron Partner Fund's performance, especially in such a volatile environment. Year-to-date, the Fund is up 6.34%, beating the Russell Midcap Growth Index by 457 basis points. In the second quarter to date, the Fund is up 34.1%, ahead of the benchmark by 177 basis points. Our long-term performance continues to be strong as well. On a one-, three-, five-, ten-year and since inception basis, we are ahead of the benchmark by over 260 basis points annualized for each period.

How are you managing the portfolio?

Michael Baron: We categorize the holdings in the Fund into four buckets: disruptive growth, core growth, financials, and real and irreplaceable assets. Much of the year-to-date performance has been driven by the disruptive and core growth categories.

Disruptive growth: The disruptive category, which accounts for around 48% of the portfolio, is up about 46% on a second quarter-to-date basis and up about 55% on a year-to-date basis. This category includes companies like Tesla, Inc., **Zillow Group, Inc. (ZG), Guidewire Software, Inc. (GWRE), Shopify Inc. (SHOP),** and **SpaceX,** which is a private company. All these companies are leaders in their category with compelling products or services. They are all benefiting from the digitization of the economy, a trend we believe will be accelerated by the current crisis. For example, Zillow is making it possible to research and even buy homes online. All of Tesla's sales are conducted online. Shopify ensures that brands are able to sell directly online to consumers without intermediaries such as Amazon.

Core growth: This category, which comprises around 34% of the portfolio, has also been a strong performer so far this year. Second quarter-to-date, this category is up around 19%, and year-to-date, it's up about 10%. The category includes companies like **Adyen N.V. (ADYEN.NA)** and **IDEXX Laboratories, Inc. (IDXX)**. These are consistent growers that have not really been impacted by the economic slowdown.

Financials: Holdings within our financials category have been harder hit in the downturn. Financials account for around 21% of the portfolio. Quarter-to-date, it's up 8%, and year-to-date it's down around -17%. Within the category, however, we are seeing a divergence in performance between financial services companies and companies more tied to the macro environment. Companies in the former category, such as FactSet and **MSCI, Inc. (MSCI)**, are doing well. Their clients are actually increasing their usage. As David mentioned, FactSet is up 15% year-to-date. MSCI's stock has increased close to 30% during the same period. These companies are heavily integrated into their clients' businesses through their SaaS business model, and their services are easily accessed in the current work-from-home environment.

Financials that investors view as more tied to macro-economic conditions have been more challenged. This category includes **The Charles Schwab Corp. (SCHW)**, **Brookfield Asset Management, Inc. (BAM)**, and **Arch Capital Group Ltd. (ACGL).** Investors tend to value these stocks based on market conditions, interest rates, and their balance sheets. We look at these companies differently. We focus on their organic growth prospects, the stickiness of their clients, the efficiencies they're able to realize, and product development. We believe some of these companies could even capitalize on market volatility to get new customers onto their platform. Schwab is a good example. Today, it was announced that the Department of Justice approved Schwab's acquisition of TD Ameritrade. We think this acquisition will help boost Schwab's leadership in the RIA space. The economies of scale of the combined companies will also serve to lower Schwab's costs. We are also seeing an acceleration in growth so far this year as the volatile market has prompted people to seek more investment advice.

Real assets: Real assets comprise about 20% of the portfolio. Although they have bounced back a bit so far in the second quarter, they are still down around -29% year-to-date. Nonetheless, we remain confident that these companies will come back when the economy recovers and should be better positioned than their smaller competitors once we emerge from this crisis.

Have you taken advantage of the volatility to add any new positions to the Fund?

Michael Baron: As long-term investors, we don't chase short-term momentum. We did not shift the portfolio drastically on the way down or the way up. That said, we are always looking to initiate or add to positions in companies at attractive prices, and the pandemic has presented a number of opportunities. In Q1, we bought Adyen and Shopify. We also added to Schwab, Zillow, **GDS Holdings Limited (GDS)**, and **Activision Blizzard, Inc. (ATVI)**. We also exited or reduced some positions, partially to help manage leverage and partially for tax reasons.

You own SpaceX in both funds. How do you value it considering it is a private company?

Ron Baron: We look at the current revenue from its launch business and projected future revenue along with debt levels and cash flow. With its reusable rockets, SpaceX offers satellite companies the ability to launch for $60 million while its competitors are charging $200 to $300 million. Other companies don't spend money on research or come up with new ideas. They haven't had to because they have had a lock on the business. [SpaceX CEO] Elon Musk has a different mindset. He is investing in research and development to disrupt the industry and grow his business.

We also think SpaceX's ability to build communications satellites for far less than its competitors has massive potential. Last year, when [SpaceX President] Gwynn Shotwell spoke at our annual conference, I told her that I thought this was a business that could do $30 billion a year in revenue with an 80% profit margin. She told me that she thought the business opportunity was bigger than that.

Any final thoughts you would like to leave us with?

Ron Baron: When you talk to companies on a regular basis over many years like we do, you get a feeling for what's happening in the business, and it enables you to make better judgment calls. We don't care what other people think about the stock market or about the business, for that matter. All we care about is figuring out what a business is worth today and what it's going to become worth over five or ten years. If we're buying it at a big enough discount to what we think it's going to be worth down the road, and we love the business – it's distinct and we think the management team is great – then we invest. We don't wait for other people to make recommendations.

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.

Baron Partners Fund's annualized returns for the Institutional Shares as of March 31, 2020: 1-year, -1.30%; 5-years, 8.18%; 10-years, 12.65%; Since Inception (1/31/1992), 12.34%. Annual expense ratio for the Institutional Shares as of December 31, 2019 was 1.96% (comprised of operating expenses of 1.06% and interest expense of 0.90%). The **Russell Midcap Growth Index**'s annualized returns as of March 31, 2020: 1-year, -9.45%; 5-years, 5.61%; 10-years, 10.89%; Since Fund Inception (1/31/1992), 9.09%.

Baron Focused Growth Fund's annualized returns for the Institutional Shares as of March 31, 2020: 1-year, -3.23%; 5-years, 6.43%; 10-years, 9.57%; Since Inception (5/31/1996), 10.51%. Annual expense ratio for the Institutional Shares as of December 31, 2019 was 1.11%, but the net annual expense ratio was 1.10% (net of the Adviser's fee waivers). The **Russell 2500 Growth Index**'s annualized returns as of March 31, 2020: 1-year, -14.40%; 5-years, 3.64%; 10-years, 10.10%; Since Fund Inception (5/31/1996), 6.99%.

The performance data quoted represents past performance. Past performance is no guarantee of future results. The investment return and principal value of an investment will fluctuate; an investor's shares, when redeemed, may be worth more or less than their original cost. The Adviser reimburses certain Baron Fund expenses pursuant to a contract expiring on August 29, 2030, unless renewed for another 11-year term and the Fund's transfer agency expenses may be reduced by expense offsets from an unaffiliated transfer agent, without which performance would have been lower. Current performance may be lower or higher than the *performance data quoted. For performance information current to the most recent month end, visit www.BaronFunds.com or call 1-800-99BARON.*

Reflects the actual fees and expenses that were charged when the Fund was a partnership. The predecessor partnership charged a 20% performance fee after reaching a certain performance benchmark. If the annual returns for the Fund did not reflect the performance fees the returns would be higher. The Fund's shareholders will not be charged a performance fee. The predecessor partnership's performance is only for periods before the Fund's registration statement was effective, which was April 30, 2003. During those periods, the predecessor partnership was not registered under the Investment Company Act of 1940 and was not subject to its requirements or the requirements of the Internal Revenue Code relating to registered investment companies, which, if it were, might have adversely affected its performance.

Performance for the Institutional Shares prior to 5/29/2009 is based on the performance of the Retail Shares, which have a distribution fee. The Institutional Shares do not have a distribution fee. If the annual returns for the Institutional Shares prior to 5/29/2009 did not reflect this fee, the returns would be higher.

Risks: Specific risks associated with non-diversification and leverage include increased volatility of the Fund's returns and exposure of the Fund to greater risk of loss in any given period. 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.

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.

Diversification does not guarantee a profit or protect against a loss.

Portfolio holdings as a percentage of net assets as of March 31, 2020 for securities mentioned are as follows: **Red Rock Resorts, Inc.** - Baron Partners Fund (0.5%*), Baron Focused Growth Fund (2.0%); **Penn National Gaming, Inc.** - Baron Focused Growth Fund (2.8%); **Choice Hotels International, Inc.** - Baron Focused Growth Fund (4.2%); **Vail Resorts, Inc.** - Baron Partners Fund (4.8%*), Baron Focused Growth Fund (8.7%); **Tesla, Inc.** - Baron Partners Fund (20.4%*), Baron Focused Growth Fund (20.7%); **FactSet Research Systems, Inc.** - Baron Partners Fund (6.4%*), Baron Focused Growth Fund (8.6%); **Hyatt Hotels Corp.** - Baron Partners Fund (4.7%*), Baron Focused Growth Fund (7.1%); **Zillow Group, Inc.** - Baron Partners Fund (3.2%*); **GuidewireSoftware, Inc.** - Baron Partners Fund (2.8%*), Baron Focused Growth Fund (3.5%); **Shopify Inc.** - Baron Partners Fund (0.4%*); **Space Exploration Technologies Corp.** - Baron Partners Fund (5.7%*), Baron Focused Growth Fund (5.6%);**%; Adyen N.V.** - Baron Partners Fund (1.3%*), Baron Focused Growth Fund (1.1%); **IDEXX Laboratories, Inc.** - Baron Partners Fund (7.0%*); **MSCI, Inc.** - Baron Partners Fund (1.3.%*); **The Charles Schwab Corp.** - Baron Partners Fund (3.4.%*); **Brookfield Asset Management, Inc.** - Baron Partners Fund (1.7.%*); **Arch Capital Group Ltd.** - Baron Partners Fund (6.7%*), Baron Focused Growth Fund (3.7%); **GDS Holdings Limited** - Baron Partners Fund (1.4%*), Baron Focused Growth Fund (1.3%); **Activision Blizzard, Inc.** - Baron Partners Fund (1.0.%*).

Top 10 holdings as of March 31, 2020

Baron Partners Fund

Holding	% Assets
Tesla, Inc.	20.4
CoStar Group, Inc.	15.6
IDEXX Laboratories, Inc.	7.0
Arch Capital Group Ltd.	6.7
FactSet Research Systems, Inc.	6.4
Space Exploration Technologies Corp.	5.7

Vail Resorts, Inc.	4.8
Hyatt Hotels Corp.	4.7
The Charles Schwab Corp.	3.4
Zillow Group, Inc.	3.2
Total	77.9
Long Equity Exposure	127.3
Cash & Equivalents	(27.3)

Baron Focused Growth Fund

Holding	% Assets
Tesla, Inc.	20.7
CoStar Group, Inc.	15.9
Vail Resorts, Inc.	8.7
FactSet Research Systems, Inc.	8.6
Hyatt Hotels Corp.	7.1
Space Exploration Technologies Corp.	5.6
Choice Hotels International, Inc.	4.2
Iridium Communications Inc.	3.9
Arch Capital Group Ltd.	3.7
Manchester United plc	3.6
Total	82.0

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

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. **Russell 2500® Growth Index** measures the performance of small to medium-sized U.S. companies that are classified as growth. The indexes and the Funds 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. The indexes are unmanaged. The index performance is not Fund performance; one cannot invest directly into an index.

Non-mutual fund products are available to institutional investors only.

Alpha measures the difference between a fund's actual returns and its expected performance, given its level of risk as measured by beta. **Beta** measures a fund's sensitivity to market movements. The beta of the market is 1.00 by definition.