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The Baron Partners Fund crushed 99% of its peers over the last 15 years while beating the Nasdaq by over 300%. 6 stocks they're betting on for the long-term — and 3 qualities they look for in companies.

By William Edwards

- **Michael Baron co-manages the Baron Partners Fund, a top 1% fund over the last 15 years.**
- **Baron said he looks for companies with a competitive advantage, low valuation, and good management.**
- **The stocks Baron likes include Tesla and MSCI.**



BARON FUNDS

Michael Baron is co-manager of the Baron Partners Fund.

When it comes to long-term returns, even good old index funds can't top the performance of the Baron Partners Fund (BPTRX), not to mention competitors.

The fund is up 1,003% over the 15-year period since mid-October 2008. Over that same time, the S&P 500 is up 385%, and the Nasdaq Composite is up 688%. That puts the Baron fund in the top 1% of similar funds, according to Morningstar data.

So, what's their secret? One of them is concentration: the fund has 85% of its money in just 10 stocks, and the other 15% in another 10. Another is diversification, making sure that those few stocks are spread across various industries which behave differently depending on the economic environment.

That means their selection process is crucial. Michael Baron, who co-manages the Baron Partners Fund, shared with Insider last week three things they look for in companies

when trying to assess if they have a path for sustainable growth.

One is a competitive advantage in the product a firm offers.

"Why can't others do what they're doing?" Baron said. "Understanding why competition can't usurp that opportunity is key."

Second, Baron said he looks for a good management team. Finding one often means speaking directly with a firm's executives about their vision and about concerns that arise.

"We're betting on people. We need to know who the management team is, what motivates them, what's their vision, where they've been successful in the past, and where they've failed in the past," Baron said.

He said his firm's relationship with a management team often develops over years or decades.

"When things arise, and obviously things do all the time, we don't sit here in New York and hypothesize on what's

going to happen and how it's going to shake out," he said. "But we get on the phone with them and understand what the business is doing, what they're seeing, how they're solving the issue that arose, and then trying to independently verify if we believe it."

Finally, there's low valuation. Lower valuations are historically correlated to better longer-term returns, and vice versa. But Baron doesn't always give credence to traditional measures like shorter-term price-to-earnings ratios, and tends to value a company based on his firm's own long-term earnings estimates. He aims for firms he thinks can double in price multiple times within a 10-year period.

Baron shared six stocks he's betting on for the long-term that he believes meet the above criteria.

6 stocks Baron is betting on

The first is electric-vehicle maker Tesla (TSLA), one of the star performers of the market being up 135% year-to-date. Despite its outperformance this year and over the last few years, Baron still believes it has upside.

One reason is because of his faith in CEO Elon Musk, as well as his confidence in the rest of Tesla's upper management team.

"To say that Tesla is only Elon Musk is an incredible oversimplification," he said.

When it comes to competitive advantage, he pointed to their expanding charging station network, which other electric-vehicle manufacturers have adapted to. Cars produced by Ford, GM, Hyundai, and more can charge using Tesla's chargers.

Baron also believes in the company's ability to continue scaling up production, and thinks the auto industry is at a "tipping point" of adopting EVs.

On a number of traditional measures, Tesla is considered to have a very high valuation. For example, its 12-month forward price-to-earnings ratio is 58.48, and its PEG ratio is 2.24. The PEG ratio is a valuation measure that allows for longer-term growth expectations, and 1.0 is considered a normal valuation. The tech sector of the S&P 500, for comparison, has a PEG ratio of 1.3.

However, Baron believes the stock is undervalued over the long-term given the breadth of its potential revenue streams.

"Obviously it looks expensive on a near-term basis," he said. "This is a lot more dynamic of a business than those other companies. Like I said, what can it do with its battery business, its energy business, what can it do with autonomous, what can it do with insurance, what can it do with robotics? There's a lot more ways that this company can win and be significantly different."

Baron also listed a handful of companies in the financials space, which he thinks is overlooked when it comes to growth potential.

One is Arch Capital (ACGL), an insurance company. He said their prices continue to rise, and that they should benefit from higher interest rates. That's also the case for brokerage Charles Schwab (SCHW), he said.

Arch Capital has a fairly low 12-month forward price-to-earnings ratio of 11.82, but no PEG ratio is available. Schwab, meanwhile has a PEG ratio of 1.07.

Schwab is down big this year amid fears surrounding bank failures. It dropped 30% in a matter of days in March and is down 34% year-to-date. But Baron says he's confident the firm will survive the pressure that high rates have put on the sector.

"We spoke to management, going back to our relationship aspect, and understood why this is different than the regional banks," he said. "While there was money flowing off of the balance sheet and into the money market funds, it was staying on the platform, which was key to us."

Next, he listed two financial services firms that provide data and analysis products: FactSet (FDS) and MSCI (MSCI). While new contracts are slow, retention rates have been strong, Baron said, and both firms are growing their capabilities.

"Both companies are entering new areas of growth in terms of providing more products and services, which should improve their average revenue per user," he said.

FactSet has a PEG ratio of 2.21, while MSCI's is 2.48.

Finally, he listed Guidewire (GWRE), a software company for insurance firms. Baron said their profit margins and revenue should increase as they've invested in cloud technology.

"They spent a lot of money over the past few years updating their product to be cloud enabled vs. software," he said.

The firm's PEG ratio is 2.13.

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Baron Partners Fund's annualized returns for the Institutional Shares as of 9/30/2023: 1-year, 5.96%; 5-year, 24.82%; 10-year, 19.31%. The annual expense ratio for the Institutional Shares as of December 31, 2022 was 1.44% (comprised of operating expenses of 1.04% and interest expense of 0.40%).

The S&P 500 Index's annualized returns as of 9/30/2023: 1-year, 21.62%; 5-year, 9.92%; 10-year, 11.91%.

The NASDAQ Composite Index's annualized returns as of 9/30/2023: 1-year, 26.11%; 5-year, 11.41%; 10-year, 14.52%.

The Morningstar Large Growth Category's annualized returns as of 9/30/2023: 1-year, 23.46%; 5-year, 9.04%; 10-year, 11.63%.

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 may reimburse certain Fund expenses pursuant to a contract expiring on August 29, 2034, 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 baronfunds.com or call 1-800-99-BARON.

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Performance for **Baron Partners Fund** 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.

Risks: The Fund is non-diversified which means, in addition to increased volatility of the Fund’s returns, it will likely have a greater percentage of its assets in a single issuer or a small number of issuers, including in a particular industry than a diversified fund. Single issuer risk is the possibility that factors specific to an issuer to which the Fund is exposed will affect the market prices of the issuer’s securities and therefore the net asset value of the Fund. As of the most recent quarter-end, about 41% of the Fund’s long positions are invested in Tesla stock. Therefore, the Fund is exposed to the risk that were Tesla stock to lose significant value, which could happen rapidly, the Fund’s performance would be adversely affected. Specific risks associated with leverage include increased volatility of the Fund’s returns and exposure of the Fund to greater risk of loss in any given period.

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

Portfolio holdings as a percentage of long investments as of September 30, 2023 for securities mentioned are as follows: MSCI Inc. (1.7%); Guidewire Software, Inc. (1.1)%.

Baron Partners Fund

Top 10 Holdings as of September 30, 2023

Holding Name	% of Total Investments
Tesla, Inc.	41.0
Space Exploration Technologies Corp.	8.1
CoStar Group, Inc.	7.6
Arch Capital Group Ltd.	7.0
Hyatt Hotels Corporation	4.8
IDEXX Laboratories, Inc.	4.7
FactSet Research Systems Inc.	4.3
The Charles Schwab Corp.	3.9
Vail Resorts, Inc.	3.3
Gartner, Inc.	3.2
Total	88.0

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

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Price/Earnings Ratio (next 12-months): is a valuation ratio of a company's current share price compared to its mean forecasted 4 quarter sum earnings per share over the next twelve months. If a company's EPS estimate is negative, it is excluded from the portfolio-level calculation.

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