Portfolio Review

- The fund underperformed its benchmark, the Russell 1000® Growth Index, largely due to stock selection in the information technology, healthcare, consumer staples and energy sectors as well as our allocation to the consumer discretionary, healthcare and industrials sectors. Stock selection in the consumer discretionary, financials and industrials sectors as well as our allocation to the consumer staples and information technology sectors contributed to relative performance.

- The fund is an actively managed strategy with a long-term, private equity approach to investing. Through our proprietary bottom-up research framework, we look to invest in those few high-quality businesses with sustainable competitive advantages and profitable growth when they trade at a significant discount to intrinsic value (our estimate of the true worth of a business, which we define as the present value of all expected future net cash flows to the company).

- All aspects of our quality-growth-valuation investment thesis must be present for us to make an investment. Often our research is completed well in advance of the opportunity to invest. We are patient investors and maintain coverage of high-quality businesses in order to take advantage of meaningful price dislocations if and when they occur. During the quarter, we added to our existing positions in Oracle, Schlumberger and Regeneron Pharmaceuticals as near-term price weakness created a more attractive reward-to-risk opportunity. We trimmed our existing position in Alibaba as it approached our maximum allowable position size.

Class Y Performance as of December 31, 2017 (%)

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<th>Cumulative Total Return</th>
<th>Average Annualized Return</th>
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<tr>
<td></td>
<td>3 MONTH</td>
<td>YTD</td>
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<tr>
<td>Fund</td>
<td>6.23</td>
<td>32.64</td>
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<tr>
<td>Benchmark</td>
<td>7.86</td>
<td>30.21</td>
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Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results. Investment return and value will vary and you may have a gain or loss when shares are sold. Current performance may be lower or higher than quoted. For most recent month-end performance, visit www.loomissayles.com.

Additional share classes may be available for eligible investors. Performance will vary based on the share class. Performance for periods less than one year is cumulative, not annualized. Returns reflect changes in share price and reinvestment of dividends and capital gains, if any. You may not invest directly in an index.

Gross expense ratio 0.66% (Class Y). Net expense ratio 0.66%. As of the most recent prospectus, the investment advisor has contractually agreed to waive fees and/or reimburse expenses once the expense cap of the fund has been exceeded. This arrangement is set to expire on 1/31/2018. When an expense cap has not been exceeded, the fund may have similar expense ratios.

The Class Y inception date is 5/16/1991. Class Y shares are sold to eligible investors without a sales charge; other Classes are available for purchase.
Contributors

- Online retailer Amazon offers millions of products – sold by Amazon or by third parties – with the value proposition to consumers of selection, price, and convenience. Amazon’s enterprise IT business, Amazon Web Services (AWS), offers a suite of secure, on-demand cloud-computing services, with a value proposition to clients of speed, agility, and savings. In both of its core markets, Amazon possesses strong and sustainable competitive advantages that would be difficult for competitors to replicate. In e-commerce these include its brand, scale, technology platform, network advantage, and logistics and distribution systems. AWS benefits from its massive scale which allows it to pass along cost savings while continuing to innovate. Growing well in excess of their underlying markets, both of Amazon’s businesses are gaining market share. Led by visionary founder Jeff Bezos, Amazon invests aggressively to expand and leverage its customer base, brand, and infrastructure, targeting businesses with strong financial returns that are anticipated to offer large and enduring growth opportunities.

A long-term holding, Amazon’s quarterly financial results exceeded management and consensus expectations for revenue, operating profit, and earnings per share (EPS). Net sales of $43.7 billion increased 34% year over year when including the contribution of Whole Foods. On an organic, constant currency basis, Amazon’s core franchise grew 29% over the prior year period. E-commerce, including retail subscription services such as prime membership and digital media subscriptions, accounted for approximately 85% of total net sales. We estimate that gross merchandise volume (GMV) grew over 30%, well above our estimate of growth in the teens for US e-commerce and low single-digit growth in global retail sales. North America accounted for approximately 65% of e-commerce sales while Amazon’s international segment contributed approximately 35%. Comprising 10% of total net sales, AWS revenue increased 42% compared with the year-ago quarter, significantly faster than our low single-digit growth estimate for global enterprise IT spending. The AWS annual revenue run rate now exceeds $18 billion. Revenue from Amazon’s physical stores, primarily Whole Foods but also including 12 Amazon book stores and other store-based purchases, was $1.3 billion and accounted for 3% of total net sales. The company articulated its vision for the Whole Foods acquisition, which is to make high quality, organic food affordable for everyone. Since the acquisition closed in August, Amazon has launched Whole Foods private label products on Amazon, added Amazon lockers to select Whole Foods store locations, started to integrate Prime benefits into a Whole Foods customer rewards program, and is taking steps to integrate Whole Foods with its other food and grocery initiatives such as Prime Now and Amazon Fresh. While we expect Amazon to continue to grow its presence in the food and beverage category, our investment thesis for Amazon is not dependent on the acquisition’s success.

With Amazon’s sales mix shifting increasingly to higher-margin product categories such as third-party e-commerce sales, AWS, and advertising, gross margins improved 200 basis points year over year to 37.1%. Gross income increased 41% year over year. Overall, Amazon reported adjusted operating income of $1.43 billion, up 4% compared with the year-ago quarter. Amazon continued rapid investment in key areas that capitalize on its strength, focusing on businesses with high, durable growth prospects and strong financial returns. Management highlighted investments in its “Alexa” voice-enabled products, which included five new Alexa-enabled devices, the introduction of Alexa in India, integration with BMW cars and Sonos speakers, and the now more than 25,000 skills that Alexa
can perform. The company reported that tens of millions of the Alexa-enabled devices have been purchased and the number of customers has increased by over five times year over year. Amazon also announced that it entered the electronics category in Brazil in partnership with third-party sellers, and expanded its business-specific purchasing solutions service, Amazon Business, to Japan and India, its fourth and fifth countries. The rapid pace of investment was reflected in part in higher operating expenses, and overall operating margins fell 90 basis points from the year-ago quarter to 3.3%. Operating expenses for fulfillment increased as a percentage of revenue by about 140 basis points to 14% of sales, and technology and content rose 90 basis points to 12% of sales. General and administrative expenses were up by 20 basis points to 1.9%, and marketing costs as a percentage of sales increased 30 basis points to 5.4%. AWS grew operating income 38% to $1.17 billion, with operating margins of 25.5%, down 110 basis points versus the year-ago quarter. Operating cash flow increased 14% to $17 billion compared with the previous trailing 12-month period, while free cash flow fell 10% in the period to $8 billion.

On a global basis, e-commerce represents approximately 9% of an estimated $15 trillion global retail market. Amazon’s GMV represents about 20% of e-commerce and just less than 2% of the global retail market. We believe a long-term, secular transition from traditional brick-and-mortar retail to e-commerce is still in its early stages and that e-commerce will come to represent a significantly higher portion of the global retail market. A disruptive force, Amazon’s structural operational advantages, network effect, and relentless focus on customer service position the company to grow faster and more efficiently than its traditional or online retail competitors. Also a disruptive force, we believe AWS is well positioned in the nascent and underpenetrated cloud computing services market, where we believe from an operating profit standpoint the potential can approach 50% of the company’s core retail opportunity. Over our investment time horizon, we believe Amazon can generate attractive and sustainable revenue growth, faster operating margin expansion, and free cash flow growth that is not currently reflected in the share price. As a result, the company is selling at a significant discount to our estimate of intrinsic value and offers a compelling reward-to-risk opportunity.

• Qualcomm designs, manufactures, and markets digital telecommunication integrated circuits (chipsets) and services, and is the global market share leader in 3G and 4G integrated circuits. The QTL segment (Qualcomm Technology Licensing) collects license fees from manufacturers for the right to use Qualcomm’s intellectual property (IP) in chipset designs as well as follow-on royalty fees on the worldwide sale of devices incorporating these chipsets. The highly profitable segment historically accounted for approximately 20% of revenues and 80% of operating profits. The QCT segment (Qualcomm CMDA Technologies) is a leading manufacturer and supplier of chipsets enabling wireless communication, particularly in mobile devices. QCT collects revenue from the sale of its chipsets to device manufacturers, historically representing approximately 80% of revenues and 20% of operating profits.

A long-term holding, Qualcomm reported stronger-than-expected quarterly results, led by the QCT segment, which sustained strong traction in China across all price tiers for its innovative mobile chipsets, and demonstrated strong growth in non-mobile applications. Shares were up sharply on an unsolicited bid from Broadcom to acquire Qualcomm for $70 per share, a 28% premium to the share price at the time of offer. Qualcomm’s Board of Directors unanimously rejected the proposal on the grounds that it substantially
undervalues the company relative to its leadership position and growth prospects in mobile technology. As the pioneer of 3G and 4G wireless communications technology, we believe Qualcomm possesses difficult-to-replicate competitive advantages in the engineering, design and manufacturing of the basebands and modems used in mobile devices. The company’s extensive portfolio of IP, which is the globally accepted standard for 3G and 4G wireless technologies, enables it to operate as a near monopoly. Although Qualcomm faces competition in the development of intellectual property for future generations of digital wireless communications technology and services, typical of its long-term approach, the company has been investing in next-generation mobile wireless technology where true global adoption could be a decade away. Leveraging its pioneering technology, cumulative IP and engineering skill, we believe Qualcomm is well positioned to maintain its leadership over the long term. We believe that Broadcom’s offer undervalues the company and highlights the value of Qualcomm’s IP, which has been underappreciated as the market has been focusing on the company’s near-term dispute with Apple.

With respect to the dispute with Apple, we believe the following. The industry-standard business model for mobile OEMs (original equipment manufacturers) has been in place for decades and withstood much scrutiny and many challenges. The model is that patent royalty rates are based on the value of the total device, not the value of the communication chipset itself. Qualcomm has demonstrated that a material amount of the perceived value of a mobile device is due to the capability of the cellular connectivity, not only due to non-cellular communication features and characteristics. The phone is primarily valuable because of its communication capability, including movement of data. Demonstrating the value of its contribution, Qualcomm has successfully argued that it must be allowed to recoup its research and development investments in order to fund ongoing innovation. Innovation in high-quality cellular communications benefits all players in the value chain, including phone manufacturers, mobile service providers, and players in emerging business models. In November, the two companies filed countersuits and additional patent infringement claims consistent with each company’s respective positioning and legal strategy.

Challenges to Qualcomm’s business model and royalty rates are not new and the company has successfully defended its business model numerous times over the last 10 to 20 years. In a particularly successful case, Qualcomm recently prevailed in China, where the NDRC (National Development and Reform Commission) had the opportunity to rewrite local industry rules for IP royalties, but instead validated Qualcomm’s business model. The settlement of this and previous cases has not only repeatedly upheld and validated Qualcomm’s business model, but established a body of legal precedent in a variety of jurisdictions around the world.

In our view, the current challenges to Qualcomm’s business model involving Apple are no different from previous challenges, except for Apple’s aggressiveness in its pursuit. This is not necessarily indicative that Apple has a strong case. We believe Apple is trying, as others have, to lower its royalty payment to Qualcomm. Because the royalty fees paid by mobile device manufacturers to Qualcomm are not insignificant, it is a rational decision to attempt to try to force the fees lower. Apple has previously taken a similarly aggressive approach with other IP providers. For example, in January 2015, after two years of negotiation with Apple, Ericsson filed a lawsuit against Apple for nonpayment of royalties. In December 2015, Apple settled the suit with Ericsson, which subsequently reported a significant increase in IP revenue, signaling to us that the basis of the agreement remained intact.
We believe the decades-long industry practice that has been repeatedly validated, and is backed by regulations around the world, is not likely to be overturned. We continue to stay informed of the situation.

For the quarter, overall revenue was down 5% year over year to $5.9 billion, above the midpoint of management guidance, and operating income fell 28%. Qualcomm’s chip-making business, QCT, reported segment revenue increased 13% year over year to $4.65 billion, with gains in shipments, average selling prices (ASPs), and non-mobile chip revenue each contributing positively. Shipments rose 4%, above the midpoint of management guidance, reflecting strong performance in China across all price tiers. Implied ASPs rose 8% due to a positive chipset product mix, as consumers in China opted for higher-end products with greater features. The segment also benefited from sales of non-mobile chip products, which accounted for 20% of segment sales over the past year. Strong segment margins of 21% were at the high end of management guidance and represented the sixth consecutive quarter of year-over-year margin improvement.

Royalty revenue in the QTL patent licensing segment declined 36% year over year to $1.21 billion as Apple’s contract manufacturers continued to withhold payment due to the ongoing dispute. QTL segment margins fell to 68% from 84% in the prior-year quarter and represented the lowest reported quarterly rate in the past 17 years. The loss of top-line revenue, coupled with heightened legal expenses from Qualcomm’s litigation strategy against Apple, accounted for the decline in margins, which we believe will represent the low point for segment margins. Finally, Qualcomm now sees its proposed acquisition of NXP Semiconductors potentially closing in the first quarter of 2018. NXP, a Netherlands-based chip manufacturer focused primarily on automotive markets, has sustainable competitive advantages in attractive areas of the semiconductor industry that are complementary and higher margin than Qualcomm’s QCT business.

We continue to believe that the body of legal precedent established in multiple jurisdictions worldwide over the past twenty years supports Qualcomm’s royalty business model. Additionally, we believe the proposed offer from Broadcom undervalues Qualcomm’s business, assigning little value to the company’s royalty model, which we believe will remain intact. We like the long-term positioning of Qualcomm as a standalone company to benefit from the long-term secular growth in mobile devices. We believe the shares are currently selling at a significant discount to our estimate of Qualcomm’s intrinsic value, offering a compelling reward-to-risk opportunity. We will continue to closely monitor and assess any proposal that would fully compensate shareholders for the intrinsic value of the company.

- **Cisco** designs, manufactures, and markets internet networking equipment and provides related technical services. Focused on the differentiated segments of data networking, the company participates primarily at the high end of the market, globally supplying the major internet service providers, major multi-national enterprises, and local enterprises. Cisco’s end-to-end architecture solution makes the company uniquely positioned to benefit from the exponential growth in internet traffic which will require a corresponding exponential increase in bandwidth capacity.

A long-term holding, Cisco reported quarterly results that were better than consensus expectations and, for the first time in over a year, provided positive guidance for year-over-year growth in the coming quarter. Cisco is transitioning its business to a software and product subscription business model, under which a portion of revenue that was
previously recognized up front is now earned as recurring revenue over time. Because the initial subscription payment is lower than the revenue booked in the up-front model, the transition creates a near-term revenue headwind. However, over the long run, recurring revenue generates a higher customer lifetime value. We believe growth in recurring revenue will also improve the overall quality of the business by increasing the visibility of future revenue streams, lowering cyclicality and raising profitability. For the quarter, revenue fell 2% year over year to $12.1 billion, in line with management’s guidance of -1% to -3%. Cisco’s product segment revenue, about 75% of total revenue, was down 4% while its services segment revenue rose 1% and accounted for about 25% of total revenue. Deferred product revenue from recurring software and subscriptions increased 37% compared to the year-ago quarter. Total recurring revenue accounted for approximately 32% of total company revenue, up from 29% in the year-ago quarter, demonstrating Cisco’s ability to embrace major industry transformations, execute well, and lead with a unique architectural approach encompassing hardware, software, and services.

Beginning this quarter, Cisco regrouped its product segment reporting categories. Infrastructure platforms is the largest product category, accounting for approximately 58% of total revenue. It includes routers, switches, data center servers, and wireless products. Applications accounted for approximately 10% of total revenue and includes collaboration products, Internet of Things software, and the recently acquired AppDynamics business. Security, about 5% of total revenue, includes unified threat and advanced threat protection, and web security products. Other products accounted for about 2% of total revenue. Revenue from infrastructure platforms declined 4% year over year, predominantly due to spending weakness by internet service providers on routers. Switching revenues were down modestly, but data center switches, representing about one-third of switching revenue, continued to experience strong growth in the ACI (application centric infrastructure) portfolio. ACI is a unique software-defined network (SDN) solution offering full visibility and integrated management of physical and virtual networked IT resources, that has seen strong uptake among data center clients. Weakness in switching revenue came from the larger campus network business where Cisco is the market leader. Representing about two-thirds of switching revenue, Cisco has been unable to drive growth in its campus category because it lacked the innovation needed to drive an upgrade cycle. However, the company reported a solid pace of adoption for its new Catalyst 9000 series switching products – announced earlier this year - with 1,100 new customers added to date, including 200 in the most recent quarter. The Catalyst 9000’s unique automation feature reduces customer operating expenses – which represents the lion’s share of IT department operating budgets – and creates an economic incentive to upgrade. The new switch series also offers higher security features such as malware detection. Cisco reported that the vast majority of customers opted for the highest level subscription, key progress in this segment as the company transitions to a recurring revenue business model. Unlike in prior upgrade cycles, Cisco has also made the subscription backward compatible with prior hardware generations, allowing the company to monetize features even if customers opt not to upgrade to the newest hardware. Another attraction of the subscription model is that it allows customers to more easily adopt future functionality and innovations from Cisco’s vast and differentiated capabilities in security, collaboration, and wireless. This approach makes it less likely that customers will base their decisions solely on the price of competing hardware options. Cisco expects to extend this model to other core products, which we believe will contribute to recurring revenue within the product segment growing from approximately 12% today to closer to 40% over our investment time horizon.
Cisco reported 6% growth in its applications category driven primarily by AppDynamics, an application performance monitoring business which Cisco acquired in March 2017. Deferred revenue for collaboration products grew by 18%. Revenue in the security category increased by 8% year over year on double-digit growth in unified threat, advanced threat, and web security products. Cisco’s security business is outperforming peers as customers prefer Cisco’s complete architecture solutions that can manage the growing complexity of a multi-cloud environment. Security product deferred revenues grew by 42% versus the prior-year quarter.

Cisco also gained traction in its relationships with large web-scale providers such as Microsoft, Google, and Alibaba. Cisco expanded its partnership with Microsoft, most recently collaborating to allow customers to operate highly secure hybrid cloud environments using Azure. In its newly announced partnership with Google, Cisco solutions will enable seamless cloud experience across private, public or hybrid cloud environments. The growing tendency for enterprises to operate in a multiple-cloud environment plays to Cisco’s strength in networking, and the company’s partnerships are giving it the opportunity to provide increasingly customized solutions to one of the fastest growing segments of data center spending. Cisco also announced its first partnership with Alibaba to employ its data switching hardware – SDN-enabled Nexus 9000 and ACI automation - to improve Alicloud’s agility and efficiency.

Accounting for about 25% of total revenue, services segment revenue rose 1% year over year, while deferred revenue was up 5% in the segment. Cisco cited growth in software and solution services. Looking at Cisco’s three geographic segments, growth was up 1% in both the Americas and the Asia Pacific, Japan, and Greater China regions, and 2% in Europe, the Middle East, and Africa. Emerging market revenue declined 6% on continuing economic weakness, with Brazil, Russia, India, China, and Mexico accounting for a 9% decline as a group.

Cisco reported gross and operating margins of 63.7% and 30.4%, respectively, at the high end of guidance, but down year over year on a recent increase in DRAM chip costs. Focused on profitable growth without sacrificing margins, Cisco is able to make strategic and productive investments. This focus has enabled the company to make better use of its scale, pursuing both organic innovation and increasing its acquisition of niche technology companies that align with its business transition goals. We believe Cisco continues to execute well in its business transition, maintaining its successful track record of embracing major industry transformations. Leading with its unique end-to-end architectural approach, including differentiated hardware and software solutions, Cisco is well positioned to benefit from the growth in cloud computing and new networking architectures. The company also benefits from its strong ecosystem of distributors and resellers and its strong installed base. The shares are selling at a discount to our estimate of intrinsic value, offering a compelling long-term reward-to-risk opportunity.

Detractors

• Purchased in the third quarter of 2016, Regeneron Pharmaceuticals, Inc. is a fully integrated biopharmaceutical company that discovers, invents, develops, manufactures, and commercializes medicines for the treatment of serious medical conditions. The company was among the leading detractors for the quarter. Regeneron reported strong revenue and earnings per share growth that were both above consensus expectations. Sales of Eylea, a
treatment for eye diseases and the company’s largest revenue generator, grew both in the US and internationally, and Dupixent, a treatment for atopic dermatitis, showed solid and improving acceptance in its first full quarter after being launched. However, the company reported that Phase 2 clinical trials for a combination therapy of Eylea and Regeneron’s ANG2 molecule failed to demonstrate greater efficacy than Eylea alone in the treatment of eye disease. The outcome is significant because success for the combination therapy would have further differentiated Eylea from competitors and sustained the therapy’s competitiveness past Eylea’s patent expiration. The failure of the trial increases the likelihood that Eylea will eventually face heightened competitive pressure. In the near term, competition is likely to come from Novartis’ RTH-258 therapy, its successor to Lucentis, which showed comparable efficacy to Eylea in Phase 3 clinical trials and could come to market in late 2018 or early 2019. Longer term, Eylea is expected to face competition from biosimilar therapies following the expiration of its relevant patents in the early-to-mid 2020s.

The outcome is a negative for Regeneron and lowers our assessment of the company’s intrinsic value. Despite the decrease in our assessment of Regeneron’s intrinsic value, the reward to risk remains attractive given our long-term investment thesis and our view of Regeneron as an innovative and differentiated company with significant growth opportunities remains intact. Regeneron was established in 1988 with the vision of empowering scientists to shape the path of the business by advancing long-term scientific outcomes over short-term results. Regeneron-invented technologies include VelocImmune, a patented technology for creating fully human monoclonal antibodies, enabling rapid discovery and development of viable candidates for clinical trials. With this accelerated process, the time and capital required for pre-clinical research is reduced, allowing Regeneron to significantly outpace its competition in bringing new therapies to trial, and ultimately to market. As a result, Regeneron was able to negotiate risk-mitigating collaborations with larger biopharmaceutical company partners which fund early-stage research and development (R&D) in exchange for a share of potential profits and research cost reimbursement, and through which Regeneron accesses scale and distribution strength. We continue to believe that Regeneron’s science-driven culture, unique technology, and long-term focus on delivering innovative medical solutions will result in substantial value creation over our investment horizon. However, as the current revenue base remains relatively small compared with more diversified biopharmaceutical companies, the success or failure of individual pipeline candidates can result in higher near-term share price volatility. We believe Regeneron is among the highest quality businesses in healthcare, and the share price embeds a lack of appreciation for the company’s multiple growth opportunities and the uniqueness of its business model.

For the quarter, revenue increased 23% year over year to $1.52 billion, above consensus expectations of $1.46 billion. Earnings per share grew 27% year over year to $3.99, ahead of consensus expectations of $3.84 on lower-than-expected R&D expenses. The timing and booking of R&D expense reimbursements between Regeneron and its collaboration partners can skew revenues, margins, and earnings per share from quarter to quarter. While the timing of these partner payments and reimbursements can result in meaningful swings in the profitability of the business over the short term, the revenue results from each of the products provide insight into the underlying structural performance of the overall business. US sales of Eylea were up 13% year over year to $953 million. Greater penetration of the patient population drove growth that was above management’s guidance for single digit
growth in 2017. Outside of the US, where Regeneron splits profits with marketing partner Bayer AG, sales for Eylea were $555 million, up 17% year over year. Sales were driven by continued strong adoption, with estimated market share growing by over 2% to 53.6%. Regeneron’s revenues from its partnership with Bayer were $205 million, up 20% over the prior-year quarter, with sales of Eylea representing the majority of that revenue. While we now expect Eylea to face heightened competition in the future, with greater clarity on the competitive landscape given the likely approval of competitor RTH-258 from Novartis and unsuccessful trial of Regeneron’s co-formulation with ANG2, we believe Eylea’s competitive advantages remain intact. Eylea has established itself as the leading branded therapy in treating a broad range of diseases of the back of the eye. Its superior efficacy over both the short and long term, long-term durability of results, and attractive safety and side effect profile, have made it the market leader and choice of physicians across multiple indications - a position that will be difficult for new competitors replicate.

In its first full quarter on the market, Dupixent generated sales of $90 million. Management reported that Dupixent has now been prescribed 23,000 times, and the more than 5,100 doctors who have written prescriptions represent approximately 70% of the atopic dermatitis specialists in the US, demonstrating early acceptance among doctors. The treatment also received approval in Europe, where it was launched in late September. In addition to atopic dermatitis, Dupixent is being studied for use in a number of other indications, including asthma, nasal polyps, and eosinophilic esophagitis (EoE). Regeneron reported positive Phase 3 results for the treatment of two types of asthma, and positive Phase 2 results for severe-to-moderate EoE, for which the FDA granted the treatment its orphan drug designation in September. Management continues to believe that the drug could receive approval for multiple disorders, thereby expanding the addressable market.

Despite patent infringement litigation with Amgen, sales of Praluent were solid, generating $49 million in revenue during the quarter and growing 29% over the prior-year quarter. In October, an appellate court vacated a prior permanent injunction against the sale of Praluent and ordered a new trial, providing Regeneron and partner Sanofi the opportunity to reintroduce evidence supporting their claims. While the loss of Praluent would be a negative for the company, Regeneron’s long-term success will be driven by the growth opportunities arising from its broad-based, established therapies and meaningful pipeline assets, which include 16 product candidates in clinical development that were generated using the company’s proprietary VelocImmune technology. The company’s shares trade at a substantial discount to our estimate of intrinsic value, and represent an attractive reward-to-risk proposition.

**Autodesk** is a global leader in 3D design software and services, providing state-of-the-art solutions to customers in the architecture, engineering, construction, manufacturing, digital media, consumer, and entertainment industries. Autodesk’s design software allows clients to design, visualize, and simulate real world performance and document their ideas through the creation of digital prototypes. A fund holding since 2012, Autodesk was among the largest detractors from performance during the quarter. The company reported fundamentally healthy results as it transitions to a subscription-based licensing business model from an up-front licensing plus maintenance model. Although the transition causes near-term income statement and cash flow metrics to remain depressed, Autodesk’s progress can be seen from the strong growth in annualized recurring revenue (ARR), which grew 25% year over year. However, Autodesk reduced its quarterly guidance for
net new subscriptions by 12,000 to 638,000 and provided revenue guidance that was approximately 0.5% below expectations, but reaffirmed its longer-term expectations. The company also announced a restructuring plan intended to prioritize resources in support of new CEO Andrew Anagnost’s refocused strategy. The strategic focus remains on completing the subscription-based transition, digitizing the company, and reimagining manufacturing, construction, and production. More specifically, the restructuring will focus on strengthening the digital infrastructure of the company, increasing its marketing and development spending in construction, and continuing to invest in its core products. As part of the restructuring, Autodesk plans to reduce staffing levels by 13% and consolidate certain leased facilities, with an expected pre-tax cost of $135 million to $149 million. We believe Autodesk is well positioned in the structurally attractive design software industry. Its new cloud-computing and mobile products are expanding its addressable market and improving its competitive advantages. With its new subscription-based business model leading to increased customer lifetime value, we believe margins will improve significantly over our investment time horizon, driving double-digit free cash flow growth.

Autodesk reported $515 million in quarterly revenue, a 6% increase in constant currency, slightly above both management and consensus expectations. Revenue generated by the new subscription-based business model increased a robust 107% year over year to $231 million, 45% of total revenue, reflecting strong uptake on all new subscription plan offerings. Partially offsetting this growth was the anticipated decline in traditional up-front licensing revenues and associated maintenance plan subscriptions. Total ARR, which provides better visibility of future revenue streams, increased 25% year over year and accounted for 92% of the revenue mix compared with 78% in the year-ago quarter, with new model subscription plans representing 49% of ARR, up 108% from the year-ago quarter. Looking at quarterly results in terms of client growth, new model subscribers totaled 1.9 million at quarter-end, up 307,000 sequentially from the prior quarter. The company has benefitted from its maintenance to subscription program, which converted 110,000 customers, approximately one-third of eligible clients this quarter, up from the mid-20% level in the prior quarter. Total subscriptions of 3.59 million grew 22% year over year and rose 146,000 from the previous quarter, with growth in new model subscriptions offset by the decline in legacy model maintenance subscriptions, which were discontinued for most products. Clients new to Autodesk accounted for about 30% of new product subscriptions during the quarter and illustrate how Autodesk’s new cloud-computing and mobile products have expanded its addressable market. The company reported that its total average revenue per subscriber (ARPS) of $530 was up 2% year over year. We expect to see mid-single digit improvement in ARPS over our investment horizon. Another model transition-related initiative is to increase direct enterprise and e-commerce sales, which grew to 30% of total sales, compared with 29% in the year-ago quarter. We believe this distribution and servicing strategy can improve the company’s cost structure and its ability to service clients.

Autodesk’s attractive financial model contributes to the quality of the business and will improve as the company moves closer to a 100% subscription-based business model. Near term, margins, earnings, and cash flow are predictably under pressure. Free cash flow for the quarter was -$64 million, a decline of $41 million from the prior year quarter. Adjusted EBIT (earnings before interest and taxes) margins of -5% were an improvement from -9% in the prior year quarter, impacted by the decline of traditional license revenue which was offset by lower expenses. Adjusted EPS (earnings per share) of -$0.12 was better than consensus expectations of -$0.13 and management guidance of -$0.14. The company’s
balance sheet remains strong with positive net cash and investments of $130 million, after spending $117 million to purchase approximately 1.2% of outstanding company shares during the period. Following the trough from the effects of the model change, we believe profitability and cash flow will increasingly improve over our investment time horizon. We believe Autodesk can generate attractive and sustainable revenue growth, faster operating margin expansion, and free cash flow growth that is not currently reflected in the share price. As a result, Autodesk’s shares are selling at a significant discount to our estimate of intrinsic value, creating a compelling reward-to-risk opportunity.

• **Cerner** is a leading supplier of healthcare information technology (HCIT) solutions. Connecting healthcare providers and patients at more than 27,000 facilities worldwide, Cerner offers mission-critical enterprise software solutions for the clinical, financial and operational needs of healthcare organizations of every size. Cerner was founded in 1979 and held its IPO in 1986, and has grown mainly organically in addition to its 2015 acquisition of Siemens Health. Cerner’s HCIT solutions are used by consumers, single doctor practices, hospitals, employers, and countries, and include software, professional services, medical device integration, remote hosting, and employer health and wellness services. Its mission is to contribute to the improvement of healthcare delivery and the health of communities. The company is focused on providing systems that support evidence-based clinical decisions, reducing medical errors and providing information to patients. Its core product platform, Millennium, offers over 60 solutions tailored to the varied needs of different healthcare segments, and is deeply embedded in client workflows, creating high switching costs. As a result, client retention is high and relationships can last for decades. A newer opportunity for Cerner is developing products and services around population health initiatives, which will support the healthcare industry’s transition from a fee-for-services reimbursement model to a risk-based model tied to performance and costs. This transition is still in its early stages, and we believe this segment of the healthcare market will be a large growth driver for the industry over the long term.

A holding in the fund since the fourth quarter of 2015, Cerner was among the largest detractors from performance during the quarter. Cerner reported quarterly results that were fundamentally sound, but total revenue and earnings per share (EPS) were at the low end of management’s guidance and below consensus expectations. New bookings were substantially below guidance and consensus expectations, reflecting several large deals that were expected to close in the quarter but did not. The decision to purchase and integrate enterprise HCIT represents a critical decision for an organization which can last for over a decade. Given the size and scope of the contracts, which may involve outsourcing, replacement of existing software, and transfer of employees, the timing of new contracts can be difficult to predict. This was also reflected in the prior quarter when new bookings were substantially above both management’s guidance and consensus expectations. Despite the volatility of quarterly new bookings, the company generated very strong free cash flow and remains on track for high-single-digit growth in both revenues and new bookings for the year.

Total revenue of $1.28 billion rose 8% year over year, but was below consensus expectations of $1.3 billion. Cerner reports revenues in three segments. Ultimately, almost 75% of Cerner’s revenue is derived from software-related business activity. The system sales segment, which accounts for approximately 26% of revenue, includes the licensing of software, software-as-a-service (SAAS) offerings, upgrades, installations, content
subscriptions, transaction processing, and the sale of computer hardware and sublicensed hardware. System sales revenue of $324 million grew 8% year over year, benefiting from growth in license software and subscriptions that was partially offset by a decline in its technology resale business. The support and maintenance segment, about 21% of revenue, includes software support and hardware maintenance, remote hosting, and managed services. Support and maintenance revenue of $263 million rose 4% year over year, driven by software support and hardware maintenance. The services segment, which accounts for about 53% of revenue, represents all professional services to clients and rose 9% year over year to $664 million, with revenue driven by revenue cycle management products, IT Works, and hosting services. By geography, US sales of $1.13 billion represented 89% of total revenue and rose 7% over the prior year quarter. International sales of $142 million accounted for 11% of total revenue and grew 10% year over year, with strong contributions from several regions.

New bookings of $1.11 billion were down 23% over the prior-year quarter, and were 27% below consensus expectations due to timing. Management indicated that some of the deals which failed to close in the third quarter have since closed or were expected to close in the fourth quarter. Management provided new bookings guidance for the fourth quarter that was over 20% higher than consensus expectations, reflecting its confidence that the deals were still likely to close. A substantial portion of the delayed deals were IT Works contracts in which clients fully outsource management of their HCIT platform to Cerner, with revenues recognized over the life of the contract. However, a portion of the delayed contracts related to high-margin managed and professional services, which contribute more quickly to earnings, and therefore contributed in part to lower-than-expected EPS. Of the new bookings, 25% represented new long-term contracts, and 30% were from outside the company’s installed base of Millennium users, representing clients that are new to the company. In particular, the company continues to have success with sales of its revenue cycle management offerings, which have been improved and expanded over the past several years and provide a large cross-selling opportunity to existing clients as well as contributing to new client wins. The company’s population health offerings have also contributed to new booking growth. Cerner announced that it was selected as the supplier of choice in Sweden, where it will provide its core solution to 10 hospitals and 190 primary care locations, representing its first Nordic population health client. Finally, the company still expects to sign a contract with the US Veterans Administration, which would represent the largest HCIT project in history and provide a large and visible earnings opportunity for the company.

Cerner generated solid gross margins of 84.1% which were down 50 basis points year over year. Adjusted EBIT (earnings before interest and taxes) margins of 23.1% declined 130 basis points, driven by a 9% year-over-year increase in operating expenses. The increase in expenses was due primarily to higher personnel costs related to revenue-generating employees and higher software development expenses. Adjusted EPS of $0.61 was up 3% year over year, 1.6% below consensus expectations. The company generated $223 million of free cash flow in the quarter, which represented 28% of revenue and grew 87% over the prior-year quarter. Capital expenditures of $140 million represented 11% of revenue and remained elevated as the company continues to invest in growth initiatives. Cerner maintains a strong balance sheet with net cash of $429 million. We believe that Cerner can grow revenue in the high single digits over our investment horizon, with faster growth in earnings and cash flow as the company improves margins and benefits from lower capital
intensity. We believe the shares are selling at a discount to our estimate of intrinsic value, offering a compelling long-term reward-to-risk opportunity.

**Outlook**

- Our investment process is characterized by bottom-up, fundamental research and a long-term investment time horizon. The nature of the process leads to a lower-turnover portfolio in which sector positioning is the result of stock selection.

- The fund ended the quarter with overweight positions in the consumer staples, information technology, financials, healthcare and energy sectors and underweight positions in the consumer discretionary and industrials sectors. We did not own positions in the materials, real estate, telecommunication services or utilities sectors.

**About Risk**

*Equity securities* are volatile and can decline significantly in response to broad market and economic conditions. *Foreign and emerging market securities* may be subject to greater political, economic, environmental, credit, currency and information risks. Foreign securities may be subject to higher volatility than US securities due to varying degrees of regulation and limited liquidity. These risks are magnified in emerging markets. *Investments in small and mid-size companies* can be more volatile than those of larger companies. *Growth stocks* may be more sensitive to market conditions than other equities as their prices strongly reflect future expectations. *Currency* exchange rates between the US dollar and foreign currencies may cause the value of the fund’s investments to decline.

**Russell 1000® Growth Index** measures the performance of the large cap growth segment of the US equity universe. It includes those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values. The Russell 1000 Growth Index is constructed to provide a comprehensive and unbiased barometer for the large cap growth segment. Indexes are unmanaged and do not incur fees. It is not possible to invest directly in an index. 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.

Outlook as presented in this material reflects subjective judgments and assumptions of the portfolio team and does not necessarily reflect the views of Loomis, Sayles & Company, L.P. There is no assurance that developments will transpire as stated. Opinions expressed will evolve as future events unfold.

**Before investing, consider the fund’s investment objectives, risks, charges, and expenses. Please visit www.loomissayles.com or call 800-225-5478 for a prospectus and a summary prospectus, if available, containing this and other information. Read it carefully.**

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