

DEAR BARON OPPORTUNITY FUND SHAREHOLDER:

PERFORMANCE

Baron Opportunity Fund had a solid second quarter, and as of the date of this letter is up over 20% on the year. During the second quarter, the Fund gained 4.30%, beating both the Russell Midcap Growth Index, which rose 2.87% and the S&P 500 Index, which increased 2.91%.

Table I.
Performance (Retail Shares)[†]
Annualized for periods ended June 30, 2013

	Baron Opportunity Fund ^{1,2}	Russell Midcap Growth Index ¹	S&P 500 Index ¹
Three Months ³	4.30%	2.87%	2.91%
Six Months ³	13.51%	14.70%	13.82%
One Year	18.48%	22.88%	20.60%
Three Years	16.46%	19.53%	18.45%
Five Years	8.87%	7.61%	7.01%
Ten Years	11.83%	9.94%	7.30%
Since Inception (February 29, 2000)	4.31%	1.96%	3.16%

REVIEW & OUTLOOK

After a very strong first quarter for U.S. stock markets, the second quarter yielded more modest gains. The quarter played out like a tale of two cities. From the start of the period through May 21, the market steadily advanced. But, the next day, Federal Reserve Chairman Bernanke told the market that the economy was continuing to improve from the recession and the release of the Fed minutes that same day led many market participants to conclude that the Fed would begin to taper its bond purchase program (QE) sooner than expected. On June 19th, Chairman Bernanke testified before Congress that the pace of QE could be reduced later this year and that all purchases might conclude by mid-2014. These two events prompted the market to give back about half the gains it had achieved over the first part of the quarter. We think it is critical to note that Chairman Bernanke emphasized the timeline for gradually exiting QE was conditioned upon developments

Performance listed in the above table is net of annual operating expenses. Annual expense ratio for the Retail Shares as of September 30, 2012 was 1.39%. 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 has reimbursed certain Fund expenses (by contract as long as BAMCO, Inc. is the adviser to the Fund) 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.

[†] If the Fund's historical performance was impacted by gains from IPOs and/or secondary offerings, there is no guarantee that these results can be repeated or that the Fund's level of participation in IPOs and secondary offerings will be the same in the future.

¹ The indexes are unmanaged. 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. The indexes and the Fund are with dividends, which positively impact the performance results.

² The performance data in the table does not reflect the deduction of taxes that a shareholder would pay on Fund distributions or redemption of Fund shares.

³ Not annualized.



MICHAEL A. LIPPERT
PORTFOLIO MANAGER

Retail Shares: BIOPX
Institutional Shares: BIOIX

in the economic outlook and that the pace of QE could even go back up if economic conditions were to weaken. In other words, the training wheels would be removed gradually only if the economy shows it can continue riding on its own.

We believe equity markets initially overreacted to the Fed's plan (and we note the third quarter is off to a healthy start). Economic conditions in the U.S. are slowly but steadily improving, particularly in housing, and corporate balance sheets are flush with cash. While the market will need to transition from relying on the Fed's support to relying on economic fundamentals and corporate profit growth, we think the foundation for each continues to build.

As reflected above, the Baron Opportunity Fund had a solid quarter. This was so even though Information Technology stocks continued to lag the broader market. The Fund's Industrial investments performed very well during the period, led by **The ExOne Company** (up 86%), a pioneer in additive (or 3D) manufacturing, and **Ryanair Holdings plc** (up 23%), Europe's disruptive low-cost airline. The Fund's Consumer Discretionary holdings also performed well. Top performers included online personal publishing leader, **Shutterfly, Inc.** (up 26%); electric car pioneer, **Tesla Motors Inc.** (up 128%); online travel agency, **priceline.com Inc.** (up 20%); and **Liberty Media Corp.** (up 13%), whose value is predominantly driven by the performance of satellite radio leader, Sirius XM Radio. Our Materials investments – **Berry Plastics Group, Inc.** (up 17%), innovator in plastic food closures and drinking cups; and **CaesarStone Sdot-Yam Ltd.** (up 17%), quartz countertop manufacturer – also contributed to performance.

Regarding Information Technology and our investments in that sector, as I wrote last quarter, the annual re-setting of IT budgets and global macro-economic concerns caused first quarter business IT spending to come in weaker than expected. While this had a short-term negative impact on the performance of the Fund, we did not make any major changes to the portfolio. Based on our long experience investing across the technology space (since the Fund's inception), we know that enterprise tech spending can be somewhat lumpy, particularly in the first quarter of the year, after the year-end budget flush and when budget



Baron Opportunity Fund

priorities for the current year are being set. Our experience tells us that now would be a particularly poor time to reduce our IT exposure. More importantly, we believe there is a dichotomy taking place in IT caused by a generational shift from old technologies to new technologies. Old technologies, like PC's and on-premise software, are ceding share and struggling for growth. At the same time, many of the new technologies, headlined by cloud computing, big data and mobility, are still on the early slopes of their adoption curves. As a result, in our view, the IT world finds itself temporarily in the valley between the adoption curves of these two technology paradigms. This has led to a transitional period of slower overall growth rates, investor confusion and lower multiples accorded to enterprise IT stocks.

As we have discussed in previous letters, our IT investments are either focused on these newer enterprise technologies, or on Internet and (what we call) information services. Indeed, several of our IT investments achieved double-digit returns during the quarter, including **Tableau Software, Inc.** (up 79%), an emerging big data analytics provider; **Angie's List, Inc.** (up 33%), a leading provider of Internet information, content and e-commerce solutions in the home services space; **Shutterstock, Inc.** (up 25%), operator of a global online marketplace for commercial digital imagery and video; **CoStar Group, Inc.** (up 18%), the leading provider of commercial real estate information and analytics solutions; **Axiom Corp.** (up 11%), a provider of digital marketing solutions; **Imperva, Inc.** (up 17%), a provider of security solutions for web applications and databases; and **FactSet Research Systems, Inc.** (up 11%), a provider of online information and analytics to the financial services industry. In addition, we took advantage of weakness among many enterprise IT stocks to add to our positions in **Citrix Systems, Inc.** and **Red Hat, Inc.**

We believe the investment strategy for the Fund remains consistent and compelling. We invest in higher growth, often innovative, businesses that are benefitting from powerful secular growth themes. The Fund's investments, in the aggregate, are growing their top lines at about twice the rate as the companies that make up the Russell Midcap Growth Index. Our investments also tend to have higher free cash flow margins (the percentage of each dollar of sales left over after deducting for cash operating expenses, cash interest, cash taxes, working capital changes and capital expenditures) and thus faster free cash flow growth than the average benchmark company. We sometimes pay higher multiples for these faster-growing businesses, and we accept slightly more volatility than the Index, but we believe over time our strategy will yield higher risk-adjusted returns for our investors than an investment in the passive benchmark.

Table II.
Top contributors to performance for the quarter ended June 30, 2013

	Percent Impact
The ExOne Company	0.98%
Illumina, Inc.	0.95
Tesla Motors, Inc.	0.69
Tableau Software, Inc.	0.60
Angie's List, Inc.	0.56

The ExOne Company, a leading innovator in the additive manufacturing (or 3D printing) space, had a successful IPO during the first quarter and was the Fund's top contributor during the second quarter. Different from the other public 3D printing companies, ExOne's systems produce metal parts or casts that are used in actual finished parts or equipment, not mere plastic proto-types. The company has seen significant customer demand for its commercial 3D printing machines and is executing on its strategy of using both machine sales and service offerings to grow revenues by over 40% per year. (Randy Gwartzman)

Shares of **Illumina, Inc.** outperformed during the second quarter. Illumina is the leading provider of next generation DNA sequencing instruments and consumables. In April, the company reported strong first quarter results. Revenues increased 21%, ahead of Wall Street estimates, driven by strength across the entire product portfolio. Earnings also exceeded expectations. We think Illumina's strong first quarter results were driven in part by market share gains, which may have accelerated after the company's main competitor announced it was evaluating strategic alternatives. (Neal Kaufman)

Tesla Motors, Inc. showed significant price appreciation during the second quarter as it continued to execute on its innovative electric vehicle (EV) business model in a nearly flawless manner. The company delivered its first profitable quarter, although we note that all of its profits came from sales of non-recurring regulatory zero-emission credits. More importantly, it appears the company is on track to achieve its 2013 goals for production and deliveries of its Model S premium EV sedan, as well as automotive gross margins. Management has also expressed confidence in reaching its longer-term goal of producing a smaller, more mainstream (less expensive) EV sedan within a few years. We sold the remainder of our Tesla shares during the quarter after the stock almost tripled against our average cost base, though in 20/20 hindsight our sale may have been too hasty as the stock has continued to work higher. We remain big fans of Elon Musk and Tesla, and plan to stay close to this pioneering company with an eye towards re-investing at a more attractive level. (Randy Gwartzman)

Tableau Software, Inc., a recent IPO, was a strong contributor to performance during the second quarter. Tableau offers proprietary data discovery and visualization tools that help business users analyze and derive insights from business data. Unlike traditional business intelligence platforms, Tableau is intuitive to use, fast to deploy, and can be configured without involving the IT department. We estimate that Tableau serves a market that is in excess of \$20 billion annually, or more than 100 times larger than the company's current revenue base, leaving a long runway for growth. (Neal Rosenberg)

Angie's List, Inc. is the leading online site where consumers can find quality local service providers for home repairs and services, accessing reviews from over a million subscribing members. Shares of Angie's List performed well during the second quarter, as the company delivered strong first quarter results with expectations for improving profit margins in the second half of 2013. (Ashim Mehra)

Table III.
Top detractors from performance for the quarter ended June 30, 2013

	Percent Impact
CARBO Ceramics, Inc.	-0.53%
Equinix, Inc.	-0.47
Fortinet, Inc.	-0.45
LivePerson, Inc.	-0.44
Radware Ltd.	-0.44

CARBO Ceramics, Inc. is the largest provider of ceramic proppants to the global oil and gas industry. Ceramic proppants are a key material in the hydraulic fracturing process, however, demand and pricing for these proppants has been hurt by a combination of reduced natural gas drilling and increased foreign competition. Competitive pressures appear to be easing and CARBO's volumes and cost pressures appear to be stabilizing, so we think volumes and margins should improve in the second half of the year. Nevertheless, reduced earnings expectations hurt the shares in the second quarter. (Jamie Stone)

Equinix, Inc. operates a global network of highly interconnected data centers that enable its customers to connect to business partners, network

providers, cloud service providers and critical eco-systems, such as financial exchanges. Equinix's shares pulled back during the quarter principally around concerns about its REIT conversion plans and REIT valuation pressure, as long-term interest rates rose sharply during the period. We continue to believe that Equinix has a differentiated business model with high barriers to entry and exit, that there is strong precedent supporting its REIT conversion, and that the business is attractively valued given the strong cash flows generated by its existing base of data centers. (Gilad Shany)

Fortinet, Inc. is a leading provider of network security solutions to service providers and enterprises. Like many other IT vendors with exposure to service providers, Fortinet missed its own first quarter guidance and the stock gave back all of its beginning-of-the-year gains. We continue to see security as a top priority for business executives, as threats are becoming more pervasive and more complex. We believe Fortinet's differentiated solutions will gain share and that its growth rates will re-accelerate. (Gilad Shany)

LivePerson, Inc. provides online engagement solutions (e.g., chat, marketing campaigns) and analytics. LivePerson's stock pulled back following first quarter results that missed management's expectations due to several enterprise customers cancelling the service. While we had been patient with the company's challenging transition from single product (chat) company to an engagement platform provider, we decided to exit our position as the large customer cancellations were inconsistent with our investment thesis. (Gilad Shany)

Radware Ltd. manufactures integrated networking solutions for application performance optimization and security. Like Fortinet, Radware's stock fell after the company missed its first quarter guidance, due primarily to weak service provider sales in Europe. At the same time, Radware's U.S. business remained quite healthy and delivered strong growth rates. We continue to believe that Radware will continue to take share in the U.S. market with its differentiated application delivery and security solutions. (Gilad Shany)

PORTFOLIO STRUCTURE

Baron Opportunity Fund had \$404.2 million of assets under management as of June 30, 2013. The Fund had investments in 61 securities, including two private-equity investments. The top 10 positions accounted for 31.1% of the portfolio. The Fund's cash position was 0.7% at quarter end. The median market cap of the Fund was \$3.0 billion at the end of the quarter. Our research continues to generate many good ideas for the Fund, and we maintained very low cash levels throughout the quarter.

Table IV.

Top 10 holdings as of June 30, 2013

	Quarter End Investment Value (millions)	Quarter End Market Cap (billions)	Percent of Net Assets
Illumina, Inc.	\$16.4	\$9.3	4.1%
Gartner, Inc.	15.9	5.3	3.9
Liberty Media Corp.	14.4	15.3	3.6
Guidewire Software, Inc.	12.9	2.4	3.2
Verisk Analytics, Inc.	11.8	10.1	2.9
IHS, Inc.	11.5	6.9	2.9
Acxiom Corp.	11.2	1.7	2.8
SBA Communications Corp.	11.1	9.5	2.7
Citrix Systems, Inc.	10.2	11.3	2.5
Discovery Communications, Inc.	10.1	18.2	2.5

As described above, we focus on investing the Fund's assets in themes and individual businesses that we believe will experience significant secular growth rates. As a result, the Fund's sector weights are an output of our process, not an input. Not surprising, most of our investments are in those industry sectors more typically associated with growth. At quarter end, about 60% of the portfolio was invested in the Consumer Discretionary and Information Technology sectors. We also have meaningful investments across the Energy, Industrials and Health Care sectors. In thinking about diversification, we pay little attention to sector weights as defined by GICS, instead focusing on the fundamental business drivers and end market exposures for our investments.

RECENT ACTIVITY

Table V.

Top net purchases for the quarter ended June 30, 2013

	Quarter End Market Cap (billions)	Amount (millions)
Liberty Media Corp.	\$15.3	\$7.2
CaesarStone Sdot-Yam Ltd.	0.9	4.6
Illumina, Inc.	9.3	4.6
CME Group, Inc.	25.4	4.4
DigitalGlobe, Inc.	2.3	4.3

We increased our investment in **Liberty Media Corp.**, a media-focused holding company led by cable and media pioneer John Malone. Liberty's key asset is Sirius XM Satellite Radio, which continues to generate significant growth in subscribers and free cash flow. We believe Liberty is undervalued given its ownership stake in Sirius, as well as Charter Communications, a cable company with a new but experienced management team.

CaesarStone Sdot-Yam Ltd. is a leading manufacturer of high-quality engineered quartz surfaces. Within the \$30 billion global countertop industry, quartz is taking share from other materials (e.g., laminate, granite, marble) because of its non-porous characteristics that offer superior scratch, stain and heat resistance versus competing products, as well as a wider array of design options. CaesarStone has a proven history of entering new markets and driving quartz penetration and taking market share. For example, in Israel, CaesarStone introduced quartz in 1987 and by 2010 drove penetration of quartz to 82% and captured 89% of the market; in Australia, CaesarStone entered the market in 1998 and by 2010 achieved 32% penetration and 59% market share. The \$6 billion U.S. countertop market, with only 5% quartz penetration, is the next big opportunity for the company. With opportunities in the U.S. and other global markets, we think CaesarStone can double its revenues over the next five years.

During the quarter, we significantly increased our investment in DNA sequencing leader **Illumina, Inc.**, making it the largest position in the portfolio at the end of the quarter. We have become increasingly confident about Illumina's opportunities in its applied markets, particularly the health care diagnostics market. By way of example, we believe the newborn screening market could be a \$350 million revenue opportunity, and the cancer market could be at least another \$250 million revenue opportunity.

We re-established an investment in **CME Group, Inc.** during the period. CME is the largest and most diversified derivatives marketplace in the U.S. Its exchanges support trading across a variety of asset classes, including interest rates, equity indexes, energy, agricultural commodities, foreign exchange and metals. We believe CME has the opportunity to significantly accelerate its growth rates due to the eventual normalization of interest rates and the attendant interest rate volatility. CME's interest rate trading volumes (ADV) have been depressed as a result of the Fed's zero interest rate policy and low interest rate volatility. For example, interest rate ADV was 4.8 million in 2012

Baron Opportunity Fund

compared to 7.1 million in 2007, before the financial crisis. However, given the Fed's recent policy statements (discussed above), market participants are starting to anticipate an end to quantitative easing (QE). On May 30, CME experienced record volume for interest rate derivatives with ADV of 19.4 million. With the globalization of CME's business, a host of new products, and the regulatory requirement for interest rate swaps to be cleared on an exchange, we believe CME's interest rate volumes can surpass their prior peak, significantly driving earnings growth for the company.

This year we initiated and have continued to build a position in **DigitalGlobe, Inc.**, the leading provider of satellite-based high resolution imagery. First, DGI is now led by CEO Jeff Tarr, an executive we got to know well while he was COO at IHS, a top information services company and another Opportunity Fund investment. Second, the merger of DGI and its closest competitor, GeoEye, has created a much better company in our view. The merger combined the two leading U.S. satellite imagery companies and consolidated a large U.S. government contract with one company. The merger not only vastly improves the competitive environment in our view, but synergies are expected to be significant, at around \$1.8 billion. Moreover, because the combined company has nearly completed its next-generation satellite builds and launches, we believe free cash flow will inflect and reach significant levels. Lastly, we believe in CEO Tarr's strategy of diversifying DGI beyond its defense and intelligence base of business and pursuing the vast commercial imagery opportunity with an information services business model.

Table VI.
Top net sales for the quarter ended June 30, 2013

	Market Cap When Sold (billions)	Amount (millions)
CBRE Group, Inc.	\$8.3	\$-8.7
Tesla Motors, Inc.	10.1	-6.7
Starwood Hotels & Resorts Worldwide, Inc.	13.2	-6.2
Artisan Partners Asset Management, Inc.	3.1	-5.6
Blue Nile, Inc.	0.4	-5.2

We decided to exit **CBRE Group, Inc.**, **Starwood Hotels & Resorts Worldwide, Inc.**, and **Artisan Partners Management, Inc.**, all solid businesses, to further focus the portfolio on higher-growth, more innovative businesses, such as some of the ones discussed above.

We discussed our sale of **Tesla Motors, Inc.** above. This was principally a valuation call, as the company's valuation started to incorporate not only success with its current EV, the Model S, but also a next-generation vehicle that is still on the drawing board and not even slated to be released until 2017 at the earliest. As I stated above, in 20/20 hindsight our sale may have been a bit too hasty, as the stock has continued to work higher. We remain believers and supporters of Tesla, its mission, and its visionary leader, Elon Musk. We plan to follow the company closely and may look to reinvest if we get a more attractive valuation level.

After being involved with the company for a long time, we decided to exit our **Blue Nile, Inc.** investment during the quarter. The main reason was that our research led us to dial down our expectations for the company's long-term growth rate and cash flow generation potential. In addition, we saw better opportunities in other Internet-based media and commerce businesses.

Thank you for your support and for trusting us with your assets. We look forward to updating you in future letters.

Sincerely,

Michael A. Lippert
Portfolio Manager
July 23, 2013

For more information about this Fund please scan this QR code with any bar code reader on your mobile device.



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The Adviser believes that there is more potential for capital appreciation in securities of high growth businesses benefiting from innovation through development of pioneering, transformative or technologically advanced products or services, but there also is more risk. Companies propelled by innovation, including technological advances and new business models, may present the risk of rapid change and product obsolescence and their successes may be difficult to predict for the long term. Securities issued by medium sized companies may be thinly traded and may be more difficult to sell during market downturns. The Fund may not achieve its objectives. Portfolio holdings are subject to change. Current and future portfolio holdings are subject to risk.

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