

Baron Opportunity Fund

DEAR BARON OPPORTUNITY FUND SHAREHOLDER:

PERFORMANCE

Baron Opportunity Fund lagged the strong broader market to start the year. The Fund gained 8.83% for the quarter, trailing the Russell Midcap Growth Index, which rose 11.51% and the S&P 500 Index, which increased 10.61%.

Table I.
Performance (Retail Shares)[†]
Annualized for periods ended March 31, 2013

	Baron Opportunity Fund ^{1,2}	Russell Midcap Growth Index ¹	S&P 500 Index ¹
Three Months ³	8.83%	11.51%	10.61%
One Year	5.86%	12.76%	13.96%
Three Years	11.63%	14.23%	12.67%
Five Years	8.57%	7.98%	5.81%
Ten Years	14.48%	11.53%	8.53%
Since Inception (February 29, 2000)	4.06%	1.78%	2.99%

REVIEW & OUTLOOK

The stock market opened the year with a very strong first quarter. The market cheered the New Year's Eve compromise averting the fiscal cliff, and the rally continued spurred on by the Fed's easy money policy, a gradually improving U.S. economy, better-than-feared fourth quarter earnings and strong money flows into U.S. equity markets, among other things.

As reflected above, the Baron Opportunity Fund did not keep pace with the broader market. The primary reasons for this were two-fold. First, the Fund's health care investments did not perform well during the period. Amounting to just under 9% of the portfolio, the Fund's health care stocks declined about 2.5% in the aggregate. Long-term holdings **Edwards Lifesciences Corp.**, **Intuitive Surgical, Inc.**, **Illumina, Inc.** and **Masimo Corp.** each fell between 2 and 9%. While we decided to exit our Intuitive Surgical position (addressed below), neither the short-term trading in these stocks nor anything we learned during the quarter altered our opinion that minimally-invasive surgical procedures and better diagnostics (including DNA-based

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

testing) will remain important secular growth trends in the health care space.

Second, the Fund's significant weighting of Information Technology and Telecommunication Services stocks acted as a drag on performance during the quarter. These two sectors lagged the broader market during the period. Amid the annual re-setting of IT budgets and global macro-economic concerns (the "fiscal cliff," sequester, Cyprus, etc.), first quarter IT spending looks to have come in weaker than expected. To be sure, a number of well-known tech companies have reported or pre-announced poor results to start the year, including Oracle, Tibco, Red Hat, F5, Radware, Compuware and Fortinet. While this has had a short-term negative impact on the performance of the Fund, we are not making any major changes to the portfolio. We have been investing across the broader technology space for more than 13 years (i.e., since the Fund's inception) and have seen this play before. Tech spending can be somewhat lumpy, particularly in the first quarter of the year, after the year-end budget flush and when budget 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. Selling at a cyclical low is anathema for secular investors, like us. More importantly, we remain confident that the technology themes in which we are investing are intact, that these themes will drive outsized growth, and that our portfolio companies are not only benefitting from these growth themes, but are taking market share within them. In fact, we have taken advantage of the broad weakness in tech stocks to selectively add to certain positions in the portfolio. At the same time, a number of our best performers during the period were IT investments, including **Guidewire Software, Inc.** (up 29%), **Gartner, Inc.** (up 18%), **ANSYS, Inc.** (up 21%), **CoStar Group, Inc.** (up 22%) and **Acxiom Corp.** (up 17%).

Aside from the companies just mentioned, other top contributors for the quarter included our Consumer Discretionary investments – led by e-commerce leaders **HomeAway, Inc.** (up 48%), **Shutterfly, Inc.** (up 48%) and **Shutterstock, Inc.** (up 40%) – and our Financial Services investments – led by **CBRE Group, Inc.** (up 27%).



BARON
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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. While we strive to outperform in every period, we acknowledge that the market doesn't work that way, and that periods of underperformance are unavoidable. We attempt to use those periods to improve the portfolio by taking advantage of compelling opportunities when they present themselves. We believe the best approach to long-term investing is to pursue a consistent and proven strategy, making tactical adjustments when necessary. That is how we operate. We continue to focus on identifying businesses with powerful secular growth drivers, predictable and/or recurring revenue streams, sustainable competitive advantages, strong balance sheets, and positive operating cash flows, and that sell products and services that will remain in high demand and critical to customers.

Table II.
Top contributors to performance for the quarter ended March 31, 2013

	Percent Impact
HomeAway, Inc.	0.95%
Shutterfly, Inc.	0.80
Guidewire Software, Inc.	0.79
The ExOne Company	0.70
Gartner, Inc.	0.68

HomeAway, Inc. was up 47.7% in the first quarter. HomeAway is the leading global provider of online vacation rental accommodations, with over 700,000 paid listings. You can think of HomeAway to vacation rental properties as Expedia or Priceline is to hotels. HomeAway's first quarter performance was driven by its strong fourth quarter results, where the company beat Street expectations and demonstrated accelerating growth in its closely tracked revenue-per-listing metric. (Catherine Chen)

Shutterfly, Inc. is the leading provider of personalized photo-based products. Shares of Shutterfly were up 47.9% in the first quarter on the back of strong fourth quarter results and an equally optimistic outlook for 2013. The company gained market share from its competitors and expanded operating margins, as its new manufacturing facilities ramped up. The company is also making significant progress in its enterprise printing business. (Ashim Mehra)

Shares of **Guidewire Software, Inc.**, a leading provider of core systems software to the global P&C insurance industry, outperformed during the first quarter after reporting significantly better-than-expected financial results. We believe that Guidewire is emerging as the gold standard in terms of P&C core systems functionality, as evidenced by its near perfect retention rates, growing installed base, and the accelerating adoption of its complete suite of offerings. (Neal Rosenberg)

The ExOne Company had a successful IPO and was a contributor in the period. The company has significant customer demand for its commercial 3-D printing equipment and is executing on its strategy of using both machine sales and service offerings to grow revenues by over 40% per year. (Randy Gwirtzman)

Shares of **Gartner, Inc.**, the leading independent provider of research and analysis on the Information Technology industry, outperformed during the period, driven by solid financial results among uneven IT end markets (as discussed above). The company continued to generate record bookings in its research business, with contract value trending up 14%. The business generates significant free cash flow, and Gartner has been a steady purchaser of its own shares. (Neal Rosenberg)

Table III.
Top detractors from performance for the quarter ended March 31, 2013

	Percent Impact
Agrinos AS	-0.63%
Liquidity Services, Inc.	-0.53%
Polypore International, Inc.	-0.43%
Rackspace Hosting, Inc.	-0.36%
lululemon athletica, Inc.	-0.31%

Agrinos AS declined 46.3% during the first quarter. Agrinos is a green technology company, whose unique microbial product significantly enhances yields across a broad array of crops. The shares were weak in the first quarter after the company disclosed that a delay in receivables collection led to management's decision to change its revenue recognition policies, resulting in no revenue being booked in the fourth quarter for its Mexican business. We continue to hold Agrinos because we believe it has disruptive technology (agri-giant Syngenta made an investment in the company last year and is partnering to offer Agrinos' products to its customers in certain regions) and exciting long-term growth prospects. We believe management is taking a conservative stance regarding revenue recognition in Mexico, and we note that the company has historically had low levels of write-offs related to its Mexican receivables. (Catherine Chen)

Liquidity Services, Inc. brings efficiencies through online auctions to a large, but fragmented, reverse supply chain industry consisting of returns, damaged goods and capital asset sales. Shares of Liquidity Services were down significantly during the period. The company reduced its outlook for 2013, after having just lowered expectations for the fourth quarter. We decided to sell our shares (predominantly to fund other investments). (Ashim Mehra)

Shares of **Polypore International, Inc.** partially retreated from their strong fourth quarter run up of 31.5%. Although its lead-acid battery separator business (about 50% of revenues) did well in the fourth quarter, sales of separators for lithium-ion (LiON) batteries were lower than expected for both consumer and vehicle applications. We believe the revenue decline associated with LiON battery separators has troughed, and with its capacity expansion, the company should see significant upside earnings leverage as electric vehicles gain penetration. We continue to believe that Polypore's shares are undervalued and its multiple will increase once end-market growth resumes. (Randy Gwirtzman)

Baron Opportunity Fund

Rackspace Hosting, Inc. is a leading hosting and cloud computing service provider. During the quarter, Rackspace completed the transition of its infrastructure to “Open Stack,” an open-source cloud orchestration project initiated by Rackspace and NASA. This transition impacted core business growth, causing Rackspace to miss revenue expectations. We have high regard for the Rackspace management team, but decided to exit our position as we continue to assess Rackspace’s competitive positioning in the rapidly evolving cloud computing service provider space. (Gilad Shany)

lululemon athletica, Inc., a manufacturer and retailer of yoga inspired apparel, was a detractor for the period. The company had some quality issues with its Luon fabric, which is used in many of its yoga pants. As a result, the company is short of product and expects to be impacted financially. We do not believe this is a long-term issue, and we think the company can rectify the issue by the end of the second quarter. We still believe lululemon possesses a great brand, strong customer loyalty and significant store expansion opportunities in the U.S. and overseas. (Laird Beiger)

PORTFOLIO STRUCTURE

Baron Opportunity Fund had \$401.6 million of assets under management as of March 31, 2013. The Fund had investments in 61 securities, including two private-equity investments. The top 10 positions accounted for 30.2% of the portfolio. The Fund’s cash position was 0.4% at quarter end. The median market cap of the Fund was \$3.0 billion at the end of the quarter. We believe our research continues to generate many good ideas for the Fund.

Table IV.
Top 10 holdings as of March 31, 2013

	Quarter End Investment Value (millions)	Quarter End Market Cap (billions)	Percent of Net Assets
Gartner, Inc.	\$16.9	\$5.1	4.2%
Verisk Analytics, Inc.	14.3	10.4	3.6
Guidewire Software, Inc.	13.1	2.2	3.3
ANSYS, Inc.	12.8	7.6	3.2
Equinix, Inc.	12.1	10.6	3.0
RealPage, Inc.	11.1	1.6	2.8
HomeAway, Inc.	11.0	2.7	2.7
Discovery Communications, Inc.	10.3	18.5	2.6
SBA Communications Corp.	10.3	9.1	2.6
CBRE Group, Inc.	9.0	8.3	2.2

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.

To illustrate, we have significant investments in a class of companies we refer to as information services businesses. These include **Gartner, Inc.** and **Verisk Analytics, Inc.**, our two largest investments, as well as **IHS, Inc.**, **CoStar Group, Inc.**, **FactSet Research Systems, Inc.** and **DigitalGlobe, Inc.** Together, these investments currently account for about 15% of the portfolio. While all of these businesses have similar characteristics that we

find attractive, they each have different end market exposures: Gartner – Information Technology; Verisk Analytics – Property and Casualty Insurance, Health Care and Financial Services; IHS – Energy and Industrials; CoStar – Commercial Real Estate; FactSet – Asset Managers and Investment Banks; DigitalGlobe – Government, Defense and Internet. GICS lacks an “information services” category, placing some of these companies in the IT sector and others in Industrials.

Information services business all start with a highly valuable proprietary asset, such as a unique data set or an unparalleled team of analysts, and then build robust analytical tools that help end users extract, manipulate, and apply the underlying data to everyday business problems. The proprietary information and accompanying analytical tools eventually become a critical part of the end users’ day-to-day workflow, creating a sticky business model with high levels of recurring revenue (usually above 80%). Since these businesses only have to invest “once” in collecting the data and building the analytical tools but can sell them “many” times, these businesses tend to have high operating leverage, as each sale of a new subscription carries high incremental margins. Finally, thanks to annual contracts that are largely paid in cash up front, these businesses typically generate significant levels of free cash flow.

RECENT ACTIVITY

Table V.
Top net purchases for the quarter ended March 31, 2013

	Quarter End Market Cap (billions)	Amount (millions)
Fortinet, Inc.	\$3.8	\$6.4
Tesoro Logistics LP	2.5	5.8
Radware Ltd.	0.8	5.8
Shutterstock, Inc.	1.6	5.0
Xoom Corp.	0.7	4.8

During the quarter, we added to our holdings in the network security space, with investments in **Fortinet, Inc.** and **Radware Ltd.** Securing customer and business data has become a leading priority for CIOs, as more and more applications are Internet enabled and as the nature of the threat has changed from teenage hackers to attacks involving organized crime, state sponsored terrorists and foreign militaries. Cyber-attacks are making the front pages of national newspapers and President Obama has made improving cyber-security a national priority. Radware, in addition to being a strong player in the application delivery market, is a leader in protecting against the growing threat of distributed denial of service (DDoS) attacks. Fortinet is the leader in the Unified Threat Management market and gaining share with its higher-throughput Next Generation Firewalls. Our timing in initiating these positions was not optimal, as both companies have since pre-announced weaker-than-expected first quarters. We believe this weakness is short term and due primarily to macro factors. We continue to believe both companies are share gainers in the critical network security space.

Tesoro Logistics LP is a master limited partnership (MLP) that owns, operates, develops and acquires crude oil and refined products logistics assets. The company owns a crude oil gathering system, refined products terminals, storage facilities and short haul pipelines. These logistics assets are integral to the success of parent-company Tesoro Corporation’s refining and marketing operations. Tesoro Logistics has long-term contracted cash flows (10 years) with little commodity exposure, a supportive parent that understands the value of MLP for capital formation, and a strong inventory of potential accretive acquisitions/drops that we think will continue to drive its growth in the future.

Shutterstock, Inc. is the leading online provider of royalty-free stock photography and film clips. The company offers over 25 million images from artists worldwide from whom they license content. Shutterstock differs from its legacy competitors in that its business is 100% online and it sells its images at dramatically lower prices (\$2-3/image) with significantly greater flexibility in how buyers can use the images. Another competitive advantage is search – finding the right picture – as matching keywords to images is a complex, big data problem. We believe Shutterstock is disrupting and gaining share in the \$4-5 billion stock photography market.

Xoom Corp. is a leading online consumer-to-consumer international money transfer company, which offers safe and secure money sending options from the convenience of a computer or mobile phone to family and friends at any time, from any Internet-enabled location. XOOM has the opportunity to become the online disrupter of the global money transfer market. Existing legacy players (The Western Union Company, MoneyGram International, Inc.) have to put expensive physical networks in place and hire additional agents to scale up, while new entrants lack the regulatory approvals, digital network and risk management systems. We believe XOOM has the potential to triple its revenue over the next 5-6 years and think that with its lean digital business model, it should be a highly profitable and cash generative business.

Table VI.
Top net sales for the quarter ended March 31, 2013

	Quarter End Market Cap or Market Cap When Sold (billions)	Amount (millions)
Rackspace Hosting, Inc.	\$7.5	\$-8.4
Cytec Industries, Inc.	3.2	-7.4
MICROS Systems, Inc.	3.3	-7.1
SBA Communications Corp.	9.1	-6.8
Intuitive Surgical, Inc.	18.5	-6.1

We sold **Rackspace Hosting, Inc.** for the reasons described above. We continue to follow the company closely and, depending on our research findings, may choose to re-invest at some point in the future.

After making a solid return, we sold **Cytec Industries, Inc.** to fund another investment we thought was a better use of capital.

We sold **MICROS Systems, Inc.** to fund investments in other Information Technology companies that we thought offered higher growth rates and better long-term returns.

We trimmed our position in **SBA Communications Corp.**, one of the best investments in the history of the Fund. SBA remains a Top 10 position.

We decided to exit our **Intuitive Surgical, Inc.** investment due to concerns about the impact that increased focus on cost containment in the health care system might have on the company's long-term growth prospects.

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
April 9, 2013

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



Investors should consider the investment objectives, risks, and charges and expenses of the investment carefully before investing. The Baron Family of Funds is described in prospectuses which contain this and other information about the Funds. You should carefully read the prospectus before investing. You can obtain a copy of the prospectus by contacting the Funds' distributor, Baron Capital, Inc., at 767 Fifth Avenue, New York, New York, 10153, or by calling 1-800-99BARON, or by going to our website at www.BaronFunds.com.

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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