Dear Baron Real Estate Fund Shareholder:

Performance

Following a remarkably stable and rising stock market environment in 2017–a year in which, for the first time, the S&P 500 Index generated positive total returns in every month of the year (based on data going back to 1928)–the first quarter of 2018 was notable for its volatility.

This year's first quarter performance was fueled in part by interest rate, inflation, and geopolitical concerns, and, surprisingly, numerous twitter announcements! The S&P 500 Index increased by as much as 7.6% in January, only to decline by 10% from its January peak through early February, then rebounded by approximately 8% through early March, and declined, once again, for the balance of March. The sum total for the S&P 500 Index was a quarterly decline of 0.76%.

In the first three months of 2018, REITs and certain real estate-related stocks declined more than the broader market largely due to concerns about higher interest rates.

Table I.
Performance
Annualized for periods ended March 31, 2018

	Baron Real Estate Fund Retail Shares[1,2]	Baron Real Estate Fund Institutional Shares[1,2]	MSCI USA IMI Extended Real Estate Index[1]	MSCI US REIT Index[1]	S&P 500 Index[1]
Three Months[3]	(5.44)%	(5.40)%	(5.28)%	(8.39)%	(0.76)%
One Year	15.11%	15.40%	5.76%	(5.60)%	13.99%
Three Years	3.47%	3.75%	5.59%	(0.43)%	10.78%
Five Years	8.68%	8.97%	9.15%	4.53%	13.31%
Since Inception (December 31, 2009) (Annualized)	14.78%	15.07%	12.57%	9.65%	13.37%
Since Inception (December 31, 2009) (Cumulative)[3]	211.80%	218.29%	165.63%	113.83%	181.53%

JEFFREY KOLITCH
PORTFOLIO MANAGER

Retail Shares: BREFX
Institutional Shares: BREIX
R6 Shares: BREUX

In the first quarter ended March 31, 2018, the Baron Real Estate Fund (the "Fund") declined 5.40% (Institutional Shares) largely in-line with its primary benchmark index, the MSCI USA IMI Extended Real Estate Index (the "MSCI Real Estate Index"), which declined 5.28%. The Fund outperformed the MSCI US REIT Index, which declined 8.39%.

Since the Fund's inception on December 31, 2009, the Fund's average annual return of 15.07% (Institutional Shares) has outperformed the average annual return of the MSCI Real Estate Index (12.57%), the MSCI US REIT Index (9.65%), and the S&P 500 Index (13.37%).

Performance listed in the above table is net of annual operating expenses. Annual expense ratio for the Retail Shares and Institutional Shares as of December 31, 2017 was 1.32% and 1.06%, respectively. 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.*

1 The indexes are unmanaged. The MSCI USA IMI Extended Real Estate Index is a custom index calculated by MSCI for, and as requested by, BAMCO, Inc. The index includes real estate and real estate-related GICS classification securities. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indexes or any securities or financial products. This report is not approved, reviewed or produced by MSCI. The MSCI US REIT Index is a free float-adjusted market capitalization index that measures the performance of all equity REITs in the US equity market, except for specialty equity REITs that do not generate a majority of their revenue and income from real estate rental and leasing operations. The S&P 500 Index measures the performance of 500 widely held large cap U.S. companies. The indexes and the Fund include reinvestment of interest, capital gains and 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.

BARON FUNDS 1987

We are also pleased to report that according to ***Morningstar****, for the period ended March 31, 2018:

- The Baron Real Estate Fund is the #1 ranked real estate fund among its peers for its 1-year, 5-year, and more than 8-year (since inception) performance.
- The Baron Real Estate Fund has been awarded the highest 5-star Morningstar rating for its overall and 5-year risk-adjusted performance.

We remain optimistic about the prospects for real estate and the Baron Real Estate Fund. Please see the "Outlook" section at the end of this letter for our forward-looking views for the Fund.

Table II.
Top contributors to performance for the quarter ended March 31, 2018

	Quarter End Market Cap (billions)	Percent Impact
CoStar Group, Inc.	$13.1	0.35%
InterXion Holding N.V.	4.4	0.32
CBRE Group, Inc.	15.9	0.21
MGM Resorts International	19.8	0.15
NEXTDC Limited	1.4	0.10

The shares of **CoStar Group, Inc.** gained 22% in the first quarter of 2018. In January, this leading provider of information and marketing services to the commercial real estate industry, reported record new business booking activity for December 2017 of approximately twice its recent average monthly sales. We believe these results bode well for revenue in 2018 and beyond.

CoStar has built the most comprehensive and proprietary database of essential commercial real estate data on more than 5 million commercial properties in the U.S. and the U.K. The company markets this data to serve a vast pertinent global real estate market that is estimated at $50 trillion.

In 2017, CoStar generated revenues of $965 million, 30% cash flow (EBITDA) margins, and $5.76 per share of free cash flow. We expect revenue to double to approximately $2 billion in the next four years and EBITDA margins to expand to more than 40%, as CoStar leverages its investments in sales headcount, product expansion, and multi-family marketing.

This combination of sustained revenue growth and dramatic margin expansion should lead to nearly a tripling of free cash flow power in the next four years to $15.74 per share in 2021. We also expect CoStar to generate more than $1 billion of cumulative free cash flow over the next four years, that the company may use to make value enhancing acquisitions or distribute this cash to shareholders. Based on the current valuation of its shares and our expectation for future growth, we believe CoStar's shares have the potential to appreciate more than 15% annually over the next few years. We remain bullish about the prospects for the company.

InterXion Holding N.V., a European-centric data center company, has been one of the Fund's top holdings. The company has consistently delivered strong business results since we began acquiring its stock in late 2015. These shares have been among the Fund's best performers in both 2016 and 2017, and they are off to a strong start in 2018.

We are especially encouraged by InterXion's January announcement of new expansion projects in seven cities across its European footprint. The company is currently expanding in each of the 11 countries in which it operates. We estimate it can increase its data center footprint by more than 25%, which translates into an almost doubling of annual cash flow in approximately five years. Ultimately, we wouldn't be surprised if the company itself became an attractive acquisition candidate for even larger global players looking to expand in Europe.

The shares of **CBRE Group, Inc.**, the largest and leading commercial real estate services firm in the world, gained 9% in the first quarter due to its strong quarterly business results amid management's expectations for solid earnings growth of approximately 15% in 2018.

We have long admired CBRE and remain optimistic about the company's prospects. It enjoys the #1 worldwide market share position in each of its key business lines–leasing, property sales, and outsourcing. Moreover, CBRE continues to pull away from the pack by growing its market share. Management, led by CEO Bob Sulentic, has, in our view, prudently improved the resilience of its business mix by increasing the percentage of CBRE's real estate businesses that generate recurring or contractual cash flows. The company boasts the strongest balance sheet in the commercial real estate services industry. Its ratio of net debt to cash flow is only 0.8 times, with zero debt maturing in the next four years. It also has more than $3 billion of available liquidity.

* Morningstar calculates the **Morningstar US Fund Real Estate Category** Average using its Fractional Weighting methodology. Morningstar rankings are based on total returns and do not include sales charges. Total returns do account for management, administrative, and 12b-1 fees and other costs automatically deducted from fund assets. As of 3/31/2018, the category consisted of 261, 198, and 157 share classes for the 1-year, 5-year, and since inception (12/31/2009) periods. Morningstar ranked **Baron Real Estate Fund Institutional** Share Class in the 1st (#1 fund), 1st (#1 fund) and 1st (#1 fund) percentiles, respectively, in the category.

As of 3/31/2018, the category consisted of 228 and 198 share classes for the 3-year and 5-year periods. Morningstar has awarded **Baron Real Estate Fund Institutional** Share Class 4 stars, 5 stars, and 5 stars for its 3-year, 5-year, and overall performance, respectively.

The Morningstar Rating™ for funds, or "star rating", is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods.

We believe CBRE may generate earnings of approximately $3.20 per share in 2018 (representing 18% growth) and $3.60 per share in 2019 (12.5% growth). At its current valuation of approximately 15 times earnings, it has the potential to generate mid-teens annual returns for at least the next few years.

We remain optimistic about the prospects for **MGM Resorts International**, a leading global hotel and casino company.

We think MGM offers an appealing combination of high-quality real estate assets, a leading presence in Las Vegas (one of the stronger real estate markets in the U.S.), a solid growth outlook, improving free cash flow, and good prospects for dividend growth. Further, we see compelling value in the shares as its domestic assets are trading at less than 8.5 times 2018 estimated cash flow–much cheaper than its casino and gaming peers. We believe the shares could appreciate 20% annually during the next few years.

The shares of **NEXTDC Limited,** an Australian-based data center company, gained 8% in the first quarter of 2018 following the announcement of strong business results and press reports that certain companies may be interested in acquiring NEXTDC.

Following our research and discussions with CEO Craig Scroggie, we are optimistic about the prospects for NEXTDC. The Australian data center market is still in the early innings of its evolution, and is growing significantly faster than in other parts of the world. We believe the company has a realistic plan in place to grow its cash flow by approximately 100% in the next two years, and by 250% in the next four years. With the successful execution of its business plan, we believe its share price should appreciate meaningfully.

Table III.
Top detractors from performance for the quarter ended March 31, 2018

	Quarter End Market Cap or Market Cap When Sold (billions)	Percent Impact
Macquarie Infrastructure Corporation	$ 3.2	–1.76%
Mohawk Industries, Inc.	17.3	–0.81
Vulcan Materials Company	15.1	–0.59
Beacon Roofing Supply, Inc.	3.6	–0.35
Equinix, Inc.	33.1	–0.30

The shares of **Macquarie Infrastructure Corporation** fell sharply in the first quarter of 2018. Macquarie witnessed unanticipated customer terminations in December 2017 and January 2018 related to its liquid storage business. This business setback, combined with management's desire to continue to pursue its planned capital investment projects without raising equity and/or debt to fund its growth ambitions, led management to elect to cut its dividend by 30%.

We are highly disappointed in management's decisions. We believe the company made unwise business judgments and could have avoided the material drop in its share price. In fact, Macquarie could have maintained its entire dividend without the need to reduce it. Management indicated that it anticipates generating sufficient free cash flow in 2018 to cover its entire dividend! Further, the company could have slowed the pace of its capital expenditures or chosen to raise additional capital (equity and/or debt) to fund its growth plans and support its dividend. We have exited our investment in the company.

Following a 38% gain in its share price in 2017 and management's expectations for slightly more moderate gains in profitability in 2018, the shares of **Mohawk Industries, Inc.**, the worldwide leader in almost all flooring categories, declined in the first quarter. We anticipate Mohawk's stock to rebound because management is making what we believe are prudent investments in its business to drive future growth.

We remain bullish about the prospects for Mohawk because we believe the company will continue to benefit from the positive cyclical trends that we see both in housing and commercial construction. Further, we expect that Mohawk will continue to gain from its initiatives to increase capacity and upgrade its production equipment, as well as its multi-year program of acquisitions that has extended its geographic and product reach. We believe Mohawk's shares are attractively valued at less than 10 times estimated 2018 cash flow, with the potential to generate mid-teens annual returns.

The shares of **Vulcan Materials Company** declined in the first quarter of 2018 due to slightly disappointing fourth quarter 2017 results (pricing and margins were below expectations) and concerns that first quarter of 2018 results could be challenging. We believe the concerns are transitory, and we maintain our bullish view on the prospects for Vulcan.

The key drivers for Vulcan's business–government spending on infrastructure projects and residential/commercial construction levels–are moving in the right direction. In 2018, we expect the company to deliver improved growth, pricing and profitability margins. Longer term, we believe management can double the company's cash flow in the next five years without having to rely on big federal infrastructure legislation. If Vulcan meets its growth targets, we think its shares could reach at least $200 per share in the next four years, quite a bit higher than its recent price of $114 per share.

After its August 2017 announcement of its $2.6 billion acquisition of Allied Building Products, shares of **Beacon Roofing Supply, Inc.** rose more than 60%. With profit taking and expectations that first quarter 2018 earnings may indicate softness in roofing pricing and profitability margins, its shares declined in the first quarter. We view this as temporary. We remain optimistic about the outlook for Beacon for four key reasons:

First, Beacon's acquisition of Allied Building Products created one of the largest and most diverse building materials distribution companies in North America, with 589 locations in 50 states and six Canadian provinces. Management is targeting to more than double its revenues from $7 billion to $15 billion, given its opportunities to increase market share in the roofing, sidewall, and wallboard segments (i.e., management is aiming for a 30% market share of an estimated $55 billion market).

Second, management also indicated that the new acquisition synergies provide ample opportunities for the combined company to cut costs and improve profitability margins through branch consolidation, overhead efficiencies, and future acquisitions.

Third, we think Beacon is well positioned to benefit from the continued rebound in U.S. residential real estate. New home construction and repair/remodeling account for approximately two-thirds of the company's combined sales.

Fourth, we believe Beacon's shares are attractively valued at less than 10 times 2019 estimated cash flow. We believe its shares can generate mid-teen annual returns in the next few years.

The shares of data center company, **Equinix, Inc.**, declined in the first quarter partly due in part to management's announcement that it plans to make larger-than-expected investments in its business in 2018. Though these investments may temporarily temper growth, we anticipate that growth in cash flow will re-accelerate in 2019.

Our research indicates that Equinix's prospects remain strong for organic and development growth, and also for possible acquisitions. We believe the company is exceptionally well positioned to benefit from the rapidly increasing number of companies that outsource their technology needs to high-tech and state-of-the-art data center firms such as Equinix. This outsourcing is also propelled by the explosive growth in data and cloud computing.

Portfolio Structure

We have structured a diversified and balanced real estate portfolio that we believe will benefit from compelling cyclical, secular, and geographic investment opportunities.

From a cyclical perspective, our research indicates that business conditions and the outlook are solid for numerous real estate-related companies. We continue to emphasize those companies that we expect to perform well as economic growth improves and endures.

Portfolio examples include:

1. Leading hotel and timeshare companies such as **Hilton Worldwide Holdings, Inc.**, **Marriott International, Inc.**, **Hyatt Hotels Corp.**, and **Wyndham Worldwide Corp.**
2. Residential real estate-related companies that should benefit from the ongoing rebound in the U.S. housing market such as **Lennar Corporation**, the largest homebuilder in the country. Lennar recently reported strong business results and provided encouraging commentary regarding the prospects for the housing market.
3. Leading building product and services companies that we expect to benefit from the rebound in residential real estate, such as **Home Depot, Inc.**, **Mohawk Industries, Inc.**, and **The Sherwin-Williams Company**.
4. Construction materials companies that should benefit from a continued rebound in residential and commercial construction activity and the expected major increase in state and federal infrastructure projects. These are companies such as **Vulcan Materials Company**, **Martin Marietta Materials, Inc.**, **Summit Materials, Inc.**, and **Eagle Materials Inc.**

From a secular perspective, the Fund continues to focus on technology-related real estate companies.

Cloud computing, the internet, artificial intelligence, autonomous vehicles, mobile data and cellphones, and wireless infrastructure are powerful secular growth opportunities that should persist for several years. At Baron, we refer to these types of enduring developments as "megatrends." These technology-related real estate companies include:

1. Tower companies, such as **American Tower Corp.** and **SBA Communications Corp.,** are positioned for long-term growth as the demand for data-intensive devices (such as iPhones) accelerates, and new technologies continue to improve. The advent and emergence of new technologies and pertinent data require more antenna locations that will continue to benefit tower companies.
2. Data center companies are also well positioned for long-term growth. An increasing number of companies are determining that it is economical to outsource their technology needs to high-tech and state-of-the-art data centers. Fund holdings include **InterXion Holding N.V.**, **Equinix, Inc.**, and **Digital Realty Trust, Inc.**
3. Industrial REITs, such as **Prologis, Inc.** and **Rexford Industrial Realty, Inc.**, are witnessing strong warehouse demand partly in response to emergent e-commerce needs, as online sales are accelerating and customers seek faster delivery.

From a geographic perspective, the Fund always prioritizes real estate companies that we think own unique and well-located real estate assets in markets with high barriers to entry that have attractive long-term demand demographics. Examples include:

1. Las Vegas-centric real estate companies, such as **MGM Resorts International**, **Red Rock Resorts, Inc.**, and **Boyd Gaming Corporation**.
2. International real estate companies, such as **Glenveagh Properties PLC**, **Cellnex Telecom, S.A.**, and **NEXTDC Limited**.
3. "Best-in-Class" U.S. REITs* that own and operate well-located real estate in supply-constrained markets. Examples include **Douglas Emmett, Inc.**, **Boston Properties, Inc.**, and **Alexandria Real Estate Equities, Inc.**

Table IV.
Fund investments in real estate-related categories as of March 31, 2018

		Percent of Net Assets
REITs		24.9%
Building Products/Services		24.3
Hotel & Leisure		15.9
Hotels & Timeshare/Leisure	12.3%	
Cruise Lines	3.6	
Casinos & Gaming Operators		8.3
Data Center Operating Companies[1]		6.8
Real Estate Service Companies		6.3
Homebuilders & Land Developers		4.0
Real Estate Operating Companies		2.4
Tower Operators[2]		0.8
		93.7
Cash and Cash Equivalents		6.3
		100.0%

[1] Total would be 11.2% if included data center REIT Equinix, Inc.
[2] Total would be 8.5% if included tower REITs American Tower Corp. and SBA Communications Corp.

* In our opinion, characteristics of a "best-in-class" real estate company are:
- Owns unique and well-located real estate assets in markets with high barriers to entry combined with attractive long-term demand demographics;
- Enjoys strong long-term growth prospects together with a leading competitive position;
- Maintains a conservative and liquid balance sheet; and, importantly,
- Employs an intelligent and motivated management team whose interests are closely aligned with shareholders.

At March 31, 2018, the Fund maintained investments in 50 companies. Our 10 largest holdings represent 40.7% of the Fund.

As of March 31, 2018, the median market capitalization of the portfolio was $10.2 billion. Companies with a market capitalization of less than $2.5 billion represented 6.6% of the Fund.

Table V.
Top 10 holdings as of March 31, 2018

	Quarter End Market Cap (billions)	Quarter End Investment Value (millions)	Percent of Net Assets
InterXion Holding N.V.	$ 4.4	$64.3	6.3%
American Tower Corp.	64.1	62.8	6.1
Vulcan Materials Company	15.1	51.8	5.1
Home Depot, Inc.	206.3	45.3	4.4
Equinix, Inc.	33.1	44.2	4.3
MGM Resorts International	19.8	38.3	3.8
Mohawk Industries, Inc.	17.3	35.0	3.4
Wyndham Worldwide Corp.	11.4	25.1	2.5
CBRE Group, Inc.	15.9	24.9	2.4
Brookfield Asset Management, Inc.	38.6	24.1	2.4

RECENT ACTIVITY

Table VI.
Top net purchases for the quarter ended March 31, 2018

	Quarter End Market Cap (billions)	Amount Purchased (millions)
Hyatt Hotels Corp.	$ 9.1	$20.8
Penn National Gaming, Inc.	2.4	18.8
Eagle Materials Inc.	5.0	13.2
Extended Stay America, Inc.	3.8	9.9
Vulcan Materials Company	15.1	9.8

In the most recent quarter, we re-acquired shares in **Hyatt Hotels Corp.** The company's hotel portfolio includes more than 700 properties with 186,000 rooms in more than 50 countries across 6 continents.

We have a positive view of Hyatt for several reasons:

First, Hyatt is a leading hotel company with a portfolio of 14 premier brands, including the Park Hyatt, Grand Hyatt, Hyatt Regency, Hyatt, and Hyatt Place. We believe Hyatt's strong hotel brands are primed to increase market share in the next few years.

Second, we believe the company is poised for long-term growth. Hyatt has a hotel development pipeline of 330 hotels and 70,000 hotel rooms. Upon completion, it would result in an almost 50% increase in its hotels from 700 to 1,030 properties and an almost 40% increase in its hotel rooms from 186,000 rooms to 256,000 rooms.

Third, management's effort to transition the company's business model to a higher percentage of managed and franchised hotels versus owned and leased hotels should result in several benefits including:

- Reduced earnings volatility;
- Increased ability to return capital to shareholders via share buybacks and dividends; and,
- Higher stock price valuation with fewer company-owned hotels

Hyatt's shares are currently valued at a sizeable discount to hotel companies that derive a higher percentage of cash flow from fees. As Hyatt increases its fee-based business to approximately 60% of its overall cash flow, we anticipate its valuation discount to narrow, as investors re-value shares upwards.

Further, we believe the shares are currently valued at a sizeable discount to where they would trade in the private market. For example, in February 2018, Hyatt sold three of its hotels for a total of $1 billion, representing 17 times its estimated 2018 cash flow, yet Hyatt's shares trade in the public market at only 12 times cash flow!

If we assume that the balance of Hyatt's owned hotels would be purchased for only 13 times 2019 estimated cash flow, and the company's managed and franchised business is valued at 15 times cash flow (which represents a one to two-point valuation discount to its managed and franchised peers), Hyatt's shares would be worth more than $100 per share versus a recent price of only $75 per share.

Finally, Hyatt maintains one of the strongest balance sheets in the hotel industry and is led by, in our view, a smart, strategic, and motivated management team and Board that has a significant ownership stake in the company. Therefore, management's interests are closely aligned with its shareholders.

We have been acquiring shares in **Penn National Gaming, Inc.** following the announcement that it is acquiring Pinnacle Entertainment. We are optimistic about Penn's prospects because:

(i) The combined company, with its 41 casino and gaming properties in 20 jurisdictions, will be the largest U.S. regional gaming operator in the U.S. with a compelling portfolio;

(ii) There are significant opportunities for Penn to benefit from the acquisition synergies in both revenues and expenses and to accelerate cash flow growth; and

(iii) At its recent price of only $26, with more than a 15% free cash flow yield for the combined company, the valuation of these shares is highly compelling.

We recently began acquiring shares in **Eagle Materials Inc.** by taking advantage of the 20% drop in its share price. The company is a manufacturer and distributor of cement, gypsum wallboard, recycled paperboard, concrete, and aggregates. Eagle's products are widely used in residential, industrial, commercial, and infrastructure construction.

We are encouraged about the prospects for the company because we see a dual opportunity for growth and an increase in its stock valuation. We anticipate that Eagle should be a key beneficiary of the improving housing market and increasing expenditures for infrastructure and non-residential construction, as its products are used in these end markets.

In the last few weeks, Knauf Entities offered to acquire one of Eagle's wallboard competitors, USG Corporation, at a price that would imply that Eagle's wallboard business is significantly undervalued. USG rejected the buyout offer, which bodes well for its view for its own business valuation and prospects. Our sense is that a portion of Eagle's business or the entire company could eventually be targeted as an acquisition candidate. At its recent price of $100 per share, we believe the shares are attractively valued relative to our estimate of its take out price of $140 per share.

Extended Stay America, Inc. is the largest hotel chain in the U.S., with its 625 hotels and 68,000 owned hotel rooms aimed at guests who typically remain at the hotel for at least five days and, in many cases, for more than 30 days. For example, the company generates approximately 70% of its revenues from guests who spend at least five nights at its hotels and 42% from guests who stay at least 30 nights.

We recently met with CEO Jonathan Halkyard and are optimistic about the company's strategic direction. Extended Stay has recently completed a multi-year hotel renovation program. It is now focusing on growing its hotel count from 625 to approximately 800. Over time, the company sees the potential to double its overall hotel count.

As Extended Stay grows its hotel base, it plans to sell its lower-quality hotels and increase the percentage of hotels that it manages and franchises. This should result in lower capital requirements and higher contracted cash flows, and, thus, an improvement in its stock valuation.

Trading at only 10 times 2018 estimated cash flow, and with a dividend yield more than 4%, we believe the shares are attractively valued relative to private market values for many of its hotels and relative to many of its public market hotel peers. Extended Stay expects to generate significant free cash flow in the next few years partly through asset sales, a portion of which we anticipate will be allocated toward share repurchases.

Table VII.
Top net sales for the quarter ended March 31, 2018

	Quarter End Market Cap or Market Cap When Sold (billions)	Amount Sold (millions)
Mohawk Industries, Inc.	$17.3	$22.3
Macquarie Infrastructure Corporation	3.2	20.9
InterXion Holding N.V.	4.4	11.3
Pinnacle Entertainment, Inc.	1.7	10.8
Equity Residential	20.9	10.7

We recently trimmed our positions in **Mohawk Industries, Inc.** and **InterXion Holding N.V.** following exceptionally strong share price performance in 2018. We remain bullish about both companies' long-term prospects.

We exited our position in **Macquarie Infrastructure Corporation** following management's disappointing and unnecessary decision to reduce its dividend by 30%.

We also exited our position in **Pinnacle Entertainment, Inc.** following the announcement that **Penn National Gaming, Inc.** would acquire the company. We think Pinnacle's management team, led by CEO Anthony Sanfilippo, has done an outstanding job creating value for shareholders. Pinnacle was an exceptionally successful investment for the Fund–the shares appreciated 126% in 2017!

We exited our position in **Equity Residential** and re-allocated the capital to real estate companies that we believe have the potential for superior share price returns.

Outlook

U.S. commercial and residential real estate have been rebounding from the Great Recession for more than seven years. As the historical average length of a real estate cycle is approximately seven years, this raises the obvious question of whether this bullish real estate cycle (and, perhaps, the broader economy) is in its very late innings. Our view is **"no."**

While there are a few signs that real estate conditions are "long in the tooth"–such as pockets of decelerating growth due to elevated occupancy and rents and increases in construction activity in a few segments of commercial real estate–we do not believe real estate has reached the end of its recovery or cycle, as we are not witnessing the broad excesses and warning signs that typically accompany the end of a cycle.

These typically include: (i) overheated economic and business growth; (ii) broad-based spikes in construction activity (commercial or residential), though we acknowledge that construction activity is elevated for some segments of commercial real estate; (iii) significantly relaxed bank lending standards and aggressive assumption of debt; (iv) elevated and onerous interest rate levels; (v) over exuberance for acquisitions; and (v) euphoric market sentiment (often a tell-tale sign that a cycle is coming to an end).

Our view is that the length of the current real estate cycle will last longer than most prior cycles–perhaps an *extra inning game*–because this cycle to-date has been relatively free of the excesses that typically accompany most real estate cycles. Additionally, due to anticipated pro-growth initiatives, such as lower taxes, fewer financial regulations, and perhaps additional infrastructure spending, we anticipate an extended economic and real estate cycle.

Further considerations that support our constructive outlook for real estate and the prospects for the Fund include:

1. We maintain that the factors that have fueled the resurgence in real estate largely remain in place: Demand continues to outstrip supply in most U.S. markets, balance sheets are generally in solid shape, and credit remains available at attractive interest rates levels;

2. Business conditions are solid for the Fund's real estate companies–both residential and commercial–and the outlook does not portend a recession;

3. As discussed in the "Portfolio Structure" section earlier in this letter, we have structured the Fund to capitalize on what we believe are compelling cyclical, secular, and geographic real estate investing opportunities; and

4. We continue to own several attractively valued companies across many segments of both commercial and residential real estate.

Of course, we will remain vigilant in researching and monitoring possible factors that would cause us to turn more cautious, such as a deceleration in demand, excessive increases in construction activity, increased restrictive lending policies, spikes in interest rates, and overly elevated valuations. While our antenna remains up, we maintain a favorable outlook.

Thank you for your past and continuing support. I remain a major shareholder of the Baron Real Estate Fund, alongside you.

Sincerely,

Jeffrey Kolitch
Portfolio Manager

Investors should consider the investment objectives, risks, and charges and expenses of the investment carefully before investing. The prospectus and summary prospectus contains this and other information about the Funds. You may obtain them from its distributor, Baron Capital, Inc., by calling 1-800-99BARON or visiting www.BaronFunds.com. Please read them carefully before investing.

In addition to general market conditions, the value of the Fund will be affected by the strength of the real estate markets. Factors that could affect the value of the Fund's holdings include the following: overbuilding and increased competition; increases in property taxes and operating expenses; declines in the value of real estate; lack of availability of equity and debt financing to refinance maturing debt; vacancies due to economic conditions and tenant bankruptcies; losses due to costs resulting from environmental contamination and its related cleanup; changes in interest rates; changes in zoning laws, casualty or condemnation losses; variations in rental income; changes in neighborhood values; and functional obsolescence and appeal of properties to tenants. The Fund may not achieve its objectives. Portfolio holdings are subject to change. Current and future portfolio holdings are subject to risk.

Discussions of the companies herein are not intended as advice to any person regarding the advisability of investing in any particular security. The views expressed in this report reflect those of the respective portfolio managers only through the end of the period stated in this report. The portfolio manager's views are not intended as recommendations or investment advice to any person reading this report and are subject to change at any time based on market and other conditions and Baron has no obligation to update them.

This report does not constitute an offer to sell or a solicitation of any offer to buy securities of Baron Real Estate Fund by anyone in any jurisdiction where it would be unlawful under the laws of that jurisdiction to make such an offer or solicitation.