## Dear Baron Durable Advantage Fund Shareholder:

### Performance

Baron Durable Advantage Fund (the "Fund") returned 8.01% (Institutional Shares) during the quarter, outperforming the 4.30% return of the S&P 500 Index, the Fund's benchmark. In the first half of the year, the Fund is up 24.03% compared to 18.54% for the S&P 500 and over the last year, the Fund is up 11.43% compared to 10.42% for the S&P 500.

**Table I.**
**Performance**
**Annualized for periods ended June 30, 2019**

| | Baron Durable Advantage Fund Retail Shares[1,2] | Baron Durable Advantage Fund Institutional Shares[1,2] | S&P 500 Index[1] |
|---|---|---|---|
| Three Months[3] | 7.94% | 8.01% | 4.30% |
| Six Months[3] | 23.86% | 24.03% | 18.54% |
| One Year | 11.15% | 11.43% | 10.42% |
| Since Inception (December 29, 2017) | 9.51% | 9.77% | 8.71% |

ALEX UMANSKY
PORTFOLIO MANAGER

Retail Shares: BDAFX
Institutional Shares: BDAIX
R6 Shares: BDAUX

In the second quarter, we saw a continuation of the solid momentum from the first three months, as the market shrugged off concerns of a global macro slowdown along with mixed signals from the U.S. economy as investors started pricing in the more dovish interest rate stance telegraphed by the Federal Reserve, which indicated there was a growing probability for rate cuts throughout the second half of the year starting with the July meeting.

This quarter, we generated 327 basis points of outperformance due to stock selection (on top of 201 basis points that we generated in the first quarter). Our stock selection added value in every sector where we have made investments, with the exception of Communication Services. We've even managed to "add value" in sectors where we held no stocks (Energy and Utilities), which we thought was pretty cool. We had 14 double-digit gainers against a lone double-digit decliner (A.O. Smith was down 11%) with 29 of our holdings overall rising in value. **Microsoft, IHS Markit, Mastercard, CME Group, TE Connectivity** and **LVMH** contributed over 50 basis points each to absolute returns, while an additional eight investments contributed over 30 basis points each. **Alphabet** (the parent company of Google), **Agilent Technologies** and **A.O. Smith** were our only decliners of note, costing the Fund 62 basis points combined.

Our goal continues to be to find and own for the long term, great businesses with sustainable competitive advantages and entrenched leadership positions in their markets. We seek to invest in high-quality businesses that earn high returns on invested capital, but no longer have the ability to reinvest all of their excess free cash flow back into the company, and are thus returning a large portion of it back to shareholders in the form of dividends or share buybacks. We believe that owning a portfolio of these businesses will enable us to outperform the S&P 500 Index over the long term, while minimizing the risk of permanent loss of capital and the inherent volatility that comes with investing in growth companies.

At Baron Funds, we are long-term investors. We have an extremely long time horizon in this Fund. We quantify it as – essentially forever. This is the framework for how we evaluate and measure the businesses in which we invest (and therefore encourage our investors to measure our performance over years and market cycles, rather than quarters). While market prices can fluctuate dramatically in any given quarter or even year, intrinsic values tend to be much more stable, especially for the types of entrenched, durable businesses we target in this Fund. This also drives the types of questions we ask management teams when we meet them, focusing on understanding how they have reinforced their competitive moats rather than whether growth would come in at 10% or 12% in the period they are about to report.

*Performance listed in the table above is net of annual operating expenses. Annual expense ratio for the Retail and Institutional Shares as of September 30, 2018 was 7.45% and 5.71%, respectively, but the net annual expense ratio was 0.95% and 0.70% (net of the Adviser's fee waivers), 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 reimburses certain Baron Fund expenses pursuant to a contract expiring on August 29, 2030, unless renewed for another 11-year term and the Fund's transfer agency expenses may be reduced by expense offsets from an unaffiliated transfer agent, without which performance would have been lower. Current performance may be lower or higher than the performance data quoted. For performance information current to the most recent month end, visit www.BaronFunds.com or call 1-800-99BARON.*

[1] The index is unmanaged. The index performance is not Fund performance; one cannot invest directly into an index. The S&P 500 Index measures the performance of 500 widely held large cap U.S. companies. The index 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.

So, what happened to the intrinsic values of our holdings in the most recent quarter?

We believe they have grown nicely while at the same time their competitive moats continued to expand. **Microsoft**, our largest holding, grew its cloud business by over 40% year-over-year to a run rate of over $38 billion, while profit margins expanded, yet again. **Mastercard** was chosen by Apple as its preferred credit card provider (adding to its ecosystem), expanded its partnerships with Santander in Brazil, Rogers Bank in Canada, and BNP Paribas in France, and closed a deal with Citibank as its exclusive network for cross-border transactions in China. The company grew revenues by 13% and EPS by 24% in its most recent reported quarter. **UnitedHealth Group** grew to serve 880,000 more people with medical benefits, driving a 9% growth in revenues and a 19% growth in operating income. While the stock underperformed during this period, driven by Medicare-for-All fears, we believe Medicare-for-All is highly unlikely and the intrinsic value of the company has expanded more than its stock price, based on our calculations. As a result, we added to our position during the quarter. **IHS Markit**, the data and analytics leader, grew revenues by 13% with industry-leading EBITDA margins (over 40%) as the company continues to power data-driven insights for over 50,000 customers globally including 80% of the Global Fortune 500. We increased our IHS Markit position as well during the quarter. A recent Gartner report showed that **Texas Instruments** ("TI") has continued to expand its market share in the Analog Semiconductor market during 2018 and, though the current semiconductor backdrop is "sketchy" and TI's exposure to Huawei (4% customer) is scaring many investors off – you guessed it – we increased our position.

We also put fresh capital to work initiating three new investments during the quarter. **Iqvia Holdings**, a leading global provider of advanced analytics, technology solutions, and contract research services to the life sciences industry, **Adobe**, the leading digital media and digital experience cloud software provider, and **Alexandria Real Estate Equities**, the leading life sciences focused REIT. We spend more time on each company under the section titled Recent Activity below.

**Table II.**
**Top contributors to performance for the quarter ended June 30, 2019**

| | Quarter End Market Cap (billions) | Percent Impact |
|---|---|---|
| Microsoft Corporation | $1,026.5 | 0.70% |
| IHS Markit Ltd. | 25.6 | 0.68 |
| Mastercard Incorporated | 270.2 | 0.61 |
| CME Group, Inc. | 69.5 | 0.58 |
| TE Connectivity Ltd. | 32.3 | 0.57 |

**Microsoft Corporation** is a software mega-cap company focusing on cloud software through Azure – its Infrastructure and Platform-as-a-Service offering, and its Software-as-a-Service offerings – Office 365, Dynamics 365, Teams, and more. Shares of Microsoft were up 14% in the quarter continuing the momentum from the first quarter as the business continued to perform well. Its cloud business grew 41% year-over-year, margins expanded, and overall commercial bookings grew 30% (this metric includes the mature, slower growing businesses). Microsoft's ability to accelerate its top-line growth to double-digits at its scale (over $115 billion in revenues) is a good case study for business transformation in our view. From a company that was a "closed-garden" focused on defending its mature Windows business, Microsoft transformed to a company that supports open source, interoperates with competing operating systems (i.e., Linux), and is one of the top two or three best-positioned companies to benefit from the significant opportunity in cloud computing (with cloud still representing only about 5% of the $3.7 trillion global Information Technology market). We believe that Microsoft's competitive advantages are strong and durable as it benefits from the long reach of its sales channel, its differentiated hybrid cloud offering, and its large installed base of enterprise customers.

**IHS Markit Ltd.** provides critical information, analytics, and expertise across the financial services, natural resources, and transportation markets, enabling customers to improve efficiency and make more informed decisions. The company employs more than 5,000 analysts, data scientists, financial experts, and industry specialists to generate proprietary content that reinforces the durability of its competitive moat. The stock was up 17% during the quarter, after the company reported solid quarterly results that were better than expected. We expect the second quarter's organic growth of 5% to improve over the next couple of quarters due to easier comparables and lapping the acquisition of the faster-growing Ipreo. Management is also optimistic about the long-term prospects of the data lake strategy, which provides customers with a single platform to explore and access all of IHS Markit's data, driving new insights, synergies, and savings. We believe the company is well positioned to achieve management's long-term targets of 5% to 7% organic revenue growth, 100 basis points of annual EBITDA margin expansion, and double-digit EPS growth.

**Mastercard Incorporated** is a leading global payment network. Shares appreciated 13% after the company reported solid quarterly results that exceeded investor expectations. The ongoing shift to electronic payments drove 12% purchase volume growth, 13% revenue growth, and 24% EPS growth on a constant-currency basis. Mastercard is an example of a business we like a lot. It has a wide moat, high barriers to entry and the opportunity to keep growing for many years as it benefits from the continued growth in global consumer spending as well as the secular shift from cash to electronic payments (with cash still used in over 80% of global transactions).

**CME Group, Inc.** is the world's largest and most diversified derivatives marketplace. Its exchanges support trading of futures and options across a variety of asset classes, including interest rates, equity indexes, energy, agricultural commodities, currencies, and metals. After underperforming earlier in the year, shares rose 18% in the second quarter as a changing interest rate outlook led to higher market volatility and 14% growth in average daily trading volume. The company also reported quarterly earnings that exceeded expectations. We continue to believe that CME operates a strong business with a wide structural moat driven by the network effects between buyers and sellers on its marketplaces (the value of a marketplace is a function of its liquidity, which rises with the number of participants), its capital-light requirements, and its experienced management team that allocates capital well. We continue to own the stock as we believe CME would benefit from higher volatility and an increasing adoption of exchange-traded futures.

**TE Connectivity Ltd.**, a leading manufacturer of connectivity and sensor solutions for harsh environments, outperformed during the quarter with shares rising 19%. The company reported a strong quarter while also raising guidance for the year as the auto business grew faster than production and as margins in the industrial business expanded. The company also made an

offer to acquire First Sensor, a German sensor manufacturer, broadening its offering to a deeper and more diverse customer pool. We continue to hold TE Connectivity as we believe the company has sustainable competitive advantages driven by its focused portfolio of harsh environment applications, and we believe it will benefit from the strong secular trend of electrification, particularly in the auto segment.

**Table III.**
**Top detractors from performance for the quarter ended June 30, 2019**

| | Quarter End Market Cap or Market Cap When Sold (billions) | Percent Impact |
|---|---|---|
| Alphabet Inc. | $751.0 | –0.31% |
| Agilent Technologies, Inc. | 23.6 | –0.19 |
| A. O. Smith Corporation | 7.9 | –0.13 |
| Taiwan Semiconductor Manufacturing Company Ltd. | 197.4 | –0.09 |
| UnitedHealth Group Incorporated | 231.9 | –0.05 |

**Alphabet Inc.** is the parent company of Google, the world's largest search and online advertising company. Shares of Alphabet declined 8% in the quarter following a deceleration in Google Sites revenue growth (as digital advertising has passed the 50% penetration mark) and more challenging sentiment amid increased regulatory scrutiny. Nonetheless, we remain confident in Alphabet's merits as it continues to benefit from growth in mobile and online video advertising, which accrues to its core assets of search, YouTube, and the Google ad network. We are further encouraged by Alphabet's investments in AI, autonomous driving (Waymo), and life sciences (Verily, Calico). We believe that even in a scenario in which regulators decide to split Google, the parts are likely to be worth more than the whole as value is revealed and a conglomerate discount removed. Several Google businesses are losing money today due to being at an earlier stage of growth (e.g., Waymo), and they artificially inflate Google's valuation multiples.

**Agilent Technologies, Inc.** sells instruments, software, services, and consumables to customers in the life sciences, diagnostics, and applied chemical markets. The stock underperformed, declining 7% during the quarter because the company reported lower-than-expected organic revenue growth, which management attributed to softness in China, as well as slower sales to large pharmaceutical customers. We think these issues are temporary and believe the company's growth can reaccelerate driven by innovation and new product development and the company's exposure to faster growing end markets (such as cancer diagnostics).

**A.O. Smith Corporation**, a world-leading manufacturer of water heaters and boilers, underperformed during the quarter with shares declining 11%. The company continues to suffer from adverse market conditions and an inventory correction in China, which is dragging down sales growth and earnings power. In addition, A.O. Smith was a target of a short report during the quarter which put substantial pressure on the stock, but in our view, was largely misguided. We continue to hold A.O. Smith as we believe the company will continue benefiting from increased penetration in emerging markets as more people join the middle class, new product introduction, and its entrenched competitive positioning in a fairly consolidated industry.

**Taiwan Semiconductor Manufacturing Company Ltd.** is the global leading designer and manufacturer of integrated circuits and wafer semiconductor devices. Shares were down 8% during the period held in the quarter due to the lingering downturn in the semiconductor cycle with continued weakness in smartphones, a pause in hyperscale spending, and the U.S.-China trade tensions that continue to weigh on the global tech sector. We decided to sell our shares and reallocate to higher conviction ideas.

**UnitedHealth Group Incorporated** is the U.S.' largest insurer and leading provider of health care services, IT/analytics, and PBM (pharmacy benefit management) services. Shares were down 1% in the second quarter on what we believe are unwarranted concerns raised by Medicare-for-All rhetoric. We think UnitedHealth's uniquely diversified and complementary set of skills, services, and expertise would allow it to deliver higher-quality health care to its members and customers at a lower cost, which are essential capabilities for successful health care enterprises. We view it as a core holding allowing us to participate in the strong secular growth of health care.

## Portfolio Structure

We expect the Fund to consist of 30 to 50 investments with position sizes ranging from 1% to 5% at the time of purchase. The portfolio is constructed on a bottom-up basis with the quality of ideas and conviction level (rather than benchmark weights and sector composition) having the highest roles in determining the size of each individual investment. Sector weights tend to be an outcome of the portfolio construction process and are not meant to indicate a positive or a negative "view." The Fund's top 10 holdings represented 44.1% of the Fund, the top 20 holdings represented 72.7%, and we exited the second quarter with 34 investments.

**Table IV.**
**Top 10 holdings as of June 30, 2019**

| | Quarter End Market Cap (billions) | Quarter End Investment Value (thousands) | Percent of Net Assets |
|---|---|---|---|
| Microsoft Corporation | $1,026.5 | $244.6 | 5.1% |
| Mastercard Incorporated | 270.2 | 230.7 | 4.8 |
| UnitedHealth Group Incorporated | 231.9 | 225.7 | 4.7 |
| IHS Markit Ltd. | 25.6 | 224.0 | 4.7 |
| S&P Global Inc. | 56.1 | 211.6 | 4.4 |
| Constellation Brands, Inc. | 37.8 | 208.8 | 4.4 |
| Danaher Corporation | 102.3 | 208.4 | 4.4 |
| Moody's Corporation | 37.0 | 207.4 | 4.3 |
| Accenture plc | 124.3 | 174.8 | 3.7 |
| Apple, Inc. | 910.6 | 173.4 | 3.6 |

## Recent Activity

We initiated three new investments during the quarter: **Iqvia Holdings Inc.**, **Adobe Inc.**, and **Alexandria Real Estate Equities, Inc.**, and used the positive flows into the Fund to add to 15 existing holdings. We eliminated **Keyence Corporation** and **Taiwan Semiconductor Manufacturing Company Ltd.**, and did not sell or trim any others.

# Baron Durable Advantage Fund

**Table V.**
**Top net purchases for the quarter ended June 30, 2019**

| | Quarter End Market Cap (billions) | Amount Purchased (thousands) |
|---|---|---|
| Iqvia Holdings Inc. | $ 31.7 | $105.8 |
| Adobe Inc. | 143.0 | 104.8 |
| Constellation Brands, Inc. | 37.8 | 63.4 |
| IHS Markit Ltd. | 25.6 | 59.0 |
| Alexandria Real Estate Equities, Inc. | 16.6 | 47.5 |

We bought **Iqvia Holdings Inc.** during the quarter. Iqvia is a leading global provider of advanced analytics, technology solutions, and contract research services to the life sciences industry. The company was formed in 2016 through the merger of Quintiles, a contract research organization ("CRO") serving biopharmaceutical companies by facilitating clinical trials, and IMS Health, a provider of information and technology services to pharmaceutical companies. Quintiles was the largest global CRO while IMS, a primarily subscription-based provider of health care insights was the dominant player in its space with a 50% market share, greater than five times larger than its closest competitor. The combined company has one of the largest and most comprehensive collections of health care data in the world, which includes more than 600 million comprehensive longitudinal non-identified patient records that generate information and insights on 85% of the world pharmaceuticals. This can be used by clients to increase clinical operations performance, support regulatory and compliance needs, and orchestrate sales operations. The company receives over 70 billion health care records annually from over 120,000 suppliers, which Iqvia's analytics can utilize to improve clinical trial design, site identification, and patient recruitment. This saves time in clinical trials, and is an extremely important value proposition for pharmaceutical and biotechnology companies trying to bring drugs to market as soon as possible. With an estimated $10.8 billion in expected 2019 sales and a total addressable market ("TAM") exceeding $230 billion, Iqvia has a significant runway for growth for years to come. Iqvia is also led by a veteran CEO Ari Bousbib, who has done well in his previous two CEO roles (IMS 2010 to 2016 and Otis elevator under United Technologies, 2002 to 2010), growing IMS revenues at a compounded growth rate of 6%, while increasing EBITDA margins from 25% to 30%; and growing Otis' revenues at an 11% CAGR, while increasing EBITDA margins from 13% to 19%.

We also bought **Adobe Inc.** during the quarter. Adobe is a leading software company providing solutions for creative and marketing professionals, offering products that range from Photoshop to digital marketing and analytics helping companies with digital transformations. Adobe's transition to the cloud has been one of the most successful in the history of the software industry, enabling the company to reaccelerate growth, increase customer retention, and strengthen its competitive moat. Adobe is the leader in creative cloud (two-thirds of revenues), and its platform has become the industry standard. Its digital experience offering (one-third of revenues) is also the most comprehensive platform, offering solutions from advertising to marketing and analytics, and it remains in the early rounds of creating the experience system of record as it integrates its recent two acquisitions of Magento (commerce solution) and Marketo (primarily a business-to-business solution). Adobe's robust opportunity is driven by some of the strongest technological shifts of our generation, including digitization of content, the growing adoption of online advertising, the transition to mobile, and the widespread adoption of video. Adobe's access to data with trillions of data points in marketing, web analytics coming from millions of users, and the artificial intelligence capabilities it adds on top, create a significant moat around its business, with a flywheel effect that continuously increases Adobe's advantages relative to competitors. We believe that the opportunity ahead of Adobe is large and expanding with a TAM estimated at over $100 billion. We believe Adobe remains the best-positioned company to attack that TAM as it benefits from its leadership position in both the creative market as well as the experience market.

Our final new purchase during the quarter was **Alexandria Real Estate Equities, Inc**., which is the largest REIT focused on owning, operating, developing, redeveloping, and acquiring office buildings for the life sciences industry. Alexandria was founded in 1994 by Jerry Sudarsky and Joel Marcus, and was the first REIT to identify and pursue the laboratory niche, which gives them first mover advantage in core life sciences cluster locations, including Greater Boston, the San Francisco Bay Area, San Diego, New York City, Seattle, Suburban Washington, D.C., and Research Triangle Park. Tenants span the life sciences industry, including academic and medical institutions, multi-national pharmaceutical companies, public and private biotechnology entities, U.S. Government agencies, medical device companies, industrial biotechnology companies, venture capital firms, and life sciences product and service companies. The core thesis underpinning the company is the cluster model which has created powerful network effects, driven by the idea that innovative life-sci companies want to locate next to each other, as well as next to world-class academic institutions, talent, and capital to foster innovation and collaboration (not too different from the notion behind Silicon Valley). In our opinion, Alexandria is well positioned to benefit from the aging U.S. population, the rising health care needs, new drug development, and more capital infusions into biotechnology and health care. Core portfolio growth is driven by a marked-to-market growth opportunity, annual rent increases, and occupancy gains, while the clusters the company owns remain in vast over demand (which in turn drives pricing power). We think Alexandria has the potential to double in size by building out its development, redevelopment, and land-holding pipeline over the next five years.

We added to our **Constellation Brands, Inc.** position making it now our sixth largest holding at 4.4% of net assets. Constellation Brands is the third largest producer of beer in the U.S. (including brands such as Corona and Grupo Modelo) and the world's leading premium wine company. The company's Corona and Modelo brands are among the fastest growing brands in the industry, aided by favorable demographic trends and overall trade-up from domestics. Within its beer portfolio, the company has also been driving industry leading top-line growth the last several years, the result of meaningful innovation (line extensions such as Corona Especial & Premier and Corona in cans) and distribution gains. Lastly, the company is well positioned to benefit from potential federal legalization of recreational marijuana use in the U.S., with the potential size of the market estimated at over $50 billion through its ownership stake in Canada's largest cannabis producer, Canopy Growth.

We continued adding to **IHS Markit Ltd**. during the second quarter after first buying it during the fourth quarter of 2018 making it now our fourth largest holding at 4.7% of net assets. We believe that its solid competitive positioning in providing data and analytics that are core to its customers' businesses will enable it to grow and expand margins for many years.

**Table VI.**
**Top net sales for the quarter ended June 30, 2019**

| | Market Cap When Sold (billions) | Amount Sold (thousands) |
|---|---|---|
| Keyence Corporation | $ 74.5 | $62.8 |
| Taiwan Semiconductor Manufacturing Company Ltd. | 197.4 | 53.4 |

We eliminated our **Keyence Corporation** and **Taiwan Semiconductor Manufacturing Company Ltd**. positions in order to reallocate capital to our higher conviction ideas.

## Outlook

Baron Durable Advantage Fund has had a pretty solid six months with a 24% gain. Of course, this period followed the last three months of 2018 when it lost almost 14%. Did the intrinsic values of the competitively advantaged businesses we own decline meaningfully during the bad period, and rise sharply during the good one? Probably not, and we have not reacted or changed the portfolio very much. From time to time, these swings create opportunities for long-term investors who focus on finding great high-quality business, to acquire them below their intrinsic values and then to hold them through market volatility and uncertainty, while they continue to compound. That is what we aim to do.

We do not attempt to predict when the next recession would occur or if the market will be up or down over the next 3, 6, or 12 months. We do know however, that over the last 40 years or so, the stock market has outperformed bonds approximately 74% of the time based on rolling five-year periods, and while history doesn't repeat itself it often rhymes. Our goal is to invest in large-cap companies with, in our view, strong and durable competitive advantages, proven track records of successful capital allocation, high returns on invested capital, and high free cash flow generation, a significant portion of which is regularly returned to shareholders in the form of dividends or share repurchases. We hope to maximize long-term returns without taking significant risks of permanent loss of capital. We are optimistic about the prospects of the companies in which we invest and will always continue to search for new ideas and opportunities.

Sincerely,

Alex Umansky
Portfolio Manager

*Investors should consider the investment objectives, risks, and charges and expenses of the investment carefully before investing. The prospectus and summary prospectus contain 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.*

**Risks:** The Fund invests primarily in large cap equity securities which are subject to price fluctuations in the stock market. The Fund may not achieve its objectives. Portfolio holdings are subject to change. Current and future portfolio holdings are subject to risk.

The 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.

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