DEAR BARON REAL ESTATE FUND SHAREHOLDER:

PERFORMANCE

Following our particularly strong performance in 2017, when the Baron Real Estate Fund (the "Fund") gained 31.42% (Institutional Shares), significantly outperforming the MSCI U.S. REIT Index that increased only 3.74%, its primary benchmark Index, the MSCI USA IMI Extended Real Estate Index Net (the "MSCI Real Estate Index") that gained 18.04%, and the S&P 500 Index that gained 21.83%, we are disappointed in the Fund's performance in 2018 (see Table I below).

Table I.
Performance†
Annualized for periods ended December 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]	(16.30)%	(16.25)%	(11.77)%	(7.05)%	(13.52)%
One Year	(22.22)%	(22.04)%	(10.73)%	(5.83)%	(4.38)%
Three Years	(0.04)%	0.22%	4.48%	1.53%	9.26%
Five Years	2.12%	2.38%	6.59%	6.43%	8.49%
Since Inception (December 31, 2009) (Annualized)	11.03%	11.31%	10.74%	9.14%	11.73%
Since Inception (December 31, 2009) (Cumulative)[3]	156.46%	162.31%	150.36%	119.80%	171.25%

Several factors contributed to the Fund's 2018 results. They include:

- Macroeconomic considerations, such as the spike in U.S. interest rates and the Federal Reserve's ("Fed") increasingly assertive removal of monetary accommodation. These factors sparked a severely negative correction, some as high as 30% to 50%, in the share prices of many real estate companies, particularly housing-related securities, such as building product/services companies, construction materials companies, and homebuilders.

JEFFREY KOLITCH

PORTFOLIO MANAGER

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

- Other factors that triggered headwinds and investor concerns for certain real estate categories and companies include:
  - Concerns about slowing economic growth and its impact on hotel and vacation timeshare companies;
  - Market weakness in technology companies (most notably in the fourth quarter of 2018 when the NASDAQ Composite declined by approximately 17%) that impacted the shares of several real estate data center companies; and
  - The temporary business slowdown in Las Vegas and Macau, and its negative impact on the share prices of several casino and gaming companies.

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.*

† The Fund's historical performance was impacted by gains from IPOs and/or secondary offerings, and 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 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

Since the launch of the Fund nine years ago, 2018 was the only period when numerous segments of real estate underperformed, even though in previous solid economic and rising interest rate environments, they had historically performed well.

While we are disappointed with this anomaly, our durable and proven investment process for the past nine years has not changed. The fundamentals of the businesses we own are generally favorable, and we have been taking advantage of opportunities to invest in and add to quality real estate companies, many of which are now trading at much lower valuations than a year ago.

We encourage you to read the "Portfolio Structure" section presented later in this letter. There, we explain why we are generally "staying the course" with regard to the structure of the portfolio, and discuss in detail, our key observations regarding the portfolio's structure and strategy.

We also urge you to review our perspective on the outlook for the market, real estate, and the Fund in the "Outlook" section later in this letter. "Spoiler alert": We are bullish.

During the Fund's nine-year performance from 2010 to 2018, there have been temporary periods when the Fund underperformed. Yet, in each case, the Fund rebounded by resuming its strong performance. For example, in 2017, the Fund rebounded sharply, gaining 31.42%, following tempered results in 2016.

We are encouraged by the early performance of the Fund this new year. The Fund has gained 10% as of January 25, 2019, exceeding the returns of the MSCI U.S. REIT Index, the MSCI Real Estate Index, and the S&P 500 Index. We are optimistic that 2019 will result in a solid year for the Fund.

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

	Quarter End Market Cap (billions)	Percent Impact
American Tower Corp.	$69.7	0.58%
China Tower Corporation Limited	33.3	0.05
SBA Communications Corp.	18.3	0.03
Americold Realty Trust	3.8	0.01

We have a long history of investing in wireless cell tower companies. Cellular towers provide critical real estate infrastructure to the wireless industry. In the U.S., for example, wireless carriers, such as AT&T, Verizon, T-Mobile, and Sprint, rent space on towers to install their communications equipment that transmits and receives wireless signals from mobile phones and other devices.

In the most recent quarter, the Fund's investments in wireless cell tower companies (**American Tower Corp.**, **China Tower Corporation Limited**, and **SBA Communications Corp.)** performed well due to their strong business results and widespread expectations for continued strength in demand.

We remain bullish on the long-term prospects for wireless cell tower companies for the following reasons:

- **Secular Growth Prospects:** The long-term demand outlook for data-intensive devices, such as cellphones, remains strong. For example:
  - U.S. mobile data traffic is expected to grow more than 40% annually for at least the next five years according to data provided by: Cisco VNI 2016, Ericsson Mobility Report June 2018, and AV&Co. Research & Analytics. This dramatic growth in wireless data demand will lead to significantly greater leasing activity and equipment installations on wireless tower locations to maintain the quality of the wireless carriers' signals and support 4G network technology.
  - Looking forward, we expect emerging 5G technology, which will provide numerous benefits to mobile users, including faster video download speeds, to extend the growth trajectory for wireless cell tower companies many years into the future.
  - In addition to smartphones, the connected home, which enables the interconnection of multiple wireless devices, the connected car and wireless delivery of cable TV will also require increased wireless bandwidth that should contribute to strong secular demand growth for the wireless tower companies.
- **Unique Business Models:** Wireless towers have excellent cash flow and economic characteristics.
  - Tenants sign leases that provide long-term revenue and cash flow visibility for the tower companies. Leases are typically non-cancellable, and generally include an initial term of 5 to 10 years with multiple renewal terms at the option of the tenant. Rent increases are typically fixed at an average of 3% annually.
  - The economic characteristics of a wireless tower are fairly unique. Most towers have capacity for four tenants. Typically, the cash flow generated from the first tenant will cover the construction cost of the tower and generate a modest single-digit investment return. Adding tenants, wireless equipment, and upgrades results in significantly higher investment returns because revenue can be added at minimal incremental cost, so more than 90% of the additional revenue flows through to cash flow.

    According to American Tower, a U.S. tower with three tenants will generate a strong 24% return on its investment capital with more than an 80% cash flow margin, and requires minimal capital expenditure for annual maintenance. Outside the U.S., capital investment returns are also high, typically ranging from 25% to 32%.
- **High Barriers to Entry, Limited Competition, and Scale Advantages:**
  - High Barriers to Entry: Despite excellent cash flow and economic characteristics, there tend to be high barriers to entry and limited competition. Why? Most people do not want to see wireless towers in their backyard. As such, government zoning approvals for new towers are often difficult to obtain.
  - Limited Competition: Additionally, in most developed markets, there tend to be only a few large wireless carriers (in the U.S, there are four: AT&T, Verizon, Sprint, and T-Mobile). Most incumbent tower companies have two-to-three carriers on their towers which means that a new tower in the same area has limited opportunity to win new business. As such, competition tends to be limited.
  - Scale Advantages: The Fund has invested in wireless tower companies that own and operate large portfolios of towers. Large tower companies are often able to achieve superior terms and efficiencies in purchasing, construction, management, and other costs given scale advantages.

The shares of **Americold Realty Trust** continued to perform well in the fourth quarter after reporting strong business results. The company is the only REIT that focuses on owning and operating temperature-controlled warehouses. It has the largest portfolio of these warehouses in the U.S. and globally. We think Americold is well-positioned to deliver superior growth relative to most REITs due to strong demand trends, limited supply, and opportunities to improve occupancy and rents in its current portfolio.

We also anticipate that Americold will bolster its growth by developing additional warehouses and by making acquisitions of other temperature-controlled warehouses. We continue to believe the prospects for the company are strong, and its shares remain attractively valued relative to most REITs.

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

	Quarter End Market Cap (billions)	Percent Impact
Penn National Gaming, Inc.	$ 2.2	–1.33%
Equinix, Inc.	28.3	–1.21
InterXion Holding N.V.	3.9	–1.08
GDS Holdings Limited	2.9	–0.94
Marriott Vacations Worldwide Corp.	3.3	–0.85

In the most recent quarter, several of the Fund's investments corrected sharply (as did the broader market) despite generally solid business results and favorable outlooks. Hawkish commentary from Fed Chairman Powell in October and December and China trade-war fears were two of the key factors that contributed to a "sell now, ask questions later" mentality during this period.

In our opinion, the concerns that led to a sharp correction in the stock market and some of the Fund's investments in the last few months of 2018 are now largely discounted in their share prices, and we see prospects for higher share prices. Notably, the shares of the companies listed in Table III above have begun to rebound sharply early in 2019. For example, the shares of **Penn National Gaming, Inc.** have already gained 30% in the first few weeks of the new year!

The shares of Penn, the largest U.S. regional casino and gaming company, declined steeply in the fourth quarter primarily due to speculation that consumer spending at casinos will slow sharply and promotional activity will increase. Following our meeting with management late in the fourth quarter, our sense is that these concerns are worse than the reality. Business appears to be stable and the company is on track to achieve its targeted revenue and expense synergies from its acquisition of Pinnacle Entertainment. At its December 31, 2018 price of only $18.83/share, with close to a 20% free cash flow yield, we believe Penn's valuation is attractive.

Despite strong business results and positive outlooks, the shares of real estate data center companies **Equinix, Inc.**, **InterXion Holding N.V.**, and **GDS Holdings Limited** declined in the fourth quarter. The NASDAQ Composite declined approximately 17% in the fourth quarter, and we believe the key factor that contributed to the recent weakness of these technology-related real estate companies was their correlation to non-real estate technology companies.

We have met with and/or spoken to the management teams of each of these real estate data center companies in the fourth quarter. Our sense is that business conditions remain robust. We believe these lower stock valuations are well below intrinsic value.

Equinix, the leading data center company in the world, is currently valued at a discount to most REITs despite the fact that we anticipate it will grow cash flow at more than twice the growth rate of most REITs.

We met with InterXion's management team both in New York and in Europe while touring some of its European data center facilities and have confidence that the company can continue to grow its cash flow at a mid-teens rate annually for the next few years. Its current valuation is only approximately 15 times cash flow.

We have recently met with the management team of GDS, the leading developer and operator of data centers in China. They report that business conditions are strong and we remain bullish on the company's long-term prospects. The shares are valued at a modest cash flow multiple of only 18 times 2019 estimated cash flow despite expectations to grow its cash flow by more than 50% in 2019 and more than 100% in the next three years.

Marriott Vacations Worldwide Corp., a leading timeshare company with more than 100 resorts, recently completed its acquisition of timeshare operator ILG, Inc. In the last few months, we suspect that certain "event-driven" and "momentum" investors have exited their shares in Marriott Vacations Worldwide, thereby pressuring the company's share price. Further, we suspect profit-taking following strong share price performance, anxieties about the impact from hurricanes and Hawaiian volcanic eruptions, and concerns that consumers may be less likely to purchase vacation timeshares if economic growth slows, have also weighed on its shares.

We have continued to acquire shares in Marriott Vacations Worldwide. We are bullish about the company's long-term prospects. Our sense is that business fundamentals remain solid and its shares are valued at less than seven times 2019 estimated cash flow and only nine times estimated earnings per share. We also believe that the company's customer loyalty program, the Marriott Rewards loyalty program, with 110 million members serves as a key competitive advantage to source and maintain future growth. Finally, we note that insiders have been buying stock at higher prices than where the shares are currently trading–a bullish indicator, in our opinion.

PORTFOLIO STRUCTURE

We continue to maintain that our philosophy of structuring a more inclusive and unique real estate fund–one that includes REITs, but is more expansive, balanced, and diversified than a typical "REIT only" fund–is a compelling long-term strategy. We also believe that the Fund is complementary to our Baron Real Estate Income Fund and most other REIT funds.

Looking forward, regarding the structure of the portfolio, we are generally "staying the course", and have been implementing only a few strategic adjustments. For example, we have been taking advantage of 2018's largely indiscriminate sell-off in several real estate companies to upgrade some of the Fund's holdings and increase our commitment to these discounted real estate categories.

The Fund's portfolio structure and strategy are as follows:

1. Real estate-related categories

   The Baron Real Estate Fund currently has investments in REITs and nine other real estate-related categories (see Table IV below). The Fund's diversification is in stark contrast to most other real estate funds that limit their investments primarily to one real estate category – REITs.

2. REITs vs. non-REITs

   Currently, the Fund has approximately 35% of net assets invested in REITs and 65% in other real estate-related categories. In 2018, the Fund's smaller allocation to REITs weighed on relative performance as many investors piled into REITs in search of "safe haven" dividend-yielding securities. Currently, however, we believe that many of the Fund's non-REIT real estate investments now present superior return potential than most REITs, because of their discounted valuations and superior growth prospects. Over the long term, we remain committed to structuring this product as a diversified and more balanced Fund than most REIT funds.

3. Commercial and residential real estate categories exposure

   The Fund continues to invest in both commercial and residential real estate-related companies.

   Non-REIT residential-related companies that the Fund considers for investment include homebuilders, building product and services companies, land developers, construction material companies, home centers, and senior housing operators.

   A slowdown in the housing market negatively impacted the Fund's performance in 2018. We do not believe the 2018 slowdown in the housing market is the beginning of a major negative inflection point for the U.S. housing market. Instead, we suspect that the current housing market slowdown represents a pause in what will continue to be a multi-year housing recovery.

   In the fourth quarter, we took advantage of lower valuations to increase the Fund's investments in housing-related securities such as homebuilders, building product and services companies, which include home centers. These businesses represented 18.2% of the Fund's net assets as of 12/31/2018. We will continue to monitor the housing market closely, and may look to add additional housing-related investments should business prospects improve.

   We encourage you to read the "Top Net Purchases" section presented later in this letter. There we discuss in more detail the U.S. housing market and the Fund's recent investments in housing-related companies.

4. Emphasis on cyclical growth real estate-related companies

   We remain committed towards real estate-related categories that often perform well in a growing economic environment. Our research indicates that business conditions and prospects are stable for the Fund's most economically-sensitive companies. Examples include casino and gaming companies (approximately 11% of Fund's assets), hotels (approximately 5%), vacation timeshare companies (approximately 5%), and cruise lines (approximately 5%).

   Most of the Fund's cyclical growth investments performed poorly in 2018 despite generally solid business results. A multitude of factors contributed to poor share price performance, including concerns regarding slowing economic growth and technical selling pressures from hedge fund closures and fund redemptions.

   In our opinion, valuations for many of the Fund's investments in cyclical growth companies, such as casino and gaming, timeshare, and cruise line companies are at the lowest valuations we have witnessed since the Great Recession.

5. Emphasis on real estate secular and megatrend growth companies

   The Fund has a long track record of prioritizing companies that we believe are positioned to benefit from enduring megatrends and secular growth opportunities. In the real estate sector, wireless tower companies, data center companies, and Industrial REITs are examples of companies that, in our view, are well positioned to benefit for several years from the technological revolution in cloud computing, the Internet, artificial intelligence, autonomous vehicles, mobile data and cell phones, and wireless infrastructure. As of December 31, 2018, 29.9% of the Fund's total investments were invested in wireless tower (9.8%), data center (18.3%), and industrial REITs (1.8%).

6. Number of Fund holdings

   As of December 31, 2018, the Fund was invested in 41 companies. Our 10 largest holdings represented 47.4% of the Fund. Our 20 largest holdings represented 70.3% of the Fund.

7. Market Capitalization and Liquidity

   We continue to invest in companies of all market capitalizations. As of December 31, 2018, the median market capitalization of the Fund's investments was $9.3 billion. Companies with a market capitalization of less than $2.5 billion constitute only 8.3% of the Fund. The liquidity of the Fund is strong.

8. "Best-in-class" companies that are attractively valued*

   We remain confident about the quality, discounted valuations, and strong long-term prospects of the Fund's holdings. We encourage you to read the "Outlook" section presented later in this letter. There, we discuss in more detail the prospects for many of the Fund's holdings.

* Note that "**best-in-class**" represents the manager's opinion and is not based on a third-party ranking. 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.

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

		Percent of Total Investments
REITs		34.9%
Hotel & Leisure		15.1
Hotels & Timeshare/Leisure	10.1%	
Cruise Lines	5.0	
Building Products/Services		13.4
Casinos & Gaming Operators		11.0
Data Center Operating Companies[1]		8.4
Real Estate Service Companies		7.8
Homebuilders & Land Developers		4.8
Real Estate Operating Companies		3.7
Tower Operators		0.9
		100.0%

[1] Total would be 18.3% if included data center REITs Equinix, Inc., Digital Realty Trust, Inc., and CyrusOne Inc.

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

	Quarter End Market Cap (billions)	Quarter End Investment Value (millions)	Percent of Net Assets
American Tower Corp.	$ 69.7	$39.7	7.3%
CBRE Group, Inc.	13.6	34.7	6.4
Equinix, Inc.	28.3	34.6	6.3
InterXion Holding N.V.	3.9	28.5	5.2
MGM Resorts International	12.8	25.3	4.6
Lowe's Companies, Inc.	74.2	22.5	4.1
Brookfield Asset Management, Inc.	38.3	20.4	3.7
Home Depot, Inc.	194.1	19.9	3.6
D.R. Horton, Inc.	12.9	18.5	3.4
Americold Realty Trust	3.8	15.5	2.8

RECENT ACTIVITY

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

	Quarter End Market Cap (billions)	Amount Purchased (millions)
Lowe's Companies, Inc.	$74.2	$23.4
D.R. Horton, Inc.	12.9	19.0
CBRE Group, Inc.	13.6	17.1
Lennar Corporation	12.6	9.0
Caesars Entertainment Corporation	4.5	8.8

In the fourth quarter, we took advantage of the widespread and sharp correction in the shares of housing-related companies to acquire several companies at what we believe are compelling valuations. Examples of three recent housing-related purchases include:

Lowe's Companies, Inc. is the second largest home improvement center in the U.S. We recently attended a meeting with Lowe's newly appointed senior management team at their corporate headquarters in North Carolina. We believe the company has a credible plan to generate strong earnings growth in the next few years. Lowe's share price peaked in 2018 at $117 per share. We have acquired shares at an average cost of $96 per share, which represents a valuation of only 15 times estimated 2019 earnings per share or 16% growth.

D.R. Horton, Inc. is the largest homebuilder by volume in the U.S. We believe the company is positioned to perform well given its status as the largest and lowest-cost producer in the entry level home segment for first-time buyers and baby boomers looking for an affordable home. We are optimistic about the company's plans to transition to a stronger and more "asset light" balance sheet by outsourcing its land development spending needs to third-party developers such as Forestar Group Inc. D.R. Horton's shares reached $53 per share in 2018. We have acquired shares at an average cost of $36 per share, which represents a valuation of only 8.5 times estimated 2019 earnings per share and 1.5 times book value per share.

Lennar Corporation is a leading national home building company. Its management team has an excellent track record of delivering strong operating results, acquiring public and private companies, and creating shareholder value. It's share price peaked in 2018 at $72 per share. We have acquired shares at an average cost of $44 per share, which represents a valuation of only 6.3 times estimated 2019 earnings per share and 1.2 times book value.

Although we are cautious about near-term business prospects for many housing-related companies, we remain optimistic about the long-term prospects for the U.S. housing market and many housing-related securities.

Concerns regarding home price affordability, mortgage rates, tax reform's impact on real estate, and a slowing economy are largely discounted in the share price valuations of most housing-related companies. Further, we believe that the recent decline in mortgage rates, moderation in home price increases, and strong job and wage growth could encourage a reacceleration in home purchases and housing-related spending.

We believe the current housing market slowdown represents a pause in what will continue to be a multi-year housing recovery. Unlike the 2008/09 housing crisis, today's housing market presents a favorable imbalance between housing demand and supply. The residential annual construction rate of approximately 1.2 million new homes has remained 20% below the 60-year annual average of 1.5 million new homes. This is striking because the U.S. population of approximately 325 million is approximately 90% larger today) than the approximately 172 million it was 60 years ago (! We have maintained that this large imbalance between pent-up housing demand and low construction levels bodes very well for new single-family home purchases when these construction levels increase.

Home prices, despite recent increases, remain more affordable than they were in 2008/09. Additionally, U.S. consumer prospects appear to be improving as job growth remains strong and wage gains continue to improve.

We will continue to monitor the housing market closely, and may look to add additional housing-related investments as business prospects improve.

In the most recent quarter, we took advantage of the declining share price of **CBRE Group, Inc.**, the largest and leading commercial real estate services firm in the world, to acquire additional shares of this "best-in-class" company.

We have long admired CBRE, and continue to be quite 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 its competition 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 three years. It also has more than $3 billion of available liquidity.

CBRE's current valuation is only 11.5 times estimated 2019 earnings per share versus its historical average valuation of approximately 16 times per share.

In the most recent quarter, the Fund acquired shares in **Caesars Entertainment Corporation**, a global casino-entertainment company that operates resorts primarily under the Harrah's, Caesars, and Horseshoe brand names. The Fund's cost basis in the shares is approximately $8.80 per share, a price that we believe is materially below the intrinsic value of the company.

In October 2018, news articles reported that Caesars had received an offer to merge with another company that values Caesars at $13 per share or approximately 50% higher than its recent price. Further, in early 2019, press reports indicated that famed activist investor Carl Icahn has been acquiring shares in Caesars. We believe the shares offer strong upside potential over the next few years.

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

	Quarter End Market Cap or Market Cap When Sold (billions)	Amount Sold (millions)
Vulcan Materials Company	$ 11.1	$20.7
American Tower Corp.	69.7	15.8
Glenveagh Properties PLC	0.5	12.2
Home Depot, Inc.	194.1	11.8
Extended Stay America, Inc.	2.9	11.3

In the fourth quarter, we trimmed some of the Fund's long-term holdings that have performed well. Examples include **American Tower Corp.** and **Home Depot, Inc.**

Additionally, we exited **Vulcan Materials Company**, **Glenveagh Properties PLC**, and **Extended Stay America, Inc.** as well as some other smaller positions, and we reallocated a portion of the proceeds to higher conviction investment opportunities.

OUTLOOK

We have consistently maintained that no one has a crystal ball regarding how macroeconomic changes, political events, and central bank actions may unfold, and what the market's reaction will be to those events. 2018 was certainly a case in point. It was a year that was replete with these influences, all of which contributed to excessive stock market volatility.

Though 2019 may also present some surprises, we continue to believe that the long-term prospects for the equity market, real estate, and the Fund are attractive. Below, we address several topics that we think are of interest.

Q. Since the launch of the Fund nine years ago, the S&P 500 Index has increased 11.73% on an annualized basis. What is our outlook for the equity market going forward?

A. We are mindful of influences and concerns that can affect market performance. These include:

- Slowing global economic growth
- Continued uncertainty regarding the Fed's future action on interest rates and quantitative tightening
- The possible continuation of the U.S.-China trade war
- High federal, corporate, and consumer debt levels
- Widening credit spreads
- Equity and credit market outflows
- Reduced market liquidity
- Continuing U.S. congressional gridlock from extreme partisan politics

Though mindful of these concerns, we are upbeat regarding the prospects for the stock market. Why?

1. Our research indicates that business fundamentals should remain positive and continue to grow (although we expect earnings growth to moderate relative to 2018, due, in part, to the absorption of the benefits derived from the broad tax reforms in 2018).

2. We believe the likelihood of a resolution to the U.S.-China trade war is high.

   The U.S. and China appear to be motivated to resolve differences. In the U.S., given that 2019 is a pre-election year to 2020, the current administration is likely determined to stabilize U.S. earnings growth, the economy, and the stock market.

3. Early in 2019, the Fed has begun to signal a more dovish tone.

   Recent commentary from Federal Reserve Chairman Powell and other Fed governors suggests that the Fed will be patient, and will not be fixated on a pre-determined course regarding future interest rate increases and quantitative tightening. Moderating economic growth and lowered inflation expectations may temper the pace of monetary policy tightening.

4. Company valuations are generally compelling.

   In 2018, the S&P 500 Index multiple compressed from around 18 times next twelve months estimated earnings to 14.4 times earnings, partly due to the acceleration in earnings growth and inflation, and the spike in interest rates. The U.S. 10-year Treasury increased from 2.44% at the beginning of the year to 3.24% at its peak, and the U.S. 30-year mortgage rate increased by approximately 100 basis points to almost 5% at its peak.

   We believe many of the above-mentioned concerns are reflected in current equity valuations. Valuations remain low in the context of interest rates, which declined from a peak of 3.24% to a recent 2.75%, and are meaningfully below the long-term average of 4% to 5%.

   The factors that contributed to the sharp correction in the broad equity market and most real estate-related stocks in the fourth quarter of 2018 have produced increasingly favorable valuations and buying opportunities. We have been identifying several companies to buy at some of the lowest prices we have seen in years! More on real estate valuations below.

Q. Real estate has performed well for most of the last nine years. What is the outlook for the real estate market going forward?

A. U.S. commercial and residential real estate have been recovering from the Great Recession for approximately nine years. As the historical length of a real estate cycle has averaged approximately seven years, some anxiety has arisen over the sheer longevity of the current real estate cycle.

We remain bullish about the outlook for real estate for a number of reasons. Principal among them are:

1. The factors that have fueled the resurgence in real estate largely remain in place:

   - Demand continues to outstrip supply in most U.S. markets and real estate categories. Supply has begun to peak for several categories of commercial real estate at relatively low levels due, in part, to elevated construction costs. In the single-family for-sale home segment of residential real estate, inventory levels remain cyclically depressed relative to historical standards and demographics.
   - Public real estate corporate balance sheets are generally in solid shape.
   - Credit remains available at historically low interest rates. As a case in point, one of the Fund's holdings, Digital Realty Trust, a leading data center REIT, early in 2019 raised $975 million of seven-year debt at an annual interest rate of only 2.50%!

2. Business conditions are generally reasonable, and the outlook does not portend a recession.

   Our ongoing discussions with most commercial and residential real estate companies suggest that business conditions are likely to remain solid, notwithstanding temporary slowdowns in some segments of real estate.

3. We anticipate that the length of the real estate cycle will persist for another few years.

   Real estate is clearly past the 1st or 2nd inning of its recovery – a period that is typically characterized by: (i) the opportunity to buy real estate at distressed prices or large discounts to replacement cost; (ii) low occupancy levels and home sales; (iii) an accommodative Federal Reserve and declining interest rates; and, (iv) the beginning of an economic cycle.

   We do not believe, however, that real estate is in the 9th inning of its recovery, because we are not witnessing the warning signs that typically signal the end of a cycle such as: (i) overheated economic and business growth; (ii) a number of spikes in construction activity (commercial and residential); (iii) exceedingly relaxed bank lending standards, accompanied by aggressive assumption of debt; (iv) overexuberance for acquisitions; and, (v) euphoric market sentiment (often a telltale sign that a cycle is coming to an end).

   In summation, our view is that the length of the current economic and real estate cycle will continue to last longer than most prior cycles because this cycle to-date has not exhibited the excesses that typically characterize most real estate cycles.

4. Substantial private capital is still in pursuit of real estate ownership, and it is encouraged by widely available debt capital at low interest rates.

   The share prices of many real estate companies corrected sharply in 2018 due to economic, interest rate, or other concerns. Large amounts of capital–from private equity investors such as Blackstone Real Estate, sovereign wealth funds, endowments, pension funds, and others–could step in and capitalize on the opportunity to buy quality real estate at depressed prices in the public markets. This "embedded put" scenario should offer protection against downside valuation and pricing, and we are identifying several beneficiaries of this scenario.

5. Any chinks in the armor are, in our opinion, manageable.

   Key warning signs that we consistently monitor include the level of increases in construction activity, deceleration in demand, increased restrictive lending policies, spikes in interest rates, and elevated valuations.

   While our antenna remains up, we maintain a favorable outlook as our research continues to confirm that the opportunities for real estate persist and outweigh the issues or possible chinks in the armor.

6. We continue to identify several real estate-related companies that are attractively valued.

Q. What are the prospects for the Fund over the next few years?

A. Taking into consideration our generally favorable view for commercial and residential real estate, we are likewise optimistic about the prospects for the Baron Real Estate Fund.

Our view is based on the following key factors:

1. The Fund is composed of best-in-class companies

   We believe the quality of the Fund's holdings is as solid as it has ever been. The businesses that we continue to emphasize: (a) are well managed; (b) are market leaders; (c) own well-located real estate; (d) grow cash flow at a faster rate than most peers; and (e) possess quality balance sheets. These special best-in-class companies should generate superior returns over the long term.

   A sampling of the Fund's best-in-class companies includes:

   - **American Tower Corp.**: A leading owner, operator, and developer of communications real estate (i.e., wireless towers).
   - **Equinix, Inc.**: The world's leading owner and operator of real estate data centers.
   - **Home Depot, Inc.**: The largest and leading home improvement center company in the world, with more than 2,200 stores.
   - **CBRE Group, Inc.**: The world's largest and leading commercial real estate services company.
   - **Hilton Worldwide Holdings, Inc.**: One of the largest hotel companies in the world with premier hotel brands including: Hilton, Waldorf Astoria, Double Tree, Embassy Suites, Hampton, Canopy, Conrad, and others.
   - **Marriott International, Inc.**: The largest hotel company in the world with several leading hotel brands including The Ritz Carlton, Westin, St. Regis, W Hotels, Le Meridien, Sheraton, JW Marriott, and others.
   - **Brookfield Asset Management, Inc.**: A premier global investor, operator, and asset manager of high quality real estate and infrastructure-related assets.
   - **The Sherwin-Williams Company**: Global leader in the manufacture, development, distribution, and sale of paint, coatings, and related products.
   - **D.R. Horton, Inc.**: The largest homebuilder by volume in the U.S.
   - **Alexandria Real Estate Equities, Inc.**: A REIT that is the premier landlord and developer to the life science industry.
   - **Douglas Emmett, Inc.**: This REIT is a leading landlord and developer of office and apartment buildings in the premier coastal submarkets of Los Angeles and Honolulu.

2. The Fund is composed of several companies trading a discounted valuations

   Regarding real estate valuations, large segments of real estate-related stocks declined sharply in 2018 in what felt like a "sell now, ask questions later" mentality. This broad-based and sharp price correction has left many real estate-related companies at valuations that we believe are at the lowest levels in several years.

   We are identifying several companies that are just too "cheap" today, and we have good prospects for strong returns over the next few years.

   Examples include:

   - Casino & Gaming Operators

     MGM Resorts International, **Penn National Gaming, Inc.**, **Boyd Gaming Corporation**, and **Red Rock Resorts, Inc.** were valued at the lowest cash flow multiples in several years. MGM, for example, a Las Vegas-focused hotel and casino company, at $24 per share, was valued at only 7.5 times 2019 estimated cash flow for MGM's domestic real estate assets. We estimate that the company would be worth $35 to $40 per share in the private market or 45%-to-65% above its December 31, 2018 price.

   - Timeshare Companies

     Hilton Grand Vacations Inc. and **Marriott Vacations Worldwide Corp.** were valued at only 6.5 times estimated 2019 cash flow, versus valuations of approximately 10 times cash flow just one year ago and now the lowest valuations in several years.

   - Cruise Line Companies

     Leading cruise line companies, **Norwegian Cruise Line Holdings, Ltd.** and **Royal Caribbean Cruises Ltd.**, were valued at only 8 to 9 times 2019 estimated earnings per share versus historical averages of approximately 14 times earnings per share!

   - Hotels

     Leading hotel companies **Hilton Worldwide Holdings, Inc.**, **Marriott International, Inc.**, and **Hyatt Hotels Corp.** were valued at the lowest valuations in several years and at significant discounts to the price that these businesses would be valued in the private market.

   - Commercial Real Estate Services Companies:

     CBRE Group, Inc., the world's number one commercial real estate services company, was valued at only 11.5 times 2019 estimated earnings versus its historical multiple of approximately 16 to 17 times earnings.

   - Real Estate Operating Companies

     Brookfield Asset Management, Inc., a premier owner and operator of real estate-related and other infrastructure assets, was valued at a 25% discount to our assessment of intrinsic value.

   - Homebuilders

     We purchased homebuilder companies, **Lennar Corporation** and **D.R. Horton, Inc.**, at the lowest valuations in several years. For example, we acquired shares in Lennar at only 6.3 times estimated 2019 earnings per share and 1.2 times book value per share, versus its average multiple of 1.9 times book value in the last five years and its prior five-year low multiple of 1.5 times book value.

   - Building Product/Services & Home Center Companies

     Following sharp corrections in the share prices of building product/services companies **Trex Company, Inc.** and **SiteOne Landscape Supply, Inc.** and retail home center company **Lowe's Companies, Inc.,** the Fund purchased shares in these companies at what we believe are compelling valuations.

   - REITs

     Several best-in-class REITs held by the Fund, including **Alexandria Real Estate Equities, Inc.** and **Douglas Emmett, Inc.**, were valued at 20% discounts to our assessment of intrinsic value. Casino and hotel gaming REIT, **Gaming and Leisure Properties, Inc.**, was valued at an 8.4% dividend yield versus many other triple net REITs with dividend yields of approximately 5% to 6%! Premier data center REIT, **Equinix, Inc.**, was valued at its lowest earnings multiple (AFFO) in several years and at a discount to most REITs despite our expectation that the company will grow its earnings at twice the rate of most REITs!

A Final Word on Real Estate and the Fund:

It is our sincere hope that you have found this letter informative.

The outlook for real estate may be more uncertain than in the early stages of the economic and real estate recovery. For example, economic growth is tempering, commercial real estate construction activity has increased, lenders are requiring wider credit spreads, and the Fed continues to monitor conditions that might lead to a pullback from 10 years of monetary accommodation.

We maintain a favorable outlook because our research continues to confirm that the opportunities for real estate and the Fund outweigh the concerns identified above. Absent a recession, our sense is that business prospects for many categories of real estate will remain positive.

Following the Fund's 2017 cumulative eight-year gain of 236.46%, and its one-year gain of 31.42% ending 2017, the Fund's performance in 2018 was disappointing to say the least. We assure you that our team is energized and motivated, with the goal of resuming our historical pattern of outperformance.

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.

Risks: 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.

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