Dear Baron Small Cap Fund Shareholder:

Performance

Baron Small Cap Fund (the "Fund") had a very good third quarter, gaining 8.71% (Institutional Shares).

For the first three quarters of 2018, the Fund is up 19.08%. The Fund outpaced the Russell 2000 Growth Index (the "Index") by 3.19% for the quarter and by 3.32% year-to-date. The Fund is also outperforming the broader S&P 500 Index for the quarter and year-to-date.

Table I.
Performance
Annualized for periods ended September 30, 2018

	Baron Small Cap Fund Retail Shares[1,2]	Baron Small Cap Fund Institutional Shares[1,2,3]	Russell 2000 Growth Index[1]	S&P 500 Index[1]
Three Months[4]	8.65%	8.71%	5.52%	7.71%
Nine Months[4]	18.84%	19.08%	15.76%	10.56%
One Year	25.00%	25.33%	21.06%	17.91%
Three Years	20.00%	20.32%	17.98%	17.31%
Five Years	11.98%	12.28%	12.14%	13.95%
Ten Years	12.53%	12.80%	12.65%	11.97%
Fifteen Years	10.62%	10.79%	10.61%	9.65%
Since Inception (September 30, 1997)	10.58%	10.71%	6.70%	7.50%

The market had its best quarter of the year, was consistently strong throughout, and made new highs. Economic growth accelerated. Corporate earnings continued to grow rapidly. Inflation remained in check, and bond yields have risen just modestly. Though trade tensions continue, and the tough rhetoric escalated with China, new agreements were signed with Mexico and Canada. These concerns, and the tense political atmosphere, took a back seat to the strong economy and corporate performance.

Second quarter GDP grew 4.2%, a significant increase from the pace of the long recovery. The jobs reports remained strong and unemployment fell to 3.7%, near historic lows. Household spending drove the increase in the quarter's growth rate and business fixed investment picked up as well. Corporate earnings are running ahead at an impressive 20%.

CLIFF GREENBERG
PORTFOLIO MANAGER

Retail Shares: BSCFX
Institutional Shares: BSFIX
R6 Shares: BSCUX

The market was led by growth stocks, with Information Technology (IT), Health Care, and Communication Services the sector leaders, as has been the case for most of the year. Larger-cap stocks outperformed smaller companies this quarter. High-quality companies and businesses with lower volatility of earnings did better–these are factors that we emphasize.

Our stock selection has driven our strong absolute and relative performance. Our higher exposure to IT stocks helped, and the performance of our particular holdings far surpassed those of the sector. Our Health Care and Industrials holdings also rose nicely. Our Consumer Discretionary and Materials stocks were weak and did poorly on a relative basis, but that was more than offset by strength elsewhere in the portfolio. Our stocks were mostly strong across the board. There were some key positions that were real standouts and drove our results.

Performance listed in the above table is net of annual operating expenses. Annual expense ratio for the Retail Shares and Institutional Shares as of September 30, 2017 was 1.31% and 1.05%, 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 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 Russell 2000® Growth Index measures the performance of small-sized U.S. companies that are classified as growth and the S&P 500 Index of 500 widely held large cap U.S. companies. The indexes and the Fund are with dividends, which positively impact the performance results. Russell Investment Group is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell is a trademark of Russell Investment Group.
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 Performance for the Institutional Shares prior to May 29, 2009 is based on the performance of the Retail Shares, which have a distribution fee. The Institutional Shares do not have a distribution fee. If the annual returns for the Institutional Shares prior to May 29, 2009 did not reflect this fee, the returns would be higher.
4 Not annualized.

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Table II.
Top contributors to performance for the quarter ended September 30, 2018

	Percent Impact
The Trade Desk	1.09%
Teladoc Health, Inc.	1.08
Acxiom Corporation	0.86
Gartner, Inc.	0.80
The Ultimate Software Group, Inc.	0.58

The Trade Desk is the leading internet advertising demand side platform, enabling advertising agencies to buy digital advertising most effectively. Trade Desk reported another tremendous quarter, growing top line by 54% with EBITDA margins of 33%, despite investing in new initiatives. The stock was the top contributor to the Fund for the second quarter in a row. We continue to be bullish on the situation, betting on the leader in the large addressable market that is transitioning to programmatic ad buying, that inventory will grow through entrance into new channels like TV and Audio, and that international expansion will remain robust. We recently previewed the company's upgraded product offering, which includes elements of intelligence, and came away very impressed.

Teladoc Health, Inc. is the largest global provider of telehealth services. The company reported a strong quarter, with revenue growing 112% (39% organically), fueled by a 48% increase in membership and an acceleration in the utilization of services. The integration of Advanced Medical, the leader in telemedicine outside the U.S., is ahead of schedule and adding to the company's competitive moat and opportunity. The Teladoc platform now has a broad set of clinical capabilities, a global reach, and improved user interface for easy engagement. The company has announced notable wins of new corporate and insurance clients, and an interesting partnership with CVS for retail access. Government plans will start to include telehealth benefits beginning in 2020, which we think will be a big tailwind.

Acxiom Corporation is a leading marketing data company, in which we have been invested for five years. During the quarter, Acxiom entered into an agreement to sell its legacy marketing services business for $2.3 billion, which exceeded Street expectations, completing the company's multi-year program to transform its business and unlock value for shareholders. LiveRamp Holdings, Inc., the surviving entity, is a pure play high-growth marketing cloud software company which provides the infrastructure to enable digital marketing to individuals. We are very excited about its prospects, as it is benefiting from similar digital ad tech trends as is Trade Desk. We believe LiveRamp can sustain strong organic growth and grow to $1 billion in revenues in five years, up four-fold from present, and be a strong stock and possible acquisition target.

Shares of **Gartner, Inc.**, the provider of syndicated research, rose in the quarter on the recognition of the management's progress in turning around the large acquisition of CEB. Organic growth of that business actually decelerated somewhat in the second quarter and the stock initially traded lower. However, management explained that was temporary and expressed their increased confidence that growth will accelerate rather significantly. Gartner is seeing nice traction with its new product upgrades, with the conversion of its offering to a seat-based sale, and with the expansion of its sales force for these channels. We think long term that revenues to the corporate functions served by former CEB products can increase almost 10-fold. Trends in the company's legacy IT research (pacing ahead at a mid-teens rate) and events business are solid. And the company is back in the market repurchasing its stock, having sufficiently de-levered after the big acquisition and in front of expected significant free cash flow generation.

Other stocks that rose over 20% in the quarter but added less to our absolute performance were: **The Ultimate Software Group, Inc., John Bean Technologies Corporation, HealthEquity, Inc., Cognex Corp., Mercury Systems, Inc., Aspen Technology, Inc., Dexcom, Inc., Hudson Ltd., Altair Engineering Inc., Wingstop Inc., Planet Fitness, Inc., Ceridan HCM Holding Inc., BJ's Restaurants, Inc.,** and **Ollie's Bargain Outlet Holdings, Inc.**

Table III.
Top detractors from performance for the quarter ended September 30, 2018

	Percent Impact
Floor & Decor Holdings, Inc.	–0.67%
Shutterfly, Inc.	–0.57
Installed Building Products, Inc.	–0.48
Summit Materials, Inc.	–0.47
Red Rock Resorts, Inc.	–0.36

Floor & Decor Holdings, Inc., the leading retailer of hard-surface flooring, fell in the quarter after the company reported same-store-sales that missed Street expectations. The company has had nine and a half years of double-digit comps (amazing!), and comps were up over 11% in the quarter that just ended. But they are expected to moderate in the future. We viewed this as inevitable. Weighing more heavily on the stock are trade concerns, as the company sources almost half its product from China and several of its categories are on the list of items affected by the latest tariffs. We think that all companies in the industry will be similarly affected and Floor & Decor will be able to negotiate lower prices with its suppliers and pass on some of the increases to customers. We understand the market's concern about the tariffs and the slowing housing market; however, we believe strongly in the long-term potential of this chain, its differentiated business model, its innovative product offerings and in-stock inventory, and the compelling value of its products that appeals to both consumers and installation pros. We added to our position during the quarter.

Shutterfly, Inc., the premier online provider of photo prints and related products declined in the quarter as the company reduced its growth expectations for later in the year. We got involved as we gained confidence that new management would be able to turn around its base consumer business and utilize its printing capacity to build a commercial printing operation and believe there is much to gain in these efforts. We are also excited about the company's acquisition of Lifetouch, the leader in school photography, that would benefit from digitization. We believe the stock is cheap on our estimates of near-term free cash flow, and we think there is considerable growth ahead…so we added to this stock on weakness as well.

Installed Building Products, Inc., an installer of fiberglass insulation and complementary products, fell as results disappointed. Margins are now negatively affected as there is a lag between the higher cost of raw materials that they are experiencing and when they will pass these costs on to builders. The company believes this will ultimately be a positive and additive to the margins. Another issue is that a large commercial building products installation business that they acquired is ramping slower than hoped and is a drag on earnings. Moreover, there is the slowdown in the residential housing industry. We continue to like the situation very much for the long term. We think management is superb and will continue to build a differentiated business that can grow fast both organically and through acquisition, and can be multiple times bigger down the road.

Summit Materials, Inc., a U.S.-based manufacturer of construction materials such as aggregates, cement, and concrete, missed consensus and the stock got beat up. Cement margins were lower, hurt by a competitor who cut price. Operational challenges related to hurricane disruptions and higher transportation costs will weigh on future results. Sentiment is now negative toward levered building products companies in light of increasing interest rates. We expect results to improve and believe the stock is cheap, though we think the company will be less acquisitive go forward since deals will be less accretive with the stock out of favor.

Other stocks that fell 20% or more in the quarter include: **Red Rocks Resorts, Inc.** and **Avalara, Inc.**

Portfolio Structure

As of September 30, 2018, the Fund had $4.7 billion under management. The top 10 positions represented 31.0% of the Fund. At the end of the quarter, we owned 70 stocks.

Table IV.
Top 10 holdings as of September 30, 2018

	Year Acquired	Quarter End Investment Value (millions)	Percent of Net Assets
Gartner, Inc.	2007	$221.9	4.7%
Guidewire Software, Inc.	2012	176.8	3.8
IDEXX Laboratories, Inc.	2008	143.6	3.1
Teladoc Health, Inc.	2017	142.5	3.0
Waste Connections, Inc.	2016	131.6	2.8
TransDigm Group, Inc.	2006	130.3	2.8
ASGN Incorporated	2012	130.2	2.8
The Ultimate Software Group, Inc.	2008	128.9	2.8
The Trade Desk	2017	124.5	2.7
ICON plc	2013	119.2	2.5

The Fund's heaviest sector concentration is in IT. This is where we are finding the most exciting growth companies, and they are up as a percentage of the portfolio as these stocks have gained the most. The comparison of our IT concentration to that of the Index looks more extreme this quarter as a result of the reclassification of the GICS IT sector, which transferred some of the Russell 2000 Growth stocks to other sectors, but not ours. We didn't change our holdings much.

We are not worried by this variance since we often view these industry characterizations as somewhat arbitrary, and since technology is affecting almost all successful businesses these days. Though we own many "application software" businesses, they serve different and varied end markets, so we believe they are less correlated than they appear. For instance, The Ultimate Software Group, Inc. and Ceridian HCM Holding Inc. are SaaS platform providers to the human capital management industry; The Trade Desk and Cision Ltd. are involved in media and advertising; Aspen Technology, Inc. serves process engineering markets; 2U, Inc. the higher education market; Guidewire Software, Inc. the property and casualty insurance industry...and their fates will be affected by how these companies are transforming those particular industries.

The Fund is underweight Health Care, as always. Biotechnology and pharmaceutical stocks make up over 15% of the Index, and we have minimal exposure. We favor more established businesses to invest in, as we have explained in detail in the past. We are about equal weight in the Industrials and Consumer Discretionary sectors, the two other sectors with significant weights in the Fund and the Index.

We are long-term investors in small growth companies. Many of our holdings have been "big winners" for the Fund. As of September 30, we have made over five times their first purchase on holdings that make up 33% of our assets. In addition, we have made at least a double on other stocks that make up 34% of the Fund. So, two thirds of the net assets are represented by stocks that have more than doubled since their first purchase. Since their first purchase, we have made strong average annualized returns on these holdings of 32.1% for the former and 51.2% on the latter, which in our minds, confirms the success of our approach and gives us confidence to pursue this strategy into the future.

Looking at the growth characteristics of our holdings at the start of the quarter, this is what we find:

- Year-to-date, based on the weighted averages of our positions, the revenues of our holdings have increased 13.7% organically, and 20.3% in total revenues including acquisitions.
- Year-to-date, EBITDA has increased 25.4%. EBIT margins are 18.6%, and EBITDA margins are 25.1%.
- Our stocks trade at 27.6 times 2018 EPS and 15.6 times 2019 EPS; 22.9 times 2018 EBITDA and 19.3 times 2019 EBITDA.
- In our opinion, strong growth, high margins, high valuations, but deservedly so.

Comparing this to two years ago, when we last did this overall growth and valuation work…our holdings are growing revenues faster organically (13.7% versus 9.6%) and EBITDA faster (25.4% versus 20.2%), and stocks are more highly valued (19.3 times vs 15.4 times). The reason for the higher growth metrics and valuations is the strong performance of our companies over the last few years, and the modest shift to a higher IT weighting in the portfolio.

Recent Activity

We were not so active this quarter, which often happens after nice runs in the market with stock valuations increasing. We bought two new names and we added to eight existing positions.

We sold out of 3 holdings and trimmed 16 positions.

Table V.
Top net purchases for the quarter ended September 30, 2018

	Year Acquired	Quarter End Market Cap (billions)	Amount Purchased (millions)
Floor & Decor Holdings, Inc.	2017	$2.9	$20.5
Americold Realty Trust	2018	3.7	18.2
Shutterfly, Inc.	2017	2.2	12.8
Sun Hydraulics Corporation	2018	1.7	9.9
Ingevity Corporation	2018	4.3	9.8

We have followed **Ingevity Corporation** ("NGVT") since its spin-off from WestRock in 2016. We recently initiated our position after building conviction that the company can meet or beat its $500 million long-term EBITDA target (from $243 million in 2017).

NGVT has been making carbon since 1914 and has a dominant position in serving the adoption of gasoline evaporative emissions control in vehicles.

While tailpipe emissions are well understood and regulated around the world, evaporative emissions are less visible (from the gas tank), and less regulated. The Performance Materials segment represents approximately half the company's profits, and as environmental standards drive stricter regulations globally, NGVT stands to meaningfully benefit. NGVT's granular and pellet carbon products are the preferred choice (and patent protected through 2022) to meet these regulatory standards. We believe NGVT has market shares approaching 90% globally! Adherence to the "China 6" standard kicks in nationally on July 1, 2020, but many provinces have declared early adoption, with approximately 60% of light vehicles expected by July 1, 2019. For NGVT, this means that its content will jump from $1 to $6 on approximately 25 million vehicles, with close to 40% EBITDA margins attached to that revenue growth. The U.S. is ramping up its standards to a 'Near Zero' system as well, with 80% of vehicles expected to be compliant by 2020, and 100% by 2022. U.S. auto OEMs will need $15 to $20 of NGVT's control technology, up from $6 to $8 previously. Given these tailwinds, we estimate this segment can grow its EBITDA from $142 million in 2017 to $280 million by 2022. Beyond China and the U.S., half the world's vehicles, including those in Mexico and Brazil, would still be operating on antiquated emissions providing further runway for growth.

NGVT's Performance Chemical division takes by-products of the Kraft pulping process and crude tall oil to make specialty chemicals, such as asphalt additives for roads and pavement and emulsion stabilization and corrosion inhibiting chemicals for oil fields. We believe its acquisition of Georgia Pacific's ("GP") pine chemicals business ($310 million purchase price), which closed in March 2018, was an important catalyst to improve segment EBITDA margins from approximately 20% this year to mid-20% over time. NVGT can improve GP's EBITDA from $31 million to $45 million via optimized customer and product mix across a three-plant network, improved yield and operating rates (GP's plant was only 20% utilized), and rapid logistics savings. As important, NVGT secures a key raw material under a favorable 20-year supply contract. With limited customer overlap, GP enables cross-selling opportunities to grow the top-line to complement tailwinds from a recovery in the energy markets. We expect an incremental $75 million of EBITDA in this division over the next four years.

We now see a clearer path of EBITDA growing from approximately $310 million this year to $500 million EBITDA in four years. During that time, NGVT will generate close to $900 million of FCF (25% of market cap) as its CAPX requirements should remain stable. On that basis, we feel like we are buying a high ROIC, high margin (30% EBITDA), strong FCF business, with low leverage at under seven times EBITDA. We believe NGVT can sustain a high multiple (currently 13.6 times '18 EBITDA) given its market leading positions, financial profile, and management's ability to pursue further M&A opportunities or return capital to shareholders. At a low double-digit EBITDA multiple on 2022 estimates, we see a $130-to-$140 stock, generating a nice return from current levels.

Table VI.
Top net sales for the quarter ended September 30, 2018

	Year Acquired	Market Cap When Acquired (billions)	Quarter End Market Cap or Market Cap When Sold (billions)	Amount Sold (millions)
GCP Applied Technologies Inc.	2017	$2.1	$ 1.8	$32.3
IDEXX Laboratories, Inc.	2008	2.0	21.6	24.4
TransDigm Group, Inc.	2006	1.1	19.6	18.6
Qualys, Inc.	2017	1.3	3.5	17.6
HealthEquity, Inc.	2014	0.9	5.9	13.9

We exited our position in **GCP Applied Technologies Inc.**, determining that the business was subscale, not for sale, and would not be able to withstand challenges with higher raw materials costs and disadvantaged foreign exchange rates. We sold the remainder of our position in Beacon Roofing Supply, Inc., disappointed with the pace of organic growth and concerned about the macro environment for building products.

We trimmed some of our larger positions into strength, as is our normal practice. The largest sales were in **IDEXX Laboratories, Inc.**, **TransDigm Group, Inc.**, **Qualys, Inc.**, **HealthEquity, Inc.**, Waste Connections, Inc., and FleetCor Technologies, Inc. All of these have been great stocks for the Fund, but near-term valuations are extended, and the market caps are high. We will use the proceeds from these sales to purchase or add to smaller fresher investments that hopefully will become our next big winners.

Outlook

Since the end of the quarter, interest rates have risen, and stocks have fallen. The correction has been sudden and dramatic. IT, Health Care and growth stocks, which have been the market leaders are now market laggards….as the best become the worst, as is often the case in big sell-offs. Small caps, which have been strong all year because these businesses are more domestically focused and are benefiting from the strong growth in the U.S., are now out of favor. The volatility of these stocks is now a source of concern. Value is favored over growth, reversing the trends of the last few years.

Why have interest rates risen? First, because economic growth is strong and accelerating, and higher rates might be necessary to prevent overheating. Second, because tight labor markets might cause inflation. And third, because trade tensions and tariffs could result in inflation as higher prices work their way through supply chains.

Our sense is that economic growth will likely moderate. Many companies are reflecting this as they report third quarter earnings. We are seeing a slowdown in certain interest rate sensitive sectors, such as housing and lending. Industrial companies are highlighting concerns about disruption caused by tariffs, of rising input and distribution costs, and the increase in the dollar, which is clouding the outlook of near-term earnings. Earnings have not been at risk for some time, but now they are in some instances. By the way, if economic growth does slow, it would take some of the pressure off rising rates and help the market.

We view the economy to be in good shape, and not so strong to stoke negative consequences. We believe that the modest increase in rates and inflation that we anticipate can easily be absorbed by the economy and our portfolio companies. We expect continued growth in the future and don't see a recession in the offing.

The overall market is no longer expensive. Net income is expected to grow over 20% this year, yet the market is flat, so present multiples have contracted significantly. The fear is that earnings growth won't materialize go forward; we don't agree. Some of this year's extraordinary growth is the result of the corporate tax reduction, but, even without that, earnings are growing mid-teens. We expect next year that earnings will grow closer to 10%.

Importantly, we have not changed our view on the near-term growth and long-term prospects for our holdings, for the most part. We believe our high-quality, special/niche growth businesses will be able to continue to accrete value at about a 20% clip in aggregate, some higher, some lower. The valuation of our holdings went from expensive on near-term results, but of great value over the long term, to now being more reasonable on 2019 estimates. We believe the bulk of our holdings deserve premium valuations because of their impregnable market positions, proven growth records, and major long-term opportunities. The market has recognized this over the last couple of years, and we expect that to return when the market regains its footing.

We believe that investing in high-quality growth companies will provide solid returns, as always.

For now, we believe that the fundamentals are being overwhelmed by technicals, geopolitics, and fear. We will stay focused on our process and our holdings and ride this out.

Thanks, my fellow investors, for investing in the Fund.

Cliff Greenberg

Cliff Greenberg
Portfolio Manager

* Acronym for Facebook, Amazon, Netflix and Google.

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: The Adviser believes that there is more potential for capital appreciation in smaller companies, but there also may be more risk. Specific risks associated with investing in smaller companies include that the securities may be thinly traded and they may be more difficult to sell during market downturns. The Fund may not achieve its objectives. Portfolio holdings are subject to change. Current and future portfolio holdings are subject to risk.

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 manager 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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