DEAR BARON SMALL CAP FUND SHAREHOLDER:

PERFORMANCE

Baron Small Cap Fund (the "Fund") fell 22.01% (Institutional Shares) in the fourth quarter, roughly in line with the Russell 2000 Growth Index (the "Index"), which declined 21.65%. For 2018, the Fund lost 7.13%, which outpaced the Russell 2000 Growth Index by 218 basis points. The broader S&P 500 Index fell 13.52% for the quarter, and 4.38% for the year.

Table I.
Performance
Annualized for periods ended December 31, 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]	(22.07)%	(22.01)%	(21.65)%	(13.52)%
One Year	(7.39)%	(7.13)%	(9.31)%	(4.38)%
Three Years	8.98%	9.28%	7.24%	9.26%
Five Years	4.52%	4.79%	5.13%	8.49%
Ten Years	12.79%	13.07%	13.52%	13.12%
Fifteen Years	8.27%	8.44%	7.96%	7.77%
Since Inception (September 30, 1997)	9.16%	9.29%	5.41%	6.68%

The market suffered a broad, swift, and substantial decline in the fourth quarter, culminating in the worst December performance since 1931. Small-cap stocks, which led the market earlier in the year, dropped more sharply than larger stocks in the quarter and in the last trading month when the declines accelerated.

A confluence of events led to the market rollover in early October. Trade tensions with China intensified. The Federal Reserve continued to raise rates and withdraw liquidity from the financial system through "quantitative tightening," while espousing plans to continue on this course. Strong employment reports raised fears of wage inflation. Companies in the housing and lending industries reported slowing trends as interest rates ticked higher. And importantly, earnings reports for the third quarter started to show some weakness in current results and/or cautious guidance about near-term outlets. The increased tariffs caused higher costs for materials, transportation, and logistics that negatively impacted reported profits. The potential of additional and larger tariffs caused many businesses to focus on reorienting their supply chains or to re-think their growth and capital deployment plans until things become clearer. Angst and uncertainty paralyzed our companies and sent the market into a tizzy.

CLIFF GREENBERG
PORTFOLIO MANAGER

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

After a brief respite in November, the sell-off picked up speed in December. In addition to the aforementioned factors, some of which intensified, there was a fresh fear of imminent recession. We quickly went from concern of overheating to talk of recession…stoked by readings of slowing global growth and fears that the U.S. could tip over since the decline in stocks cost U.S. consumers $5 trillion in wealth. We believe the market also lost faith in policy makers and politicians, leading investors to just throw in the towel. As volatility picked up, downside momentum accelerated, and quantitative and algorithmic trading strategies took over. Company fundamentals didn't matter. By the way, we believe fundamentals do matter and in the long run, stocks track company earnings and prospects.

Our Fund acted in line with the Index. We usually outperform in down markets, but this period our stocks traded in lock step, as stocks traded like commodities, without much regard to the individual attributes of our holdings. Also, in major sell-offs like we just experienced, the stocks of the blue chip, high-quality, leading performers usually hold up the best and longest, but when they fall, they fall the hardest because their relative values are much higher, and the holders of these stocks are often taking profits and booking gains as they decline. Many of our worst performing stocks this quarter on a percentage basis (**Teladoc Health, Inc., HealthEquity, Inc., 2U, Inc., ASGN Incorporated, Cision Ltd., IDEXX Laboratories, Inc.,** and

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, 2018 was 1.30% and 1.04%, 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.

BARON FUNDS 1987

Ollie's Bargain Outlet Holdings, Inc.) didn't have any issues with their results and outlooks, yet suffered significant losses since they were some our biggest winners earlier in the year.

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

	Percent Impact
Guardant Health, Inc.	0.11%
Americold Realty Trust	0.01
Planet Fitness, Inc.	0.01

There were a few stocks that didn't decline in the quarter during the broad market sell-off. The stocks that held up best were those of companies with stable business models and whose equities have performed well over the long term, as these are stocks that investors get less nervous about in times of stress. This includes many of our larger and longest held positionings, such as **SBA Communications**, **Bright Horizons**, **Waste Connections**, **Mettler-Toledo**, and **TransDigm Group, Inc.** All of these stocks outperformed the Index this quarter.

Our best performing stock this quarter was **Guardant Health, Inc.**, a new position for the Fund that we bought as part of its IPO in October. Guardant offers liquid biopsy tests for advanced-stage cancer and is developing liquid biopsies for detecting the recurrence of existing cancers in cancer survivors and early detection of cancer in high risk individuals. Liquid biopsies are better than standard tissue biopsies because they are less invasive, do not require access to the tumor samples, enabling repeat sampling, have faster turnaround times, and support real time monitoring of progression. Guardant has unique technology and patent protection, and is the industry leader with demonstrated clinical utility, regulatory approval, and commercial adoption. We believe the company has the potential to revolutionize cancer care, and we think that its revenues can grow over five-fold in the next five years.

Shares of **Americold Realty Trust**, the largest owner/operator of temperature-controlled warehouses, contributed positively to performance. Americold reported a solid third quarter, with NOI growth of 9%. The fundamental backdrop remains positive, with steady demand and limited supply because of high barriers to entry. The company has an expanding pipeline of new development opportunities. They are on track to open a new high-tech facility in Chicago that is being built on spec in the first quarter of 2019, and recently announced it won a large contract to build three large custom facilities for an Australian retailer. We think that accretive acquisitions will be another lever of growth, though we expect transactions to be episodic. We believe that the stock is undervalued, not reflecting its high-quality franchise and solid growth prospects, and that its trading multiple (cap rate in REITs) will increase over time.

Planet Fitness, Inc., the franchisor and operator of low-cost Planet Fitness gyms, helped performance in the quarter after the company reported a broad-based beat to third quarter expectations and increased full-year guidance. System wide same-store sales increased 9.7% and are up double-digits for the year. Total gyms in operation are up 15% and membership is up 26%. The company also announced that it executed a $300 million share repurchase program on an accelerated basis, which we favor since we think this business should have a more appropriately leveraged balance sheet. We admire the company's positioning, as the industry behemoth benefiting from its scale, alongside its approach of offering high-end gyms at rock bottom monthly membership prices. The asset-light franchise business model drives high margins, great returns, and strong free cash flows. We think the company can continue to grow EBITDA at mid double-digit rates for the foreseeable future as it expands its chain from the 1,600 gyms now operating towards their goal over of 4,000 in the U.S.

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

	Percent Impact
GTT Communications, Inc.	–1.11%
Teladoc Health, Inc.	–1.10
Gartner, Inc.	–0.99
ASGN Incorporated	–0.86
John Bean Technologies Corporation	–0.82

Most of the biggest decliners in the fourth quarter were among the top performing stocks in the Fund for the first nine months of the year. Two-thirds of our stocks that declined more than the Russell 2000 Growth Index this quarter had outperformed the Index year-to-date coming into the quarter, including many of our best stocks, which had appreciated anywhere from 40% to 230% for the first nine months. These were mostly high-growth stocks that trade at higher multiples, and sold off the hardest…including **The Trade Desk**, **Teladoc Health, Inc.**, **Wix.com Ltd.**, HealthEquity, Inc., **Yext, Inc.**, **Aspen Technology, Inc.**, **WEX Inc.**, Ollie's Bargain Outlet Holdings, Inc., and **BJ's Restaurants, Inc.** Nothing changed with the fundamentals of any of these companies in the quarter. All have been reporting strong business trends for the year, which had driven strong stock performance coming into the quarter.

Usually the worst performers in any period are companies that stub their toes or are hurt by changes in business conditions. We had some of those this quarter, but they were not the real issue.

Shares of **GTT Communications, Inc.**, a telecommunication service provider to global enterprise customers, was down in the quarter. GTT made a large acquisition of European telco company Interoute, which we think will be accretive and strategic long term, but is blurring the near-term picture. GTT increased its leverage to do the deal, and leverage was a negative market factor in the quarter. GTT is walking away from some acquired unprofitable contracts and is rebuilding its international sales force, which is pressuring organic growth, while expected cost savings are still to come. We like the deal and support its financing, since we consider the balance sheet sound and the company avoided issuing more equity, which is dilutive. We think the company is well positioned to gain significant share in its niche because of superior product offerings and service. We believe the company will post good organic growth, continue to do accretive acquisitions, and has the opportunity to become a major global player. Its stock can rise multiple fold.

Teladoc Health, Inc., the leading provider of telehealth, fell in the quarter along with other high-growth market leaders. The sell-off also reflected news of the resignation of the CFO/COO for violating internal corporate policies. A capable new executive has been installed in the role and guidance was reiterated, so we don't think the company will miss a beat. In the third quarter, business was very strong-membership grew 18% and utilization of services as measured by visits was up 44%. Teladoc has substantial momentum in establishing itself as the dominant provider in the rapidly evolving and expanding telehealth industry. They are rolling out a new point of sale retail service with CVS and government health care programs are soon to adopt the service in droves. We like the company's strategic vision and admire how they have expanded their offerings and reach over the years.

Shares of **Gartner, Inc.**, the provider of syndicated research on technology and business functions, declined in the quarter in conjunction with other tech stocks. The integration of CEB is proceeding well, and management is expanding its sales resources to ramp sales of its revamped offerings. Though not yet evident in the numbers, we sense that CEB is on the verge of a big uptick in its growth rate over the medium term. Gartner's traditional IT research business remains robust, as contract value grew 14% in the latest quarter. Leverage has now been reduced to its target range and the company has begun to repurchase its shares with its free cash flow. We expect repurchase activity to increase significantly. We see growth in free cash flow/share accelerating and believe the stock now trades at a modest multiple by our estimates, yielding significant upside from growth and multiple expansion.

ASGN Incorporated, a large U.S. staffing firm serving the IT, design, and government service sectors, declined in the quarter along with others in the sector on fear of a potential slowdown in the economy. ASGN has had a terrific year. Organic growth has been double-digits and accelerated through the year, benefiting from the tight labor market and increased utilization of temporary staffing that took share from offshoring and consulting. Execution has been solid, with the company continuing to grow much faster than its industry peers. Management has improved the trends in one of its lower performing units and seamlessly integrated the acquisition of ECS, which launched the company's entrance into a new vertical. We expect business trends to remain positive, though the government shutdown might delay some federal contracts. The stock traded down to an unjustifiably low multiple, in our opinion, of adjusted earnings and EBITDA, which we believe does not properly reflect the value of the franchise and the prowess of management.

John Bean Technologies Corporation, a leading global technology solutions provider to the food processing and air transportation industries, detracted during the quarter. The company reported disappointing results due to a sales shortfall in the food business as customers postponed orders due to macro-related uncertainty. In addition, the stock sold off with most Industrials late in the quarter. We continue to hold the stock as we retain conviction in John Bean's ability to grow, improve margins, and consolidate the fragmented food processing equipment industry.

PORTFOLIO STRUCTURE

As of December 31, 2018, the Fund had $3.5 billion under management. The top 10 positions accounted for 32.1% of the Fund. We owned 68 stocks at the end of the quarter.

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

	Year Acquired	Quarter End Investment Value (millions)	Percent of Net Assets
Gartner, Inc.	2007	$166.2	4.8%
Guidewire Software, Inc.	2012	140.4	4.1
Waste Connections, Inc.	2016	120.7	3.5
TransDigm Group, Inc.	2006	110.5	3.2
IDEXX Laboratories, Inc.	2008	102.3	3.0
ICON plc	2013	96.9	2.8
SBA Communications Corp.	2004	93.1	2.7
Bright Horizons Family Solutions, Inc.	2013	91.9	2.7
Ultimate Software Group, Inc.	2008	91.8	2.7
ASGN Incorporated	2012	89.9	2.6

The makeup of the Fund doesn't change much from period to period, as we are long-term investors and our turnover is modest. As before, the Fund is heavily invested in the IT sector, which is where we find the most compelling opportunities. This makes up about 32% of our Fund at year end. We are overweight this sector versus the Index because of our excitement for the growth prospects of our holdings. Industrials are our second highest weighting, at about 18% of the Fund, and we are overweight versus the Index as well. We have about 15% of our assets invested in Consumer Discretionary and 18% in Health Care stocks. We are well underweight the Index in Health Care, primarily because we have just a modest exposure to biotechnology/pharmaceuticals stocks, and are a little higher in Consumer Discretionary. We don't own any Energy or Consumer Staples stocks, and have only minimal exposure to Financials, as we find fewer differentiated businesses and secular growers in those sectors.

Most of our IT investments are application software companies that provide the operating software that serves as the backbone of so many businesses' operations. These are companies that have commanding stature in their niche segments, and whose position we believe is only getting stronger. These are mostly companies that sell their services on a subscription basis with renewal rates (on a dollar basis) of 100% or more and are adding additional products and services to expand their opportunity. We favor these business models as they generate consistent and highly visible results, expand margins and free cash flows with scale, and generally require modest capital so generate high returns.

The Industrials we own are not typical. Our holdings are not very cyclical. We own businesses that are leaders in their segments, benefiting from their market position and business opportunities that are not reliant on external macro factors. Our big holdings are in sub-industries with secular tailwinds such as aerospace & defense (**TransDigm Group, Inc.** and **Mercury Systems, Inc.**), industrial machinery (**RBC Bearings Incorporated**), environmental & facilities services (**Waste Connections, Inc.**), and human resource & employment services (**ASGN Incorporated**). Our smaller investments are in what we consider special companies in niches where there is good secular growth and often international opportunities.

Last quarter we laid out the financial characteristics of our holdings. Unfortunately, our holdings are about 25% lower now and cheaper on a multiple basis, since we think the vast majority of our holdings are still on pace to meet the estimates, we based our calculations on last quarter. For all our holdings, our research group does our own fundamental projections for near-term and long-term earnings (or EBITDA, free cash flow…whatever the appropriate metric). We value each company based on what we think are reasonable and conservative multiples for the applicable metric that is most appropriate for each stock. From year end levels, we presently project over 40% upside to those target stock prices based on calendar year 2020 estimates. Of course, stocks never perform exactly as we underwrite them, but the upside points to the relative attractiveness of our portfolio and is wider than normal.

RECENT ACTIVITY

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

	Year Acquired	Quarter End Market Cap (billions)	Amount Purchased (millions)
Dechra Pharmaceuticals PLC	2018	$2.7	$24.9
Ingevity Corporation	2018	3.5	21.2
Guardant Health, Inc.	2018	3.2	10.3
Cantel Medical Corp.	2014	3.1	7.7
Installed Building Products, Inc.	2017	1.1	5.3

During the quarter we bought two new positions and increased our holdings in nine existing stocks.

Dechra Pharmaceuticals PLC is a U.K.-based $2.7 billion market cap company that develops, manufactures, and sells specialty veterinary pharmaceuticals. The company is the 10th largest animal veterinary company in the world with approximately $400 million in fiscal year 2018 sales. Its largest markets are in the U.K. and U.S.; it has a direct sales and marketing presence in 24 countries, with distributor partnerships in 50 other countries.

We are bullish on the $31 billion animal health market, which is experiencing positive secular trends, with a 5%-to-6% CAGR driven by humanization of pet health care and the increasing demand for animal protein. We believe that Dechra, with an approximate 2% share, is well positioned to continue to outperform through its focus on niche end markets that are underserved by large pharma. It focuses on animal endocrinology, dermatology, ophthalmology, analgesics, and equine. Roughly 90% of Dechra sales are generated from their key strategic therapy areas.

We think Dechra can sustain top-line organic growth of around 10%, supplemented by a healthy dose of acquisitions. Dechra had completed over a dozen deals since 2010, which have served to expand its geographic footprint and product lines. Recent significant transactions include the transformative 2016 $200 million acquisition of Putney, a leading developer of companion animal drugs, which brought Dechra into the U.S. and the early 2018 $422 million acquisition AST/LeVet, which strengthened Dechra's European portfolio and brings significant sales synergies.

Dechra has multiple areas for growth. While about 65% of its sales are related to the higher value, non-commoditized companion animal market, it is still under-indexed in Farm Animal Products (FAP), which represents 60% of the global animal pharmaceutical market. It is also less geographically diverse than its global competitors. The company has been pursuing a successful land and expand strategy, entering attractive new geographic markets such as Mexico and Brazil. Lastly, there is Dechra's pipeline comprised of 75+ products estimated to be worth $140 million risk adjusted at peak sales. We expect most of these to launch over the next five years, helping to support our outlook for low double-digit top-line growth for the next several years. Further, the animal health market is undergoing consolidation, and while not part of our immediate investment thesis, we believe Dechra would be an attractive acquisition target for a larger animal pharmaceutical company, particularly given its heavier mix of higher value companion animal drugs.

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

	Year Acquired	Market Cap When Acquired (billions)	Quarter End Market Cap or Market Cap When Sold (billions)	Amount Sold (millions)
LiveRamp Holdings, Inc.	2013	$1.6	$ 2.6	$33.0
FleetCor Technologies, Inc.	2010	1.8	24.1	30.3
Bright Horizons Family Solutions, Inc.	2013	1.8	6.5	20.4
Teladoc Health, Inc.	2017	1.8	3.5	16.1
Liberty Expedia Holdings, Inc.	2016	2.4	2.3	14.1

During the quarter, we exited our positions in **FleetCor Technologies, Inc.**, **Liberty Expedia Holdings, Inc.**, and **REV Group, Inc.** The first two were good stocks for the Fund that we sold at full valuations. The latter has a business that was severely hurt by tariffs, and we were concerned that the business could remain under pressure for some time, so sold at a loss.

We reduced our **LiveRamp Holdings, Inc.** position by a third by participating in the company's dutch auction and were able to properly resize our position and get a good price in the sale. We trimmed a bunch of other existing holdings, mostly stocks that held up in the quarter (**Bright Horizon Family Solutions, Inc.** and Mettler-Toldeo International, Inc.) or stocks that had risen a lot earlier in the year (**Teladoc Health, Inc.**, Wingstop Inc., and The Trade Desk).

Outlook

It was very painful to have our success for the year all be reversed in the fourth quarter. Markets are fickle and sometimes unkind. Whenever stocks plunge, we do our best to remain calm and analytical, and we consider if the decline in stocks is a harbinger of deterioration in fundamentals or just an emotional sell-off. In this case, we side on the latter.

It is our view that the market environment is actually pretty favorable as of now. We believe business is pretty good and that recession is not nearby. We think stocks are cheap and that the market leaders coming into the downturn will likely resume leadership on the flip side. This is premised on our belief that cooler heads will prevail, that irrational political behavior will not upset economic conditions, and fundamentals will again reassert themselves as the guiding factor for stock valuation.

The positives are:

- Interest rates have fallen significantly, down over 50 basis points on the 10-year bond.
- The Federal Reserve has changed its stance and now professes "patience" and "flexibility." U.S. balance sheet normalization is no longer on autopilot, and all "appropriate tools" would be used in case of crisis.
- Stocks are much cheaper. The market is trading at about 15 times projected earnings. We believe our holdings are now inexpensive on our near-term projections and offer great upside as we look out even further.
- The economy is doing just fine, as evidenced by the latest jobs report, which was a gangbuster. Though we do expect lower growth in GDP and corporate earnings in 2019 versus last year, we still think growth will be respectable.
- The U.S. dollar is lower, which is good for earnings translations.
- Market sentiment is awful, which is good for stocks.
- China and the U.S. are presently at an impasse with respect to the trade war, but there is hope that the dispute with China gets settled over the near term.

Offsetting these positives, are:

- Trade issues with China are not settled, and if additional tariffs are to be enforced or tensions escalate, we would expect a major negative shift in sentiment and a significant negative impact to growth.
- U.S. corporate debt levels are higher, and liquidity is lower, which could lead to higher borrowing costs and some refinancing risk. Corporate credit spreads widened late in the year.

- The U.S. government deficit increased as the budget ran a deficit even after the past year of strong economic growth. Higher rates could result if these imbalances are deemed fiscally irresponsible.
- Trump is a wild card, especially with the new Democratic Congress and the findings of the Mueller probe in the offing.
- The market's structural issues, that helped exaggerate the sell-off in the last quarter, might augur lower multiples.
- Fourth quarter results and guidance might be muted because of slowing economic conditions at the end of 2018 and uncertainty about pending tariffs. We expect growth to improve over the year.

As the year begins, the market has been bouncing back from oversold conditions. Fear is residing with trade tensions easing and early upbeat earning reports. Market leadership has returned to high-quality growth companies and small caps are outperforming large caps.

We believe we are well positioned and own a portfolio of what we believe are terrific businesses. We own:

- Companies that are leaders in their sectors and are often disrupting those industries while strengthening their competitive position.
- Companies that have great business models, with visible, recurring, and sustainable revenues and cash flows.
- Companies run by sharp, often founding executives, who have proven track records of success, and are of high character.
- Stocks that now trade at reasonable valuations on this year's estimates and offer great upside as earnings compound over time and/or multiples expand to recognize the special qualities of these businesses.

Our approach to invest primarily in these high-quality companies has served us well in the past. We supplement these holdings with a smattering of situational investments that we believe offer great near-term upside. We have a strong group of analysts and fund managers all focused on this same approach working together to uncover great investments, and believe the Fund is laden with such. Hopefully, the market we experienced in the fourth quarter is behind us, and we can get back to making good returns for all.

Thanks for investing with us.

Cliff Greenberg
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: 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.

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