Dear Baron Real Estate Fund Shareholder:

Performance

We are pleased to report that *Barron's*, the highly regarded weekly business magazine, recently profiled Baron Real Estate Fund® and Baron Real Estate Income Fund® in an interview that was published on June 29, 2023. A link to the article, titled *"Real Estate Stock Swoon Is a 'Gift' to Investors, This Manager Says"* can be accessed on our Baron website homepage at www.baronfunds.com in the "News & Events" section.

In the first six months of 2023, Baron Real Estate Fund (the Fund) appreciated 15.00% (Institutional Shares), outperforming the MSCI USA IMI Extended Real Estate Index (the MSCI Real Estate Index), which increased 12.11%, and the MSCI US REIT Index (the REIT Index), which increased 4.78%.

The Fund increased 7.41% in the second quarter of 2023, modestly outperforming the MSCI Real Estate Index, which increased 7.04%, and beating the REIT Index, which rose 2.34%.

As of June 30, 2023, the Fund has maintained its:

- **#1 real estate fund ranking for each of its 10-year, 5-year, and 1-year performance periods**
- **5-Star Morningstar Rating™ for each of its 10-year, 5-year, and 3-year performance periods**
- **5-Star Overall Morningstar Rating™**

JEFFREY KOLITCH
PORTFOLIO MANAGER

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

We will address the following topics in this letter:

- Our current top-of-mind thoughts
- Portfolio composition and key investment themes
- Top contributors and detractors to performance
- Recent activity
- Concluding thoughts on the prospects for real estate and the Fund

As of 6/30/2023, the Morningstar Ratings™ were based on 230, 211, 151, and 230 share classes for the 3-year, 5-year, 10-year, and Overall periods, respectively. The Baron Real Estate Fund received 5 stars for each period. The Morningstar Ratings are for the Institutional Share Class only; other classes may have different performance characteristics. The Morningstar Ratings are based on the Morningstar Risk-Adjusted Return measures.

As of 6/30/2023, the Morningstar Real Estate Category consisted of 254, 230, 211, and 151 share classes for the 1-, 3-, 5-, and 10-year periods. Morningstar ranked Baron Real Estate Fund Institutional Share Class in the 1st, 1st, 1st, and 1st percentiles, respectively. On an absolute basis, Morningstar ranked Baron Real Estate Fund Institutional Share Class as the 1st, 3rd, 1st, and 1st best performing share class in its Category, for the 1-, 3-, 5-, and 10-year periods, respectively.

As of 6/30/2023, Morningstar ranked Baron Real Estate Fund R6 Share Class in the 1st, 1st, and 1st percentiles, for the 1-, 3-, and 5-year periods, respectively. On an absolute basis, Morningstar ranked Baron Real Estate Fund R6 Share Class as the 1st, 2nd, and 2nd best performing share class in its Category for the 1-, 3-, and 5-year periods, respectively.

Morningstar calculates the Morningstar Real Estate Category Average performance and rankings using its Fractional Weighting methodology. Morningstar rankings are based on total returns and do not include sales charges. Total returns do account for management, administrative, and 12b-1 fees and other costs automatically deducted from fund assets.

The **Morningstar Rating™** for funds, or "star rating", is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The Morningstar Rating does not include any adjustment for sales loads. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10- year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods.

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Baron Real Estate Fund

Table I.
Performance
Annualized for periods ended June 30, 2023

	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]
Three Months[3]	7.31%	7.41%	7.04%	2.34%
Six Months[3]	14.82%	15.00%	12.11%	4.78%
One Year	15.86%	16.17%	15.79%	(1.38)%
Three Years	12.06%	12.35%	11.90%	7.67%
Five Years	11.38%	11.67%	7.30%	3.34%
Ten Years	10.53%	10.82%	8.86%	5.10%
Since Inception (December 31, 2009) (Annualized)	13.31%	13.60%	10.73%	7.82%
Since Inception (December 31, 2009) (Cumulative)[3]	440.52%	459.45%	296.08%	176.48%

Our Current Top-of-Mind Thoughts

At the halfway point of 2023, our current top-of-mind thoughts can be summarized as follows:

We remain optimistic about the prospects for the stock market, public real estate securities, and the Baron Real Estate Fund.

- As noted in our year-end 2022 shareholder letter, we continue to believe that 2023 may ultimately emerge as a mirror image of 2022 in that many of the headwinds of 2022 reverse course (e.g., multi-decade high inflation and rising interest rates) and become tailwinds in 2023, thereby contributing to solid full-year returns.
- We are bullish looking out two to three years.

We do not believe that a commercial real estate crisis is on the horizon.

- We believe forecasts of widespread distress in commercial real estate are sensationalized and unlikely to materialize.
- In our opinion, a commercial real estate crisis is unlikely for the following reasons:
  - Most of commercial real estate is performing well (e.g., industrial, multi-family, data centers, senior housing, self-storage).
  - New construction activity has been and is expected to remain low. The dearth of new real estate construction activity compares favorably with prior real estate cycles when overbuilding of real estate contributed to a deterioration in real estate business prospects.
  - Balance sheets are generally in strong shape (appropriate leverage levels, staggered debt maturities, the mix of fixed versus floating rate debt).
  - The banking system is in a strong capital position. We expect future challenges for banks to be, in most cases, an earnings issue (higher deposit rate requirements and less lending) rather than a solvency issue (most banks are appropriately capitalized).
  - We believe future loan defaults will be mostly isolated to class "B" and "C" office buildings. Better bank loan underwriting practices and the increase in commercial real estate values over the last decade should mute the loan loss cycle.

The valuations of several real estate-related companies remain cheap.

- A good portion of public real estate – including both REITs and non-REIT real estate-related companies – is attractively valued relative to historical averages.
- Currently, several public REITs and non-REIT real estate-related securities are meaningfully discounted relative to private real estate alternatives.

We continue to believe the near-term and long-term prospects for real estate in the public markets are compelling.

- *Near-term case for real estate*
  - The share prices of several real estate companies have lagged in part due to the aggressive Federal Reserve interest rate tightening cycle, and, more recently, the commercial real estate crisis narrative.

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, 2022 was 1.33% and 1.07%, 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 may reimburse certain Fund expenses pursuant to a contract expiring on August 29, 2033, unless renewed for another 11-year term and the Fund's transfer agency expenses may be reduced by expense offsets from an unaffiliated transfer agent, without which performance would have been lower. Current performance may be lower or higher than the performance data quoted. For performance information current to the most recent month end, visit www.BaronFunds.com or call 1-800-99BARON.

[1] The **MSCI USA IMI Extended Real Estate Index Net (USD)** is an unmanaged custom index calculated by MSCI for, and as requested by, BAMCO, Inc. The index includes real estate and real estate-related GICS classified 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 Net (USD)** 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. MSCI is the source and owner of the trademarks, service marks and copyrights related to the MSCI Indexes. The indexes and the Fund include reinvestment of dividends, net of foreign withholding taxes, which positively impact the performance results. The indexes are unmanaged. Index performance is not Fund performance; one cannot invest directly into an index.

[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.

- Several real estate companies have repriced for a higher cost of capital and expectations of slowing growth.
- Several real estate companies are cheap.
- The current real estate environment is far superior relative to prior real estate cycles for two key reasons: first, in most cases, the use of debt has been disciplined relative to history; second, commercial and residential real estate are not overbuilt, and expectations for new supply are not concerning.
- We believe substantial private capital is in pursuit of public real estate because private funds can buy quality public real estate at a discount relative to private real estate.
- We continue to believe the Fund's two- to three-year return prospects are compelling with a favorable upside/downside return ratio.

• *Long-term case for real estate*

- Real estate has generated solid historical long-term returns, and we believe it can continue to do so. For the 25-year period ended June 30, 2023, U.S. equity REITs have delivered a better cumulative return than the S&P 500 Index, fixed income alternatives, international equities, and commodities. Since the Fund's inception on December 31, 2009 through June 30, 2023, Baron Real Estate Fund, which owns REITs and non-REIT real estate-related companies, has delivered a cumulative return of 459%, which compares favorably to the 176% return of the REIT Index.
- Real estate continues to offer diversification benefits. According to Morningstar, over the last 25 years through June 30, 2023, REITs have provided diversification benefits due to their modest correlation to stocks (0.64 correlation to the S&P 500 Index) and low correlation to bonds (0.27 correlation to Bloomberg Barclays U.S. Aggregate Index).
- Real estate may provide inflation protection. Real estate owners with short-lease durations in supply-constrained markets are well equipped to raise rents to combat inflation's impact on their businesses.

Portfolio Composition and Key Investment Themes

We currently have investments in REITs, plus seven additional non-REIT real estate-related categories. Our percentage allocations to these categories vary, and they are based on our research and assessment of opportunities in each category on a bottom-up basis (See Table II below).

Table II.
Fund investments in real estate-related categories as of June 30, 2023

		Percent of Net Assets
REITs		27.2%
Non-REITs		70.0
Homebuilders & Land Developers	18.1	
Casinos & Gaming Operators	14.6	
Building Products/Services	11.5	
Real Estate Operating Companies	10.6	
Real Estate Service Companies	10.1	
Hotels & Leisure	4.7	
Tower Operators	0.4	
Cash and Cash Equivalents		2.8
Total		100.0%*

* *Individual weights may not sum to the displayed total due to rounding.*

Investment Themes

We continue to prioritize four long-term high conviction investment themes or real estate categories:

1. REITs
2. Residential-related real estate
3. Travel-related real estate
4. Other real estate-related opportunities

REITs

Since the Fund's inception on December 31, 2009, REITs have been an important part of our real estate-related portfolio. We have tended to limit our REIT allocation to 25% to 35% of the portfolio so that the Fund is differentiated from other REIT funds.

Following a 25% correction in the REIT Index in 2022 and ongoing relative underperformance in the first six months of 2023, we believe valuations of several REITs are attractive. Business fundamentals and prospects for many REITs remain solid although slower growth is expected in 2023. Balance sheets are in good shape. Several REITs have inflation-protection characteristics. Dividend yields are well covered by cash flows and are growing.

Should the contraction in economic growth evolve into no worse than a mild recession and the path of interest rates peaks in 2023 at levels not much higher than current rates, we believe the shares of certain REITs may perform relatively well given the contractual nature of cash flows that provide a high degree of visibility into near-term earnings growth and dividend yields. Should long-term interest rates begin to decline and credit spreads compress, REIT return prospects may also benefit from an improvement in valuations as valuation multiples expand (e.g., capitalization rates compress).

We continue to prioritize secular growth REITs and short-lease duration REITs with pricing power:

Secular growth REITs: Our long-term focus remains on real estate companies that benefit from secular tailwinds where cash-flow growth tends to be durable and less sensitive to a slowdown in the economy. Examples include our investments in industrial logistic, data center, and wireless tower REITs.

Short-lease duration REITs with pricing power: We have continued to emphasize REITs that are able to raise rents and prices on a regular basis to combat inflation's impact on their businesses. Examples include our investments in self-storage and single-family rental REITs.

For a more detailed discussion of the investment case for REITs and the various REIT categories, we encourage you to read our June 30, 2023 Baron Real Estate Income Fund shareholder letter.

As of June 30, 2023, we had investments in six REIT categories representing 27.2% of the Fund's net assets. Please see Table III below.

Table III.
REITs as of June 30, 2023

	Percent of Net Assets
Industrial REITs	11.1%
Data Center REITs	6.1
Self-Storage REITs	4.2
Wireless Tower REITs	2.1
Health Care REITs	2.0
Single-Family Rental REITs	1.6
Total	27.2%[1]*

[1] Total would be 27.6% if included wireless tower operator Cellnex Telecom S.A.
* *Individual weights may not sum to the displayed total due to rounding.*

Residential-related real estate

We remain bullish on the prospects for the U.S. housing market. The multi-decade structural underinvestment in the construction of residential real estate relative to the demographic needs of our country bodes well for long-term housing construction activity, sales, rentals, pricing, and repair and remodel activity.

We agree with the findings of housing-related research reports published by *Evercore ISI Research*. In a report on October 4, 2022, Evercore cited the constrained inventory of the U.S. housing market:

> "After briefly reaching above 2 million total (housing) starts way back in 2005, the U.S housing industry entered the longest sustained period of under-building since the modern homebuilding industry began in the late 1940s. On a trailing fifteen-year basis, housing starts have averaged just over 1 million annually, well below the industry's 1.5 million long-term average. Since housing starts include both for-sale and rental units, this accumulated shortfall is visible in both record low levels of existing homes for sale and rental vacancy rates. And just as this deficit was more than a decade in the making, it cannot dissipate quickly."

In a more recent report on May 18, 2023, Evercore said:

> "…We do not have enough houses in the country, due to 15 years of under-building…It would take a decade of 2 million (annual) housing starts to make up the deficit."

Long-term housing-related demand prospects are also encouraging, especially from the approximately 72 million millennials – ages 25 to 40 – many of whom have been looking to buy or rent a home. Millennials are the largest generation in the workforce, their wages are increasing, and their multi-year delay of household formation is reversing. There are clear signs that millennials are debunking the view that the American Dream to own or rent a home is over.

The large imbalance between pent-up housing demand and low construction levels bodes well, long term, for new single-family home purchases. It also bodes well for home and apartment rentals.

Please see "Top contributors and detractors to performance" and "Recent activity" later in this letter. There, we discuss various homebuilder and residential building product/services companies and explain the rationale for recent performance, purchases, and sales.

As of June 30, 2023, residential-related real estate companies represented 29.6% of the Fund's net assets. Please see Table IV below.

Table IV.
Residential-related real estate companies as of June 30, 2023

	Percent of Net Assets
Homebuilders	16.5%
Building Products/Services	10.2
Home Centers	3.0
Total	29.6%[1]*

[1] Total would be 31.3% if included residential-related housing REIT Invitation Homes, Inc.
* *Individual weights may not sum to the displayed total due to rounding.*

Travel-related real estate

We remain long-term bullish about the prospects for travel-related real estate companies.

In our opinion, several factors are likely to contribute to multi-year tailwinds for travel including a favorable shift in consumer preferences, a growing middle class, and other encouraging demographic trends.

Even though travel-related business conditions may moderate in the year ahead given the likelihood of an economic slowdown, which would negatively impact leisure spending and business travel, we maintain an allocation to select travel-related real estate companies because **we believe the long-term investment case for travel is compelling**:

- *Demand for services over goods:* We have seen an increased wallet share going to travel. The 72 million millennials are increasingly driving this shift aided by their preference for experiences, such as travel, over durable goods.
- *Demographic trends:* Delays in marriage and having children have led to the millennial cohort having more disposable income than prior generations at this age.
- *Work-from-home:* Flexible job arrangements have led to an increase in travel bookings and lengths of stay, leading to the emergence of a new category of travel (hush trips).
- *Certain travel-related businesses remain cyclically depressed, not secularly challenged, and should rebound as economic strength re-emerges.* For example, the business operations of Macau-centric casino and gaming companies such as **Wynn Resorts, Limited** and **Las Vegas Sands Corporation** have yet to fully recover from COVID-19 restrictions and challenges in China from 2020 through 2022. We expect business to rebound sharply when economic growth recovers just as it did in Las Vegas.
- *Healthy balance sheets:* The travel-related real estate companies we invest in maintain well-capitalized and liquid balance sheets and should be able to comfortably withstand any slowdown in economic growth just as they did during the early days of COVID-19.
- *Private equity companies such as Blackstone have a long history of investing in travel-related companies and have continued to highlight the travel segment as an important investment opportunity.* Given the highly discounted share prices and valuations of certain travel-related companies, we would not be surprised if private equity firms take advantage of the favorable valuation arbitrage between the public and private markets and acquire public travel companies.

As of June 30, 2023, travel-related real estate companies represented 19.3% of the Fund's net assets. Please see Table V below.

Table V.
Travel-related real estate as of June 30, 2023

	Percent of Net Assets
Casinos & Gaming Operators	14.6%
Hotels	2.1
Timeshare Operators	1.6
Ski Resorts	0.9
Total	19.3%*

* *Individual weights may not sum to the displayed total due to rounding.*

Other real estate-related opportunities

Our *other real estate-related opportunities* category includes companies that do not fit neatly in more traditional real estate categories of REITs, residential-related real estate, and travel-related real estate. They currently include:

- Commercial real estate services companies
  Examples: **CBRE Group, Inc.** and **Jones Lang LaSalle Incorporated**
- Real estate-focused alternative asset managers
  Examples: **Brookfield Corporation** and **Blackstone Inc.**
- Real estate data analytics/property technology companies
  Example: **CoStar Group, Inc.**

Commercial real estate services companies: We remain bullish on the long-term growth opportunity for the commercial real estate brokerage category because of structural and secular tailwinds that should benefit leading global companies such as CBRE and Jones Lang LaSalle.
Tailwinds include:

- *The outsourcing of commercial real estate:* A growing number of companies are increasingly looking to outsource their commercial real estate needs. CBRE estimates that the overall facilities management market will be $1.9 trillion by 2024, representing a massive growth opportunity for large global commercial real estate services companies.
- *The institutionalization of commercial real estate:* Institutional allocations to real estate continue to increase, in part due to real estate's diversification, inflation protection, and relatively stable long-term growth attributes.
- *Opportunities to increase market share:* The commercial real estate industry remains highly fragmented and is likely to continue to consolidate. Customers tend to prefer commercial real estate companies that can provide a broad set of services. We believe CBRE and Jones Lang LaSalle are best positioned to drive market share gains given that they are the clear #1 and #2 commercial real estate services firms, respectively, and they have the capability to provide the full array of real estate offerings on a global scale.

CBRE and Jones Lang LaSalle have scale, product breadth, and leadership positions across their diversified real estate business segments. They continue to gain market share and are well positioned to capitalize on ample attractive acquisition opportunities in the years ahead given strong and liquid balance sheets. Though growth in certain segments of their businesses has slowed and is likely to remain under pressure in the months ahead due to the global economic slowdown, higher interest rates, and the likelihood of more restrictive bank lending, we believe both are attractively valued and present compelling return potential over the next few years.

Real estate-focused alternative asset managers: We are optimistic about the long-term prospects for Brookfield and Blackstone because we believe both companies are likely to increase market share in a secular growth opportunity for alternative assets.

Institutional allocations to alternative investment assets such as real estate, infrastructure, and private equity are likely to continue to grow significantly in the years ahead because alternatives have a long track record of generating attractive relative and absolute returns with less volatility than several other investment options.

We are bullish on the long-term prospects for Brookfield and Blackstone. Both companies are led by exceptional management teams that attract and retain exceptional talent. They are two of the largest real estate managers in the world with impressive investment track records. Both Brookfield and Blackstone have global franchises, strong brands, and loyal customers.

We believe the shares of both companies are attractively valued and are optimistic about the long-term potential for the Fund's investments in both companies.

Real estate data analytics/property technology companies: The real estate industry, which represents approximately 17% of U.S. GDP according to the National Association of Realtors, has eschewed decades of technological innovation while many other industries have evolved rapidly. We are seeing evidence of that trend beginning to change as real estate companies are increasingly adopting technology as a source of competitive differentiation and evolution across property sectors.

This collision of real estate and technology has led to a new category within real estate–real estate technology, also referred to as *proptech*. Proptech businesses use technology and software to assist in meeting real estate needs.

The emergence of proptech and the digitization of real estate is an exciting and promising new development for real estate. We believe we are in the early innings of a technology-driven investment cycle centered on data and digitization that allows real estate-related businesses to drive incremental revenue streams and lower costs.

CoStar, the leading provider of information, analytics, and marketing services to the real estate industry and a top holding in the Fund, is well positioned to capitalize on this burgeoning secular growth trend.

As of June 30, 2023, other real estate-related companies represented 20.7% of the Fund's net assets. Please see Table VI below.

Table VI.
Other real estate-related companies as of June 30, 2023

	Percent of Net Assets
Real Estate-Focused Alternative Asset Managers	10.6%
Commercial Real Estate Services Companies	5.3
Real Estate Data Analytics Companies	4.8
Total	20.7%*

* *Individual weights may not sum to the displayed total due to rounding.*

Top Contributors and Detractors to Performance

Table VII.
Top contributors to performance for the quarter ended June 30, 2023

	Quarter End Market Cap (billions)	Percent Impact
Toll Brothers, Inc.	$ 8.6	2.30%
CoStar Group, Inc.	36.4	1.23
Lennar Corporation	35.6	0.78
D.R. Horton, Inc.	41.5	0.75
SiteOne Landscape Supply, Inc.	7.5	0.42

Our investments in homebuilder companies – **Toll Brothers, Inc.**, **Lennar Corporation**, and **D.R. Horton, Inc.** – performed well in the first six months of 2023. The share price of Toll Brothers increased nearly 60% and the shares prices of Lennar and D.R. Horton each gained more than 35%.

Year-to-date, each company has witnessed a meaningful uptick in demand to buy homes:

- Home buyers continue to come off the sidelines and buy homes despite 30-year mortgage rates remaining in the 6.5% to 7.0% range. Several factors are contributing to the recent strength, including pent-up demand to buy homes and fears that mortgage rates could move higher.
- The sticker shock of rapidly rising mortgage rates appears to have cooled down. Homebuilders have made homes more affordable to prospective home purchasers by offering mortgage rate buydowns to the mid-5% mortgage rate range while maintaining strong profitability margins.
- A dearth of inventory in the existing home market and an overall housing supply shortage is driving home buyers to “stretch their wallet” due to fears that they could miss the opportunity to buy a home.

We remain optimistic about the long-term potential for the Fund’s investments in Toll Brothers, Lennar, and D.R. Horton for several reasons including:

- Housing supply shortages and pent-up demand to buy homes should lead to several years of strong home production.
- Each homebuilder is well positioned to increase market share because: (i) many of their competitors are private homebuilders that are capital constrained and lack comparable access to materials, labor, and land; and (ii) activity in the existing home sale market may remain subdued if many homeowners continue to choose to stay in their homes due to low in-place mortgages. According to *Goldman Sachs*, 72% of borrowers have a mortgage rate at or below 4%.
- Toll Brothers, Lennar, and D.R. Horton have scale advantages that help each company procure materials, labor, and land more easily and at more favorable prices than many of their competitors.

Regarding share price return prospects for our homebuilder investments:

- Should homebuilder valuations remain in their historical valuation range, we believe the Fund’s homebuilder investments have the potential to continue to generate strong annual performance returns given our expectation for durable long-term earnings growth and, in some cases, an improvement in valuation multiples. This is our base case valuation assumption.
- We believe, however, there is a compelling case for a favorable paradigm shift in how homebuilding companies are valued in the public markets. Why?
  - Since the beginning of 2020, Toll Brothers, Lennar, and D.R. Horton have demonstrated substantial resilience and operating prowess. Despite several black swan events – COVID-19, a sharp increase in mortgage rates from 3% to 7%, and supply-chain disruptions – each company has managed its business exceptionally well and demonstrated that the demand to buy homes is resilient. Further, each company maintains a well-capitalized and liquid balance sheet, focuses on generating strong profitability margins, free cash flow and returns on equity, and has an opportunity to generate strong long-term earnings growth.
  - Homebuilding companies tend to be valued in the public market at a price-to-book value per share multiple of approximately 1 to 2 times book value. This compares to the S&P 500 Index average book value since 2000 of approximately 3 times (minimum book value of 1.78 times and maximum book value of 5.06 times). Similarly, homebuilding companies have tended to be valued in the public market at steep discounts (often 5 to 10 times earnings per share) to the long-term average S&P 500 Index P/E multiple of 17 times earnings per share.
  - If a paradigm shift in valuation multiples materializes due to the reasons cited above, and homebuilder valuations re-rate structurally higher – closer to an S&P 500 Index valuation – the long-term share price return potential for our homebuilder companies would become notably compelling.

Shares of **CoStar Group, Inc.** increased 29.3% in the second quarter of 2023. We believe the shares performed well due to growing optimism about the prospects for the company’s planned expansion into the residential market and improved sentiment for certain technology-centric companies such as CoStar.

CoStar is the leading provider of information, analytics, and marketing services to the real estate industry. CoStar initially focused on serving the domestic commercial real estate industry and built a comprehensive proprietary database of essential data to help participants buy, sell, and lease properties. The company has since expanded its focus to offer products and services to multi-family, industrial, commercial land, mixed-use and hospitality end-markets across North America and Western Europe.

Today, the company’s non-residential operations generate over $2 billion of recurring revenue with cash flow (EBITDA) margins above 40%. We expect this portion of the business to grow its revenue at a mid-teens rate for several years as the company launches new products, upsells existing customers, and raises prices. We expect profit and cash flow to grow at an even faster rate given the low marginal costs inherent in CoStar’s business model. We think that cash flow from this business can double over the next five years, which implies a similar return for the stock.

The company undertook an audacious expansion plan and invested approximately $230 million in 2022 to enter the domestic residential real estate market. We believe management’s initial 2023 guidance included a $500 million investment in its residential business. We suspect that management set expectations conservatively and is unlikely to spend the

full $500 million, leading to likely earnings upside over the year. Notwithstanding our view of management's conservatism, we believe CoStar's residential investment is nominal relative to the company's $4 billion net cash balance and its ability to generated free-cash-flow. We think that the residential market is vast, and that CoStar is well positioned to build a compelling and differentiated business serving this market. If successful, we think that CoStar could generate almost $1 billion of incremental revenue over the next 5 to 10 years at 40% EBITDA margins. If unsuccessful, CoStar can easily throttle back on its investment and redeploy resources towards other markets without having impacted the fundamentals of its non-residential business.

Based on its current valuation and our expectation for future growth, we believe CoStar's shares have the potential to double in the next three to four years.

Table VIII.
Top detractors from performance for the quarter ended June 30, 2023

	Quarter End Market Cap (billions)	Percent Impact
Rexford Industrial Realty, Inc.	$11.2	–0.48%
Extra Space Storage Inc.	20.1	–0.21
Wynn Resorts, Limited	12.0	–0.21
Marriott Vacations Worldwide Corporation	4.5	–0.15
Caesars Entertainment, Inc.	11.0	–0.14

Following solid share price performance in the first three months of 2023, the shares of **Rexford Industrial Realty, Inc.**, a high-growth REIT that owns a $12 billion portfolio of infill industrial real estate properties concentrated in Southern California, declined in the second quarter primarily due to concerns that demand and rent growth are moderating in Southern California.

Since the beginning of 2020 through March 31, 2023, rents in Rexford's markets have increased more than 100%! Though we do expect rent growth to moderate from its frenzied pace of the last few years, we remain optimistic about the long-term prospects for Rexford and the Fund's other industrial REIT holdings **Prologis, Inc.**, **EastGroup Properties, Inc.**, and **Terreno Realty Corporation**.

With industrial vacancies at less than 4%, new supply expected to moderate in 2024, rents on in-place leases at more than 50% below market rents, and multi-faceted demand drivers including the ongoing growth in e-commerce and companies' seeking to improve inventory supply-chain resiliency, we believe the Fund's industrial REIT investments are uniquely positioned and have compelling multi-year cash-flow growth runways.

We believe that Rexford has one of the best long-term growth opportunities among all publicly traded REITs. The company has two significant prongs for long-term growth. First, the management team has an irreplaceable portfolio of 44 million square feet of industrial real estate and its in-place rents on signed leases are 66% below market. As such, the company has line of sight to at least 66% growth as it adjusts rents up to market levels over the next four to five years. Second, Rexford's management team is pursuing acquisitions of additional square footage within its 250 million square foot market. Through acquisitions, we believe management will significantly increase the size of its portfolio over time. Many of the industrial properties that Rexford is targeting are industrial real estate assets owned by individuals who have managed their real estate passively for decades; in many cases they have not increased rents consistently. That is the opportunity for Rexford – acquire assets, upgrade the properties, and begin to increase rents.

Following its pending merger with Life Storage, Inc. which is expected to close late in 2023, **Extra Space Storage Inc.,** a best-in-class self-storage REIT, will be the largest self-storage operator with a $46 billion self-storage operating portfolio. In the most recent quarter, the shares declined because rent growth is moderating from its strong pace of the last few years.

Though 2023 may be a transition year for Extra Space as growth retraces to a more sustainable run-rate and the management team prepares to incorporate Life Storage, we remain optimistic about the long-term prospects for the company and believe the current price of its shares reflects a good portion of this anticipated transition.

We believe Extra Space's management team is excellent. Over the last decade, management has delivered strong occupancy gains, rent growth, and expense control that has led to a cost-of-capital advantage relative to its peers. Management has capitalized on its cost-of-capital advantage relative to its peers by tripling its owned self-storage count since 2010. We believe the management team will continue to create tremendous value for shareholders and believe the long-term growth opportunity for the company remains strong.

After increasing 23% during the period held in the first quarter of 2023, the shares of **Wynn Resorts, Limited**, an owner and operator of hotels and casino resorts, modestly declined in the most recent quarter.

We remain optimistic about the multi-year prospects for the company. We believe the re-emergence of business activity in Macau will drive additional shareholder value. If cash flow returns to the level achieved in 2019 prior to COVID-19, we believe Wynn's shares will increase to $150 per share, or approximately 45% higher than where it has recently traded.

We believe additional drivers for future value creation beyond a re-emergence in Macau business activity include: (i) our expectation for long-term growth opportunities in the company's U.S.-centric markets of Las Vegas and Boston, including an expansion of Wynn's Encore Boston Harbor resort; (ii) Wynn's plans to develop an integrated resort in the United Arab Emirates with 1,500 hotel rooms and a casino that is similar in size to that of its Encore Boston Harbor; (iii) opportunities to improve cash-flow margins by rightsizing labor and achieving lower staff costs in Macau; (iv) the possibility that Wynn is granted a New York casino license in 2023; and (v) an expansion in the company's valuation multiple to levels achieved prior to the pandemic.

Recent Activity

Table IX.
Top net purchases for the quarter ended June 30, 2023

	Quarter End Market Cap (billions)	Net Amount Purchased (millions)
Digital Realty Trust, Inc.	$33.9	$25.6
Installed Building Products, Inc.	4.0	21.2
Equinix, Inc.	73.3	14.3
Hyatt Hotels Corporation	12.1	10.4
CBRE Group, Inc.	25.1	10.1

We believe the multi-year prospects for real estate data centers are highly compelling – perhaps as strong as they have ever been.

Accordingly, we recently increased the Fund's exposure to data center REITs by acquiring additional shares in **Equinix, Inc.** and re-initiating a position in **Digital Realty Trust, Inc.**

Data center landlords such as Equinix and Digital Realty are benefiting from record low vacancy, demand outpacing supply, more constrained power availability, and rising rental rates. Several secular demand vectors, which are currently broadening, are contributing to robust fundamentals for data center space globally. They include the outsourcing of information technology infrastructure, increased cloud computing adoption, the ongoing growth in mobile data and internet traffic, and artificial intelligence as a new wave of data center demand. Put simply, each year data continues to grow exponentially, and all of this data needs to be processed, transmitted, and stored – supporting increased demand for data center space. In addition, while it is still early innings, we believe artificial intelligence could not only provide a source of incremental demand but also further accelerate existing secular trends by driving increased prioritization and additional investment in digital transformation among enterprises.

We recently spent time with the management teams at both Equinix and Digital Realty and are optimistic about their prospects. We believe Equinix, the premier global operator of network-dense, carrier-neutral colocation data centers, is well positioned to grow its cash flow per share by more than 10% annually for the next few years.

Digital Realty is a global data center operator with 290 data centers across North America, EMEA, APAC, and LATAM. Over the last few years, the company has been undergoing a business transformation, which accelerated after its acquisition of Interxion in March 2020, a pure-play European network-dense data center operator. The company has been shedding non-core slower-growth assets, investing and expanding in Europe, growing its retail colocation business, improving its balance sheet, and adding operational expertise by supplementing new management leadership. We have spent a significant amount of time with CEO Andy Power over the years and believe the investments the company has made are on the cusp of bearing fruit and will pay dividends for years to come. In addition, we believe the fundamentals in its core business are at an inflection point with robust demand/bookings, pricing power, hyperscale cloud players outsourcing a higher percentage of their digital infrastructure needs, and limited competitive capacity. We believe these factors will lead to growth in the core business in 2023 and are optimistic about the long-term prospects for the company.

In the most recent quarter, we reacquired shares in **Installed Building Products, Inc.** (IBP), one of the nation's largest insulation installers for the residential new construction market. The company is also a diversified installer of complementary building products. IBP should be a prime beneficiary of growth in new home construction as approximately 77% of IBP's business is generated from new housing construction (67% new single-family and 10% new multi-family).

We believe the company has several opportunities for growth including:

(i) Expanding its approximately 30% market share of insulation for new residential construction organically by offering a superior customer experience;

(ii) Expanding its less than 10% market share of complementary building products by leveraging its established insulation footprint for cross-selling (complementary building products currently represent 34% of sales); and

(iii) Acquiring other businesses – IBP has a successful track record of acquiring and integrating more than 160 companies, realizing meaningful cost savings, and enhancing the growth and profitability of these acquired businesses.

We believe our investment in IBP has the potential to compound at 15% per year over the next few years.

Table X.
Top net sales for the quarter ended June 30, 2023

	Quarter End Market Cap or Market Cap When Sold (billions)	Net Amount Sold (millions)
Caesars Entertainment, Inc.	$ 11.0	$21.0
Fifth Wall Acquisition Corp. III	0.4	12.9
Prologis, Inc.	113.2	7.7
Hilton Worldwide Holdings Inc.	38.5	6.3
Floor & Decor Holdings, Inc.	11.0	6.0

In the most recent quarter, we reduced our investment in **Caesars Entertainment, Inc.**, the largest casino-entertainment company in the U.S. and one of the world's most diversified casino-entertainment providers. We chose to modestly reduce our significant exposure in travel-related real estate companies and reallocated the capital to other non-travel related real estate companies. We are big fans of CEO Tom Reeg and remain optimistic about the long-term prospects for the company.

In the most recent quarter, we redeemed for cash the Fund's investment in **Fifth Wall Acquisition Corp. III**, a blank check company that aims to acquire one or more real estate businesses and assets.

We recently modestly trimmed our large investment in **Prologis, Inc.**, the world's largest industrial REIT, and reallocated the capital to smaller positions in the Fund that we believe have compelling shareholder return prospects. We continue to believe the appreciation potential for the shares of Prologis remains compelling given that the company's rents on its in-place leases are more than 65% below current market rents, thus providing a strong runway for growth in the next three to five years.

Concluding Thoughts on the Prospects for Real Estate and the Fund

We remain optimistic about the prospects for the Fund because we believe we have assembled a portfolio of best-in-class competitively advantaged real estate companies with compelling long-term growth and share price appreciation potential. We have structured the Fund to capitalize on high conviction investment themes. Valuations and return prospects are attractive.

We continue to believe the benefits of our flexible approach, which allows us to invest in a broad array of real estate companies including REITs and non-REIT real estate-related companies, will shine even brighter in the years ahead.

For these reasons, we remain positive on the outlook for the Baron Real Estate Fund.

Table XI.
Top 10 holdings as of June 30, 2023

	Quarter End Market Cap (billions)	Quarter End Investment Value (millions)	Percent of Net Assets
Toll Brothers, Inc.	$ 8.6	$130.6	8.4%
Brookfield Corporation	55.2	98.0	6.3
Prologis, Inc.	113.2	84.0	5.4
CoStar Group, Inc.	36.4	74.6	4.8
Lennar Corporation	35.6	72.4	4.6
Equinix, Inc.	73.3	68.8	4.4
D.R. Horton, Inc.	41.5	54.7	3.5
Wynn Resorts, Limited	12.0	53.2	3.4
MGM Resorts International	16.0	52.8	3.4
Blackstone Inc.	109.2	50.8	3.2

I and the rest of our Baron real estate team – David Kirshenbaum, George Taras, and David Baron – remain energized, focused, and busy meeting with and speaking to real estate management teams. We continue our comprehensive research. We speak to a broad swath of real estate companies – both owned and not owned – in many cases a few times each quarter to make sure our research remains current. We believe our corporate relationships, access to management, and our real estate research are critical elements that contribute to competitive advantages for our real estate team versus many of our peers.

I, and our team, remain fully committed to doing our best to deliver outstanding long-term results, and I proudly continue as a major shareholder, alongside you.

Sincerely,

Jeffrey Kolitch

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 contain this and other information about the Funds. You may obtain them from the Funds' 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 as well as by interest rate fluctuations, credit risk, environmental issues and economic conditions. The Fund invests in companies of all sizes, including small and medium sized companies whose securities may be thinly traded and 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.

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

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

The portfolio manager defines "**Best-in-class**" as well-managed, competitively advantaged, faster growing companies with higher margins and returns on invested capital and lower leverage that are leaders in their respective markets. Note that this statement represents the manager's opinion and is not based on a third-party ranking. **Free cash flow (FCF)** represents the cash that a company generates after accounting for cash outflows to support operations and maintain its capital assets. **Price/Earnings Ratio (next 12-months)**: is a valuation ratio of a company's current share price compared to its mean forecasted 4 quarter sum earnings per share over the next twelve months. If a company's EPS estimate is negative, it is excluded from the portfolio-level calculation.

BAMCO, Inc. is an investment adviser registered with the U.S. Securities and Exchange Commission (SEC). Baron Capital, Inc. is a broker-dealer registered with the SEC and member of the Financial Industry Regulatory Authority, Inc. (FINRA).