

# Baron Fifth Avenue Growth Fund

## DEAR BARON FIFTH AVENUE GROWTH FUND SHAREHOLDER:

### PERFORMANCE

The first three months of 2012 were good to U.S. equity investors. The S&P 500 Index rose 12.59%, the Russell 1000 Growth Index increased 14.69% and the Baron Fifth Avenue Growth Fund (the "Fund") returned 22.69%. Relative to the Russell 1000 Growth Index, 75% of our outperformance came from alpha (stock selection). We undoubtedly benefited from a "Rising tides lifting all boats" environment.

A lot has been said and written about **Apple, Inc.'s** meaningful contribution (12.3% of S&P 500 Index and 18.4% of Russell 1000 Growth Index) to index returns. We are happy to report that as our largest investment (7.3% of the Fund on average during the quarter), Apple indeed was our largest contributor as well. The Fund's returns however, were broad based with four positions generating over 100 basis points each, 15 investments contributing between 50 and 100 basis points each, and only 2 out of 46 holdings declining in value during the first three months of the year.

The portfolio also benefited from an unsolicited takeover bid for one of our companies and from the only IPO that we chose to participate in, which performed well above our most optimistic expectations.

**Table I.**  
**Performance (Retail Shares)<sup>†</sup>**  
**Annualized for periods ended March 31, 2012**

|                                  | Baron Fifth Avenue Growth Fund <sup>1,2</sup> | S&P 500 Index <sup>1</sup> | Russell 1000 Growth Index <sup>1</sup> |
|----------------------------------|---|----------------------------|--|
| Three Months <sup>3</sup>        | 22.69%  | 12.59%                     | 14.69%                                 |
| One Year                         | 15.85%  | 8.54%                      | 11.02%                                 |
| Three Years                      | 23.93%  | 23.42%                     | 25.28%                                 |
| Five Years                       | 2.06%   | 2.01%                      | 5.10%                                  |
| Since Inception (April 30, 2004) | 4.95%   | 5.22%                      | 6.03%                                  |

Performance listed in the table is net of annual operating expenses. Annual operating expense ratio for the Retail Shares as of September 30, 2011 was 1.59%, but the net annual expense ratio is 1.30% (net of the Adviser's fee waivers). *The performance data quoted represents past performance. Past performance is no guarantee of future results. The investment return and principal value of an investment will fluctuate; an investor's shares, when redeemed, may be worth more or less than their original cost. The Adviser has reimbursed certain Fund expenses 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](http://www.BaronFunds.com) or call 1-800-99BARON.*

<sup>1</sup> The S&P 500 Index and the Russell 1000 Growth Index are unmanaged. The S&P 500 Index measures the performance of large cap U.S. equities in the stock market in general. The Russell 1000 Growth Index measures the performance of large U.S. companies classified as growth. The indexes and the Baron Fifth Avenue Growth Fund are with dividends, which positively impact the performance results.

<sup>2</sup> 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.

<sup>3</sup> Not annualized.



**ALEX UMANSKY**  
**PORTFOLIO MANAGER**

In January, the Swiss pharmaceutical giant, **Roche Holding AG**, made an all cash offer to acquire **Illumina, Inc.** for \$44.50 per share. While the stock contributed 110 basis points to our performance, we were less than thrilled with Roche's hostilities, firstly, because we thought the offer meaningfully undervalued Illumina's long term opportunities, and secondly, because we did not get a chance to build a full position. Illumina's Board of Directors has decided to fight the takeover at this price, which we believe is the correct course of action, and hence, we will not tender our shares. There is a good deal of uncertainty in this situation as Roche (or someone else) could offer a significantly higher price or the takeover could collapse all together. Should Roche walk away and no other bidder emerge, there is likely some downside to the stock, and we may get another chance at acquiring a full position. In any event, we will likely be discussing Illumina in our future letters.

**Table II.**  
**Top contributors to performance for the quarter ended March 31, 2012**

|                     | Quarter End Market Cap (billions) | Percent Impact |
|---------------------|-----------------------------------|----------------|
| Apple, Inc.         | \$558.9                           | 3.13%          |
| Equinix, Inc.       | 7.3                               | 1.38           |
| priceline.com, Inc. | 35.7                              | 1.24           |
| Illumina, Inc.      | 6.4                               | 1.10           |

We believe that over the last few years **Apple, Inc.** has transformed itself into a "platform" company and will continue to benefit from the "network effect" that is associated with this transformation. While the company's robust (unprecedented really, for its size) growth resulted in strong stock performance, its valuation contracted on every metric. It appears that investors continue to view Apple as a transactional company and compare the iPhone business, one of its main growth drivers, to Motorola's Razor or Research In Motion's BlackBerry, in other words, a company in the midst of a strong but unsustainable product cycle. We believe that the

breadth and depth of Apple's products – iTunes, AppStore, iCloud, eBooks, Siri, Facetime, in addition to the iPhones, iPads, and Macs, all seamlessly integrated, create a platform with strong brand loyalty and customer lock-in, suggesting a higher valuation is warranted.

**Equinix, Inc.** was up 55.3% in the quarter, as data-center business trends remained strong, and management began to explore converting the company's structure to a REIT. Comparable data-center REITs trade at dramatically higher multiples, and accordingly, investors have begun to revalue Equinix's shares to close that gap. We continue to see meaningful upside in the shares, through both further valuation expansion and sustained robust growth. (Rich Rosenstein)

**priceline.com, Inc.** is a leading online travel agency that operates several online sites including Booking.com, priceline.com, rentalcars.com, and agoda.com. Shares of priceline.com were up 53.4% in the quarter following the release of strong fourth-quarter results. We believe priceline is an exceptionally well-managed company addressing a large and rapidly growing market of global online travel. Priceline's penetration is still relatively low, particularly in the European and Asian markets giving it a significant opportunity for further market share gains and accelerating growth. (Ashim Mehra)

**illumina, Inc.** is the market leader in the genetic sequencing market. The stock appreciated 72.6% during the quarter. In January, 2012, Roche made an unsolicited offer to acquire all outstanding shares of Illumina for \$44.50 per share in cash. Illumina's Board of Directors recommended that shareholders reject Roche's offer. Illumina's stock is trading above the offer price, as investors expect Roche to raise its bid. We continue to believe genetic sequencing is on the verge of being broadly applied beyond research into clinical diagnostics and personalized medicine and that Illumina has the potential to experience significant growth. (Neal Kaufman)

**Table III.**  
Top detractors from performance for the quarter ended March 31, 2012

|                | Quarter End Market Cap (billions) | Percent Impact |
|----------------|-----------------------------------|----------------|
| Golar LNG Ltd. | \$ 3.0                            | -0.15%         |
| Google Inc.    | 209.4                             | -0.11          |

We initiated a position in **Golar LNG Ltd.**, which declined 11.4% during the period held. Golar is engaged in the transportation, trading, liquefaction and regasification of liquefied natural gas (LNG). The company owns, operates and charters LNG carriers and floating storage and regasification units. While worldwide supply of LNG has increased, shipyard manufacturing of LNG vessels bottomed in the last two years, creating a supply/demand imbalance that is driving steep rate increases on available vessels. We believe that the current valuation substantially undervalues Golar's unique assets, which include a fleet of 19 vessels. (Gilad Shany)

**Google, Inc.**, which was the single largest contributor to performance last quarter declined less than 1% in the first quarter. Google is a global leader in online search and advertising. Shares of Google underperformed when the company's mobile search capabilities generated less revenue than anticipated and fourth-quarter results came in below expectations. We believe, while an important opportunity for future growth, mobile is largely incremental to Google's core search business, which continues to be healthy. We continue to be positive on Google's long-term prospects and

find the current valuation especially attractive relative to the company's existing opportunity set. (Ashim Mehra)

**PORTFOLIO STRUCTURE**

The Fund's portfolio is constructed on a bottom-up basis with the quality of ideas and conviction level having the highest roles in determining the size of each individual investment. Sector weights tend to be an outcome of the portfolio construction process and are not meant to indicate a positive or a negative "view."

Relative to the Russell 1000 Growth Index, the Fund was overweight in Information Technology, Financials, and Consumer Discretionary and underweight in Energy, Consumer Staples, and Health Care. Just over 75% of "excess" returns came from stock selection, with the balance attributed to the allocation effect with the Fund generating excess returns across every sector with the exception of "cash," a scenario that is rather unlikely to be repeated.

**RECENT ACTIVITY**

We eliminated our holdings in **Hyatt Hotels Corp.**, **FactSet Research Systems, Inc.**, and **Starwood Hotels & Resorts Worldwide, Inc.** as we felt our other existing investments offered better risk/reward propositions for the long term. We believe all three companies continue to have good prospects and offer good values and they are still held by other Baron Funds. We ended the quarter with 43 holdings.

**Table IV.**  
Top net purchases for the quarter ended March 31, 2012

|                   | Quarter End Market Cap (billions) | Amount (millions) |
|-------------------|-----------------------------------|-------------------|
| Apple, Inc.       | \$558.9                           | \$1.6             |
| Wynn Resorts Ltd. | 12.6                              | 1.1               |
| Golar LNG Ltd.    | 3.0                               | 0.9               |
| Monsanto Co.      | 42.7                              | 0.9               |
| Google, Inc.      | 209.4                             | 0.7               |

**Table V.**  
Top net sales for the quarter ended March 31, 2012

|   | Quarter End Market Cap or Market Cap When Sold (billions) | Amount (millions) |
|---|---|-------------------|
| Hyatt Hotels Corp.                        | \$ 6.7  | \$-0.7            |
| FactSet Research Systems, Inc.            | 4.1   | -0.6              |
| Starwood Hotels & Resorts Worldwide, Inc. | 10.7  | -0.6              |

**OUTLOOK**

We continue to focus on identifying and investing in unique companies with sustainable competitive advantages that in our view, have the ability to reinvest capital at high rates of return. While we would not extrapolate the market's (or the Fund's) first quarter results, we are excited about the current portfolio and see many attractive opportunities we hope to take advantage of over the long term.

# Baron Fifth Avenue Growth Fund

Table VI.

Top 10 holdings as of March 31, 2012

|                     | Quarter End<br>Market<br>Cap<br>(billions) | Quarter End<br>Investment<br>Value<br>(millions) | Percent of<br>Net Assets |
|---------------------|--|--|--------------------------|
| Apple, Inc.         | \$558.9                                    | \$4.6  | 8.1%                     |
| Google, Inc.        | 209.4                                      | 2.7  | 4.7                      |
| Amazon.com, Inc.    | 92.2                                       | 2.6  | 4.6                      |
| Monsanto Co.        | 42.7                                       | 2.1  | 3.7                      |
| Baidu, Inc.         | 50.9                                       | 2.0  | 3.6                      |
| Visa, Inc.          | 96.0                                       | 1.8  | 3.2                      |
| priceline.com, Inc. | 35.7                                       | 1.8  | 3.1                      |
| YUM! Brands, Inc.   | 32.8                                       | 1.8  | 3.1                      |
| CME Group, Inc.     | 19.2                                       | 1.7  | 3.0                      |
| Wynn Resorts Ltd.   | 12.6                                       | 1.7  | 3.0                      |

Thank you for investing in Baron Fifth Avenue Growth Fund.

Sincerely,



Alex Umansky,  
Portfolio Manager  
May 17, 2012

For more information about this Fund  
please scan this QR code with any  
bar code reader on your mobile device.



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

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

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