Buffalo Small Cap Fund

Quarterly Commentary as of 12/31/16

Average Annualized Performance (as of 12/31/16) Expense Ratio: 1.01%	1 year	3 years	5 years	10 years	Since Inception (4/14/98)
Buffalo Small Cap Fund	6.22%	-1.75%	10.39%	5.77%	10.80%
Russell 2000 Growth Index	11.32%	5.05%	13.74%	7.76%	5.39%

Data represented reflects past performance and is no guarantee of future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original value. Current performance may be lower or higher than the performance quoted. Performance current to the most recent month end may be obtained by visiting the Funds' website at www.buffalofunds.com.

Capital Market Overview

Capital markets got off to a volatile start in 2016 with the Russell 3000 Index dropping over 11% and West Texas Intermediate (WTI) Crude Oil down almost 30% by mid-February. Concerns about soft Chinese economic growth contributed to equity market weakness early in the year, and the energy complex was struggling to resolve its oversupplied condition. Meanwhile, perceived "safe-haven" assets performed strongly as U.S. 10-year Treasury notes advanced and gold appreciated over 15% during the same time frame. Economic concerns and a falling stock market led the Federal Reserve to adopt a less aggressive stance toward interest rate increases, and falling crude production eventually calmed fears of oversupply. These drivers led to a rebound in prices of both equities and crude oil and began a period of steadily rising prices and declining volatility that would continue from mid-February through the end of the year with only minor interruption. Interestingly, perceived "safe-haven" assets continued to perform strongly as gold and U.S. Treasuries rallied alongside equities into the summer and largely held those gains into the fall. The fourth quarter of 2016 began with this uneasy disequilibrium still largely intact, but sentiment changed dramatically with Donald Trump's surprise election victory on November 8th. The election outcome created expectations of pro-growth policies and deregulation that drove accelerating gains in stock prices, higher interest rates and associated declines in the prices of both Treasury bonds and gold, all of which generally persisted through the end of 2016.

The Russell 3000 Index returned 12.74% for the full year. The Russell 3000 Value Index outperformed the Russell 3000 Growth Index by 11.01% during the year, and smaller-capitalization indices such as the Russell Microcap Index, the Russell 2000 Index and the Russell Midcap Index outperformed the large-capitalization Russell 1000 Index by 8.31%, 9.25% and 1.74%, respectively. Much of the outperformance of value stocks can be attributed to the strong performance of the energy sector. Outperformance of small-capitalization stocks was reflective of investor aversion to greater international exposure of larger companies in the face of a rising dollar, as well as increasingly optimistic expectations for the domestic economy and for a lower U.S. corporate tax rate following the election. For the year, Energy and Materials were the best performing sectors in the Russell 3000 Index as expectations for infrastructure investment and increasing investor risk appetite following the election contributed to the reversal of prior-year underperformance that was already underway. Health Care was the worst performing sector for the year, as concerns about political backlash against rising drug prices contributed to declines in Pharmaceutical & Biotech stocks.

For the fourth quarter, the Russell 3000 Index returned 4.21%. The Russell 3000 Value Index outperformed the Russell 3000

Growth Index by 6.04% during the quarter while smaller-capitalization indices such as the Russell Microcap Index and the Russell 2000 Index outperformed the large-capitalization Russell 1000 Index by 6.22% and 5.00%, respectively. The Russell Midcap Index of mid-sized companies underperformed the Russell 1000 Index by 0.62% in the fourth quarter and was the lone exception to the trend of small outperforming large. Outperformance of more cyclically sensitive value stocks and small-capitalization stocks reflected some of the same drivers that were in place earlier in the year, as well as increasingly optimistic expectations for economic growth, higher interest rates and expectations of a lower corporate tax rate in the U.S. following the election. Financial Services was the best performing sector in the fourth quarter, benefiting from higher interest rates and expectations for a less adversarial regulatory regime under the new Republican administration. The flip-side of greater risk appetite was less demand for stable, “bond-like” equities which was reflected in the lower-risk Consumer Staples sector performing poorly during the quarter. Political risk continued to put pressure on the Health Care sector, as uncertainty regarding potential for drug price regulation and repeal of the Affordable Care Act contributed to Health Care being the worst performing sector during the quarter.

Performance Commentary

The Buffalo Small Cap Fund declined 0.28% in the fourth quarter while the Russell 2000 Growth Index gained 3.57%. There was a very obvious disparity on what sectors worked in the Index and what did not. Financials, Industrials, Consumer Discretionary, and Materials all gained over 9% for the quarter while Healthcare declined almost 8% and Technology and Staples gained less than 2%. As discussed above, the surprise election of Donald Trump brought about dramatic repositioning and massive sector rotation as investors sold growth stocks in technology and healthcare to fund purchases of cyclical and financial stocks with the belief that regulations would be reduced and the economy would accelerate. While Financials, Industrials and Materials stocks comprise 32% of the Russell 2000 Growth Index, they contributed 94% of the Index’s return this quarter. As a manager that focuses more on growth companies over pure cyclicals, we are not surprised that we underperformed in a market that shunned growth stocks in favor of value, but we are disappointed by the magnitude of the underperformance. In the first few weeks of January, there are signs that the “Trump trade” has started to fade as investors realize that political and regulatory change will take some time to take effect and our relative performance has improved.

While the market backdrop was not favorable for our style, there were also some fundamental disappointments by some portfolio companies that detracted from performance. The largest underperformer was Nevro, the spinal cord stimulation company that had been one of our biggest winners so far this year. While Nevro has dramatically outperformed Street revenue expectations over the past couple of quarters, company management failed to raise guidance for the December quarter and reigned in aggressive Street analysts’ revenue expectations for 2017. Medical devices were perceived as “losers” in the Trump trade as investors worried that the 20 million Americans that received healthcare coverage from Obamacare might leave the system and the rotation away from healthcare was also partially responsible for Nevro’s decline.

Fitbit was also a meaningful underperformer for the quarter. Growth in the wearables category in which they compete has decelerated and the company has also experienced some manufacturing issues on a new product forcing them to reduce guidance for the fourth quarter which caused the stock’s decline.

Paylocity, an outsourced payroll provider, was hurt by the Trump victory as they received some revenue from filing regulatory forms that confirmed compliance with the Affordable Care Act (ACA) which will likely be significantly modified or repealed by the new Administration. While we believe this composes less than 10% of the company’s revenue, the stock declined over 30% in the quarter.

On the upside, Dave & Buster’s Entertainment was our biggest winner. The restaurant and entertainment complex continued to outpace the casual dining industry as their novel entertainment experience and a greater focus on sports viewing has drawn new visitors to its establishments and provided growth much better than expectations.

Outlook

The setup for 2017 appears to bode well for both accelerated economic growth and the performance potential of U.S. equities. The new Administration's focus on deregulation, infrastructure spend, and tax reform point to a more pro-growth, business-friendly environment. Factoring in higher interest rates, one can make a case for continued rotation out of fixed income into equities. At the same time, many of the new Administration's proposals are not well-defined, and could be difficult to implement in reality. With the market already discounting a more business-friendly environment, we could experience increased market volatility throughout 2017.

We believe that the recent push into value stocks has left many outstanding growth stocks with attractive valuations. We remain focused on investing in secular growth companies that we believe are attractively priced with strong balance sheets. With higher domestic revenues, U.S. small cap stocks could be positioned well going forward if President Trump follows through on his more protectionist policies. We remain convinced that the inefficiencies inherent in small cap and our current position in the economic cycle are best suited for disciplined, active management of the portfolio and we are thankful for your continued support as shareholders.

The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The Statutory prospectus contains this and other important information about the investment company, and it must be obtained by calling 1-800-49-BUFFALO or visiting www.buffalofunds.com. Read it carefully before investing.

As of 9/30/16 the Buffalo Small Cap Fund's top ten equity holdings were: Nevro Corporation 2.88%, LogMeIn, Inc. 2.78%, Monolithic Power Systems, Inc. 2.44%, MarketAxess Holdings Inc. 2.40%, WageWorks, Inc. 2.21%, Supernus Pharmaceuticals, Inc. 2.15%, HealthEquity, Inc. 2.12%, Bio-Techne Corp. 2.10%, Costar Group Inc. 2.10%, Cepheid, Inc. 2.06%.

Top 10 holdings for the quarter are not disclosed until 60 days after quarter end. Those listed are for the previous quarter.

The opinions expressed are those of the Portfolio Manager(s) and are subject to change, are not guaranteed and should not be considered recommendations to buy or sell any security. Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

The U.S. 10-year Treasury Note is a debt obligation issued by the United States government that matures in 10 years. The Russell 3000 Index measures the performance of the 3,000 largest publically held companies incorporated in the U.S. based on market capitalization. The Russell 3000 Value Index is a market-capitalization weighted equity based on the Russell 3000 Index, which measures how U.S. stocks in the equity value segment perform. The Russell 3000 Growth Index includes companies that display signs of above average growth. The Russell Microcap Index is a capitalization weighted index of 2,000 small cap and micro cap companies. The Russell 2000 Index is a small-cap stock market index of the smallest 2,000 stocks in the Russell 3000 Index based on market capitalization. The Russell Midcap Index measures performance of the 800 smallest companies in the Russell 1000 Index. The Russell 1000 Index is a subset of the Russell 3000 Index, which measures the performance of the 1,000 largest publically-held companies incorporated in the U.S. based on market capitalization. The Russell 2000 Growth Index measures the performance of those Russell 2000 Index companies with higher price-to-book ratios and higher forecasted growth values. You can not invest directly in an index.

Mutual Fund investing involves risk. Principal loss is possible. The Fund invests in smaller companies, which involves additional risks such as limited liquidity and greater volatility. Investments in foreign securities include additional risk such as greater volatility, and political, economic, and currency risks, as well as difference in accounting methods.

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