

Capital Market Overview

Equity markets extended their rally in the 4th quarter, with the S&P 500 Index returning 12.15%. This capped the end to a historic year in which the S&P advanced 18.40% despite the world suffering through a global pandemic. The biggest news in the quarter was the U.S. Food and Drug Administration's (FDA) approval of two separate vaccines, following very encouraging clinical results. This helped investors look beyond worsening COVID-19 trends and provided hope that an end to the pandemic could be in sight.

The Russell 3000 Index increased 14.68% in the quarter. Value stocks led the advance, as the Russell 3000 Value Index advanced 17.21% compared to the Russell 3000 Growth Index return of 12.41% during the period. Relative performance was inversely correlated by market cap in the quarter (i.e., small caps outperformed big caps). The Russell 1000 Index delivered a return of 13.69% compared to the Russell Mid Cap Index return of 19.91%. Smaller market cap indexes surged even more as the Russell 2000 Index returned 31.37% and the Russell Micro Cap Index returned 31.39%. Cyclically-sensitive sectors such as Energy, Financials, Industrials, and Materials performed best in the quarter. The more defensive areas like Telecom Services, Consumer Staples, Utilities, and Healthcare lagged. All sectors produced positive absolute results.

Performance Commentary

Producing a return of 19.63%, the Buffalo Discovery Fund (BUFTX) ended the 4th quarter 25 basis points ahead of the Morningstar U.S. Mid Growth Index, which rose 19.38%. The Fund finished the calendar year with a return of 33.81%, a result that ranked in the top half of the Morningstar Mid-Cap Growth Category, but trailed the surging index return of 46.17%. The primary reason for the shortfall compared to the benchmark in 2020 was a portfolio underweight to high growth software companies, which we believe are largely overvalued and over-owned.

There are a myriad of variables that can affect investment performance over a quarter, and the COVID-19 global pandemic, as it did much over 2020, continued to impact the investing environment. As a result, there are accelerating economic trends that are driving new opportunities across the growth universe. Our Fund successfully navigated and leveraged several of these accelerating force changes in the 4th quarter of 2020, helping enable the outperformance.

Average Annualized Performance (%)

| As of 12/31/20 | 1 YR | 3 YR | 5 YR | 10 YR | 15 YR | Since Inception |
|--|-------|-------|-------|-------|-------|-----------------|
| Investor Class - BUFTX | 33.81 | 18.08 | 16.87 | 15.27 | 12.56 | 10.65 |
| Institutional Class - BUITX ¹ | 34.03 | 18.26 | 17.04 | 15.44 | 12.73 | 10.82 |
| Morningstar U.S. Mid Growth Index | 46.17 | 24.40 | 20.83 | 15.59 | 11.96 | 10.02 |
| Morningstar Mid-Cap Growth Category | 39.26 | 19.77 | 17.80 | 13.83 | 10.87 | 8.52 |

¹For performance prior to 7/1/19 (Inception Date of Institutional Class), performance of the Investor Class shares is used and includes expenses not applicable and lower than those of Investor Class shares. 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 buffalofunds.com. Each Morningstar category average represents a universe of funds with similar objectives.

Fund Facts

| | Investor | Institutional |
|-----------------|-----------------------------------|---------------|
| Ticker: | BUFTX | BUITX |
| Inception Date: | 4/16/01 | 7/1/19 |
| Expense Ratio: | 1.02% | 0.87% |
| Fund Assets: | \$1.80 Billion | |
| Category: | Mid Cap Growth | |
| Benchmark: | Morningstar U.S. Mid Growth Index | |

Management Team



Dave Carlsen, CFA

Co-Manager since 2004
B.B.A. – University of WI-Madison



Jamie Cuellar, CFA

Co-Manager since 2020
M.B.A. – Southern Methodist
B.B.A. – Univ. of San Diego



Ken Laudan

Co-Manager since 2020
B.S. – Kansas State Univ.

For instance, as we discuss in more detail in the Top Contributors section, our top three contributing stocks benefited from the ongoing thrust for cloud-based enterprise software, video streaming, and remote online marketplace for outsourced job opportunities.

While stock selection was the primary driver of relative performance during the quarter, two over-arching factors were headwinds: (i) the relative underweight of the Information Technology sector (see comments below) and (ii) stock selection in Financials, although up 13%, underperformed the relative sector benchmark returns.

↑ Top Contributors

Upwork, the leading digital marketplace for outsourced job or “gig opportunities”, was our largest positive contributor in the quarter, posting a 98% return. Performance was mostly a result of positive quarterly earnings and heightened confidence in the longer-term revenue growth outlook of nearly 20%.

Cardlytics, a digital marketing firm, was another standout performer, as a beneficiary of the ongoing thrust to digital financial transactions, coupled with reinvigorated marketing campaigns by both existing and new customers.

8x8, a leading cloud-based “all in one” communications platform for video, voice, and chat, performed well, following the hiring of a highly-regarded new CEO who helped to re-rate the stock's valuation more in-line with peers in the enterprise software sector.

↓ Top Detractors

Bandwidth was our largest detractor in the 4th quarter, declining 11% in the period, owing mostly to rotation away from the more defensive sectors and beneficiaries of the work-from-home toward re-opening centric investments. Nothing in the structural fundamentals drove the underperformance, in our opinion.

eHealth, an online health insurance broker, was down 10% in the quarter as there was some ongoing noise in quarterly results with customer churn. We believe the company will show improvement in their churn metrics as we progress throughout 2021, and, as a leading provider of Medicare policies delivered online, the valuation has the potential to re-rate higher once they do so.

SBC Communications, a wireless tower leasing company in the Real Estate sector, experienced some investor rotation out of its predictable, stable growth towers business into more macro and interest rate sensitive areas of the market, as optimism grew for COVID-19 vaccines and more fiscal stimulus. Churn resulting from the merger of Sprint and T-Mobile may weigh on leasing growth in the first half of 2021 while we wait for more significant 5G and C-band deployments in the 2nd half of the year. We continue to like the long-term growth prospects of the tower business, driven by expanding 5G and rural coverage, new spectrum deployments, more tenants per tower, and growth in mobile devices.

Outlook

Although political tensions remain high as we enter 2021, most of the political uncertainty has now abated. Coupled with two different COVID-19 vaccines approved, the so-called COVID-19 “worst-case scenario” is ostensibly off the table.

We see the 1st half of 2021 quite wobbly from an economic perspective, with the 2nd half of the year weathering the COVID-19 pandemic more effectively, becoming a better proxy of a more typical economic recovery. Accordingly, we see some risks to projected revenue and earnings broadly in the 1st half of the year and particularly the 1st quarter of 2021. It does seem Wall Street is starting to gain a sense of this with some estimates starting to come down.

Our more optimistic 2nd half economic outlook is predicated on the vaccine rollout gaining more traction and efficiency the next 90 days than it has over the initial 45. Only a tad over 5.5 million individuals have received their first injection as of January 6. The goal is clear; we must get to at least 100 million fully-vaccinated individuals by June 1 to put the country on a trajectory of a more normalized second half of '21. An unappreciated factor, in our opinion, in achieving this will be the upcoming single injection COVID-19 phase 3 vaccine data from Johnson & Johnson, expected later this month.

We also will monitor to see how patchy the economic recovery will be in the U.S. as indications of a slowing economy are already appearing. Private sector employment data for December 2020 released from ADP on January 6th showed a 123,000 decrease in employment versus an estimate of an increase of 45,000.

In the meantime, it certainly seems the U.S. Federal Reserve will remain committed to the lower bound on interest rates while supporting increased monetary stimulus when they see the need. It bears pointing out the yield on the 10-year Treasury Bond is now above 1%, and implied inflation expectations are 2%, so we'll keep a cautious eye on the various leading indicators of deflation, as any sustained acceleration would have implications for equity valuations.

In closing, one of the most important aspects of generating long-term, top-tier outperformance as an equity growth manager is to have both the conviction and consistency to lean in on those investments where we fully understand the fundamentals and where we are able to recognize a disconnect or misperception by the market. In our view, finding that disconnect and misperception was more difficult in 2020. In 2021, it is certainly possible there will be some regime change in growth stock investing as the economy, valuation levels, and other risks wax and wane. Notwithstanding, the average growth stock investment experience on the Buffalo Discovery Fund team of 29 years, supported by a well-defined process, gives us confidence we'll continue to generate returns which benefit our shareholders. ▲

Interested in more info?

For questions or to speak with a relationship manager about adding any of the 10 Buffalo Funds to your portfolio, contact:

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The Fund's investment objectives, risks, charges, and expenses must be considered carefully before investing. The summary and statutory prospectuses contain this and other important information about the investment company and can be obtained by calling (800) 49-BUFFALO or visiting buffalofunds.com. Read carefully before investing.

Earnings growth is not representative of the Fund's future performance. Investing in both actively and passively managed mutual funds involves risk and principal loss is possible.

As of 9/30/20 the Buffalo Discovery Fund top 10 equity holdings were Penn National Gaming 2.26%, Natera 1.74%, IHS Markit 1.73%, CoStar Group 1.67%, Bandwidth 1.67%, Kansas City Southern 1.62%, Take-Two Interactive 1.58%, Ametek 1.56%, IAA 1.55%, Generac Holdings 1.53%. Top 10 holdings for the quarter are not disclosed until 60 days after quarter end.

The opinions expressed are those of the Portfolio Managers 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. A basis point is one hundredth of a percentage point (0.01%). The S&P 500 Index is a capitalization weighted index of 500 large capitalization stocks which is designed to measure broad domestic securities markets. The Russell 3000 Index measures the performance of the 3,000 largest publicly held companies incorporated in the U.S. based on market capitalization. The Russell 3000 Value Index is based on the Russell 3000 Index, of companies with lower price-to-book ratios and lower expected growth rates which measures how U.S. stocks in the equity value segment perform. The Russell 3000 Growth Index is a market-capitalization weighted index that measures the performance of those Russell 3000 Index companies with higher price-to-book ratios and higher forecasted growth rates. The Russell 1000 Index is a subset of the Russell 3000 Index and measures the performance of the 1,000 largest publicly-held companies incorporated in the U.S. based on market capitalization. The Russell Midcap Index measures performance of the 800 smallest companies in the Russell 1000 Index. The Russell 2000 Index is an unmanaged index that consists of the smallest 2,000 securities in the Russell 3000 Index, representing approximately 10% of the Russell 3000 total market capitalization. The Russell Micro Cap Index measures the performance of 2,000 small cap and micro cap companies. The Morningstar U.S. Mid Growth Index measures the performance of U.S. mid-cap stocks that are expected to grow at a faster pace than the rest of the market as measured by forward earnings, historical earnings, book value, cash flow and sales. One cannot invest directly in an index. Duration is a measure of the sensitivity of the price of a fixed income investment to a change in interest rates.

Mutual fund investing involves risk. Principal loss is possible. The Fund invests in small and mid-cap companies, which involve additional risks such as limited liquidity and greater volatility than large-cap companies. The Fund invests in foreign securities which involve greater volatility and political, economic, and currency risks as well as differences in accounting methods.

Kornitzer Capital Management is the advisor to the Buffalo Funds, which are distributed by Quasar Distributors, LLC.

