

Capital Market Overview

The stock market extended year-to-date losses during the 3rd quarter and has now fallen for three consecutive quarters. The S&P 500 Index retreated by -4.88% from July 1st to September 30th bringing the YTD total return to -23.87%, which is bear market territory. Stubbornly-high inflation, aggressive interest rate increases, rising fear of a recession, and expectations for softer corporate earnings in the upcoming reporting period were the main headwinds. The Federal Reserve's hawkish stance on inflation resulted in two more oversized federal funds rate hikes during the quarter, bringing the target rate to 3.00%-3.25%. Federal Reserve officials also signaled for additional rate hikes moving forward and holding higher rates for as long as necessary to curb inflation, even if it leads to economic pain. Short-term Treasury yields (two-year notes) are higher than long-term yields (10-year notes) and the yield curve is now inverted by the most since 2000, an indication of a potential recession.

The broad-based Russell 3000 Index declined -4.46% in the quarter and has fallen -24.62% year-to-date. Value stocks fell more than growth stocks during the quarter as the Russell 3000 Value Index returned -5.56% versus a return of -3.37% for the Russell 3000 Growth Index. Relative performance improved going down in market cap size as small caps declined less than large caps in the quarter. Larger cap stocks, as measured by the Russell 1000 Index, returned -4.61% compared to the smaller cap Russell 2000 Index return of -2.19% and the Russell Microcap Index return of -0.48%.

Performance Commentary

The Buffalo Early Stage Growth Fund (BUFOX) generated a return of -3.57% for the quarter ended September 30, 2022. This result compared to the Russell 2000 Growth Index return of 0.24% during the period.

Average Annualized Performance (%)

As of 9/30/22	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
Investor Class - BUFOX	-34.58	6.42	6.90	9.98	7.64	8.12
Institutional Class - BUIOX¹	-34.44	6.59	7.07	10.15	7.80	8.28
Russell 2000 Growth Index	-29.27	2.94	3.60	8.81	6.82	7.91
Morningstar U.S. Small Growth Index	-34.89	0.53	3.35	8.24	6.49	7.61

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 Institutional 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.

Small cap growth stocks rallied in the first part of the quarter but were unable to sustain it, and Index returns ended up flattish for the quarter overall. Markets have failed to climb a wall of worry this year with inflation at 40-year highs, the Federal Reserve (the "Fed") raised interest rates at an aggressive pace to combat inflation, and significant geopolitical conflicts resulted in difficult environments for those regions not self-sufficient in energy production.

As a reminder, the Fund is positioned towards the smaller end of the small cap spectrum and holds companies that are often in the earlier stages of their growth and profitability curve. This has proved challenging to our recent performance. In the 2nd quarter alone, those companies with greater than a \$2 billion market capitalization (these names made up 62% of the weighting of the Index) were up 6.5% on average during the quarter compared to companies with less than a \$1.1 billion market capitalization (making up 15% of the weighting of the Index), which were down 12% on average in the quarter.

Fund Facts

	Investor	Institutional
Ticker:	BUFOX	BUIOX
Inception Date:	5/21/04	7/1/19
Expense Ratio:	1.46%	1.33%
Fund Assets:	\$83.21 Million	
Category:	Small Cap Growth	
Benchmark:	Russell 2000 Growth Index	

Management Team



Craig Richard, CFA

Co-Manager since 2013
M.B.A. – Univ. of Kansas
B.S. – Kansas State Univ.



Doug Cartwright, CFA

Co-Manager since 2015
M.B.A. – Univ. of WI-Madison
B.S. – Baylor University

The Fund underperformed in the Consumer Discretionary and Healthcare sectors and partially offset this with outperformance in the Information Technology sector. The Fund remains underweight Healthcare due to our long-term strategy of not exposing ourselves to binary events in the Biotech industry related to drug failures and approvals. In this quarter, our positioning was a drag given Healthcare had the strongest performance across the various sectors.

↑ Top Contributors

Our largest positive contributor in the quarter was **Calix**, a leading provider of hardware and software that enables broadband service providers to manage and optimize their networks. Strong 2nd quarter results, a continued positive outlook communicated by management, and a new stock buyback authorization drove the shares higher in the quarter. The digital divide between urban/rural and work-from-home trends has created a strong demand set-up for small- and mid- size broadband service providers to continue to build out and optimize their networks. Calix has created a more stable model with recurring software revenue along with a focus on smaller providers, eliminating the lumpiness and volatility from large customers. Broadband access should remain somewhat insulated from any macro weakness in the coming time periods. Calix is also a prime beneficiary of federal government stimulus funds from a couple of legislative acts that should provide a strong tailwind over the next several years, as over \$100 billion in stimulus funds starts to be spent on broadband access.

↓ Top Detractors

The Fund's largest individual detractor in the quarter was **Willdan Group**. Willdan is an engineering and consulting firm focused on partnering with utilities, corporations, and public sector entities to provide them with energy efficiency solutions (windows, lighting, grid modifications, etc.). Energy efficiency is the cheapest solution in the drive towards cleaner energy solutions and initiatives. However, COVID-19 was a significant disruptor to the timelines for some major initiatives with some of the largest utilities in the state of California. These are very large, multi-year contracts which required Willdan to ramp up personnel. However, these COVID-19 related delays pushed out revenue and pressured reported profits. Additionally, Willdan does have debt on its balance sheet, and small cap companies with financial leverage saw outsized share price declines in the quarter given the aggressive interest rate moves by the Fed. That said, the company still has projects in place to more than double profits over the next several years if they can overcome some of the hurdles of working with these large utilities.

Outlook

The Russell 2000 Growth Index has now seen a 38% drawdown from November 2021 levels. Declines of this magnitude historically would suggest that much of the pain is behind us. Many of our Consumer Discretionary holdings are now trading below 6 times annual EBITDA (a cash flow-like metric), multiples which would have been virtually unheard of in years past. Similarly, many recurring revenue software companies have seen their valuations compress by 60-70% or more. However, many of these companies have not yet cut their earnings expectations, a change that we believe is coming as companies look toward 2023 and the macro environment they face. We believe some of the decline in valuation multiples we see already anticipates these coming revisions.

With that said, the economy is at full employment, personal balance sheets remain strong, and corporate balance sheets and margins are at very healthy levels. This should provide a solid foundation in an economic downturn.

Buffalo Early Stage Growth Fund

QUARTERLY
COMMENTARY

September 30, 2022

Regardless of the macroeconomic headwinds we face, our job remains to find attractive small cap companies that have not been fully appreciated by the market or are mispriced due to recent results or events. We believe less investor interest in our segment of the market creates opportunity for us to uncover value.

The Fund typically invests at the smaller end of the small cap growth spectrum and the managers continue to seek companies with sustainable growth due to secular growth trends or innovative or disruptive products.

The Buffalo Early Stage Growth Fund is focused primarily on identifying innovation within U.S. companies with primarily North American revenue bases. With an active share of greater than 90% and a lower turnover strategy with 50-70 holdings, we believe the Fund will continue to offer a distinct offering from the Index and category peers. ▲

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:

Christopher Crawford
ccrawford@buffalofunds.com
(913) 647-2321

Scott Johnson
sjohnson@buffalofunds.com
(913) 754-1537

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.

As of 6/30/22 the Buffalo Early Stage Growth Fund top 10 equity holdings were NV5 Global 3.55%, Kinsale Capital Group 3.15%, i3 Verticals 2.85%, Compass Diversified 2.72%, Paya Holdings 2.56%, Air Transport Services Group 2.54%, Willdan Group 2.45%, Federal Signal Corp 2.40%, ICF Intl 2.24%, Accel Entertainment 2.23%. 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.

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 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 Microcap Index is a n unmanaged capitalization weighted index of 2,000 small cap and micro cap companies. 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. The Morningstar U.S. Small Growth Index measures the performance of U.S. small-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. Active share is a measure of the percentage of stock holdings in a manager's portfolio that differs from the benchmark index. EBITDA stands for earnings before interest, taxes, depreciation and amortization. EBITDA is one indicator of a company's financial performance and is used as a proxy for a company's current operating profitability.

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 than larger companies. Investments in foreign securities involve greater volatility and political, economic and currency risks and differences in accounting methods. This risk is greater in emerging markets.

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

