

Capital Market Overview

The U.S. high yield sector continued its rally in the quarter, keeping yields at record lows. High yield bond prices continued their recovery from the COVID-19 sell-off in March 2020 amid stimulus and vaccine optimism. The high yield market, as demonstrated by the JP Morgan Domestic High Yield Index, posted positive returns in each month of the quarter (0.56% in January, 0.44 % in February, and 0.39% in March) maintaining yields at a 4.72% level. The 10-year U.S. Treasury Bond declined -7.08% during the quarter while the S&P 500 Index logged a return of 6.17%.

Following \$3.4 billion in cash outflows in the final quarter of 2020, high yield mutual funds recorded another \$10.2 billion in outflows this quarter. Interestingly, between the months of April to August 2020, high yield funds posted five consecutive months of inflows totaling \$59.1 billion, which included the two largest monthly inflows ever recorded in April (\$17.1 billion) and May (\$20.5 billion), only to be followed by seven consecutive months of outflows totaling -\$9.2 billion.

High yield new issuance volume was a record \$158.6 billion during the three-month period after posting \$99 billion in the previous quarter. Refinancing continued to be the primary use of proceeds accounting for ~77% of transaction volume in the quarter. According to JP Morgan, mid-tier and upper tier (B-split BBB) issues accounted for the bulk of activity in the quarter (86%) with the heaviest volume coming from Energy (20.3%), Gaming/Lodging (9.8%), and Telecommunications (6.8%).

The yield on the 10-year Treasury Bond increased 82 basis points (bps) during the quarter, from 0.92% to 1.74%, as early signs of inflation and a “return to normal” post-COVID outlook crept into the market. According to data from JP Morgan, the higher credit rating silos, which are more sensitive to interest rate movements, posted negative returns in the quarter while the lower tier silos performed better, as investors sought higher yields. The Defaulted segment produced the largest gain of 21.86% and the BB segment was the worst performer with a 0.09% loss.

According to data from JP Morgan, the U.S. high yield market’s spread to worst for the period was 406 bps, 38 bps tighter than the preceding December quarter and 194 bps tighter than its 20-year historical average of 600 bps. The yield to worst for the high yield market at quarter end was 4.72%, below the 20-year average of 8.34%, and essentially unchanged from the 4.71% at the end of the 4th quarter of 2020.

Performance Commentary

The Buffalo High Yield Fund (BUFHX) increased 1.73% in the quarter, outperforming the ICE BofAML U.S. High Yield Index return of 0.90% for the three-month period. The Fund also outperformed the Lipper High Yield Bond Funds Index return of 1.47%.

Average Annualized Performance (%)

As of 3/31/21	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
Investor Class - BUFHX	27.07	7.06	6.54	5.68	6.21	7.08
Institutional Class - BUIHX ¹	27.28	7.19	6.68	5.83	6.36	7.24
ICE BofAML U.S. High Yield Index	23.31	6.53	7.94	6.31	7.21	7.15
Lipper High Yield Bond Funds Index	24.07	5.95	7.30	5.68	6.07	5.95
Morningstar High Yield Bond Category	21.79	5.43	6.54	5.31	6.00	5.89

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:	BUFHX	BUIHX
Inception Date:	5/19/95	7/1/19
Expense Ratio:	1.03%	0.89%
Fund Assets:	\$275.73 Million	
Category:	High Yield Bond	
Benchmark:	ICE BofAML U.S. High Yield Index	

Management Team



Paul Dlugosch, CFA
Co-Manager since 2007
B.S. – University of Iowa



Jeff Sitzmann, CFA
Co-Manager since 2007
M.B.A. – Univ. of Chicago
B.B.A. – Univ. of Toledo



Jeff Deardorff, CFA
Co-Manager since 2015
B.S. – Kansas State Univ.

Fund Composition by Asset Class

	3/31/20	6/30/20	9/30/20	12/31/20	3/31/21
Straight Corporates	60.1%	55.4%	60.6%	61.0%	62.7%
Convertibles	16.7%	20.1%	17.6%	14.7%	16.3%
Bank Loans	19.1%	16.6%	16.3%	17.2%	11.2%
Preferred Stocks	1.3%	1.7%	1.5%	1.2%	2.2%
Convertible Preferreds	0.0%	0.0%	0.0%	0.0%	0.0%
Common Stocks	1.0%	0.6%	0.4%	0.1%	0.0%
Cash	1.8%	5.6%	3.6%	5.8%	7.6%
TOTAL	100.0%	100.0%	100.0%	100.0%	100.0%

Approximate Rate & Contribution of Return in 1Q21

	Contribution to Return
Straight Corporates	1.31%
Convertibles	0.19%
Bank Loans	0.29%
Preferred Stocks	0.14%
Convertible Preferreds	0.00%
Common Stocks	0.00%
TOTAL	1.73%

↑ Top Contributors

During the period 112 out of the 143 issues in the Buffalo High Yield Fund produced positive returns. The three top contributors were **Southwest Airlines** 1.25% convertible bonds, **J2 Global** 1.75% convertible bonds, and **Quad Graphics** 7.00% corporate bonds. The rise in Southwest Airlines convertible bonds was driven by the underlying common stock rallying throughout the quarter as COVID-19 vaccinations began rolling out and interest in air travel picked up steam. J2 Global improved on the back of the underlying common stock increasing over 22% during the quarter, driven by better than expected earnings and continued demand for its cloud-based communication services. Quad Graphics corporate bonds returned to near par levels, after the company reported better than expected earnings during the quarter, and investors were attracted to its higher coupon, lower duration profile.

↓ Top Detractors

Guidewire 1.25% convertible bonds, **Smile Direct Club** zero coupon convertible bonds, and the **Air Transport Services** 1.125% convertible bonds were the worst performers during the quarter. Guidewire performed well in the December quarter and gave some of that back this period as investors rolled out of Technology and into value sectors. Smile Direct Club convertible bonds were issued during the quarter as the stock was peaking and then retreated after the issuance. Air Transport Services convertible bonds declined after the common stock peaked at year-end despite Amazon announcing that it was purchasing another eleven aircraft from the company.

Outlook

We are managing the Fund cautiously yet actively, focusing on high quality, below investment grade issuers with defensive business models and manageable credit metrics. We will continue to deploy cash in opportunities that we believe offer the most appealing risk/reward tradeoff with a bias toward shorter durations and less levered credits. Additionally, we believe bank loans offer a more defensive position as they provide senior positioning in the capital structure and less interest rate sensitivity due to their floating rate structures. Finally, we continue to look for opportunities in convertible bonds and preferred stocks. We ended the period with 143 positions, up slightly from the previous quarter's level of 138 (excluding cash). ▴

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.

As of 12/31/20 the Buffalo High Yield Fund top 10 holdings were Open Lending (1 mo LIBOR + 6.500%, 3/11/27) 2.58%, Nuance Communications (1.500%, 11/1/35) 2.46%, MPLX (6.875%, 8/15/23) 2.17%, Daseke (1 mo LIBOR + 5.000%, 2/27/24), 1.86%, Builders FirstSource (5.000%, 3/1/30) 1.62%, Michaels Stores (8.000%, 7/15/27) 1.61%, CNX Resources (7.250%, 3/14/27) 1.61%, Treehouse Foods (4.000%, 9/1/28) 1.55%, Diebold Nixdorf (8.500%, 4/15/24) 1.52%, Comstock Resources (9.750%, 8/15/26) 1.41%. 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 10-year Treasury bond is a debt obligation issued by the United States government that matures in 10 years. A basis point (bps) is one hundredth of one percent (0.01%). Yield is the income return on an investment. This refers to the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost, its current market value or its face value. Yield to worst is the lowest potential yield that can be received on a bond without the issuer actually defaulting. Spread to worst measures the difference from the worst performing security to the best, and can be seen as a measure of dispersion of returns within a given market or between markets. Duration is a commonly used measure of the potential volatility of the price of a debt security, or the aggregate market value of a portfolio of debt securities, prior to maturity. Securities with a longer duration generally have more volatile prices than securities of comparable quality with a shorter duration. A coupon or coupon payment is the annual interest rate paid on a bond, expressed as a percentage of the face value and paid from issue date until maturity. JP Morgan Domestic High Yield Index is designed to mirror the investable universe of the U.S. dollar domestic high yield corporate debt market. 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 ICE BofAML U.S. High Yield Index is an unmanaged index comprised of over 1,200 high yield bonds representative of high yield bond markets as a whole. The Lipper High Yield Bond Funds Index is a widely recognized index of the 30 largest mutual funds that invest primarily in high yield bonds. One cannot invest directly in an index. The LIBOR (London InterBank Offered Rate) is a benchmark interest rate at which major global banks lend to one another in the international interbank market for short-term loans. A Standard & Poor's Rating of B means an obligor is more vulnerable the obligors rated 'BB', but the obligor currently has the capacity to meet its financial commitments. A Standard and Poor's Rating of BB means an obligor is less vulnerable in the near term than other lower-rated obligors. A Standard and Poor's Rating of CCC means an obligor is currently vulnerable, and is dependent upon favorable business, financial, and economic conditions to meet its financial commitments. The highest rating is AAA and the lowest rating is D. A Standard & Poor's Rating of BBB- or higher represents investment grade securities. In limited situations when the rating agency has not issued a formal rating, the Advisor will classify the security as nonrated.

Mutual fund investing involves risk. Principal loss is possible. Investment by the Fund in lower-rated and non-rated securities presents a greater risk of loss to principal and interest than higher-rated securities. Investments in debt securities typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities. Investments in foreign securities include additional risk such as greater volatility, and political, economic, and currency risks, as well as difference in accounting methods.

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