Buffalo International Fund

QUARTERLY
COMMENTARY

June 30, 2022

Capital Market Overview

Global equity markets were once again in the red in the quarter, as the war in Ukraine carried on, along with all of its negative effects on the global economy, especially in Europe. Equity markets priced in additional interest rate hikes as central banks around the world raised rates in the face of continued high inflation. We also began to see signs that the rising costs of living are weighing on economic growth, as numerous companies in the United States and Europe began reporting that consumers were beginning to trade down or tighten their purse strings. As a result markets began pricing in the increased risk of an economic recession.

Developed markets declined by double-digits in U.S. dollar terms. The dollar continued to strengthen in the quarter against foreign currencies, which made poor performance in foreign markets even worse for U.S. investors. The stock markets in Europe saw steep declines, as higher inflation weighed on consumer confidence, and worries multiplied about the possibility of a recession and a potential energy crisis if Russia were to completely cut of its supply of gas to the Eurozone. It became clear that more rate hikes from the European Central Bank are on the horizon. The Japanese market was also very weak due to currency moves, declining -4.60% in local terms, but -13.88% in U.S. dollar terms after the currency adjustment. As the Japanese central bank continued to resist rate increases, the yen carry trade continued and the yen continued to weaken against the dollar. Hong Kong was a relative bright spot in the quarter, as that developed market fell just -1.0% in U.S. dollar terms.

Emerging markets were also mostly negative in the quarter. The Brazilian and Korean markets were especially weak, producing returns of -26% and -21% in U.S. dollar terms, respectively. Chinese markets, however, were positive in local currency, and only slightly negative in U.S. dollar terms, like Hong Kong. Better results in China could be attributed to investors returning to the markets after the lockdowns in Shanghai, and other cities were successful in bringing down COVID infections, and also after the Chinese Government stated its intentions to support the economy.

While the S&P 500 Index declined -16.10% during the quarter, the MSCI ACWI ex USA Index declined -13.54%, and the developed country MSCI EAFE Index fell -14.51%.

Performance Commentary

The Buffalo International Fund (BUFIX) produced a return of -16.59% for the quarter, a result that slightly underperformed the MSCI ACWI ex USA Growth Index return of -15.59%. The Fund lagged the broad FTSE All-World ex US Index return of -13.56% by a greater margin.

Average Annualized Performance (%)

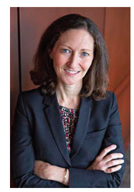
As of 6/30/22	1 YR	3 YR	5 YR	10 YR	Since Inception
Investor Class - *BUFIX*	-21.99	3.70	5.41	7.70	4.48
Institutional Class - *BUIIX*[1]	-21.90	3.85	5.57	7.86	4.64
FTSE All-World ex US Index	-18.64	2.23	3.16	5.54	2.00
Morningstar Global Markets ex-US Index	-19.50	1.66	2.65	–	–
MSCI ACWI ex USA Growth Index	-25.59	1.92	3.77	6.07	–
Lipper International Fund Index	-19.30	2.44	2.85	5.85	1.93

[1]For 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.

Fund Facts

	Investor	*Institutional*
Ticker:	BUFIX	BUIIX
Inception Date:	9/28/07	7/1/19
Expense Ratio:	1.04%	0.89%
Fund Assets:	$482.98 Million	
Category:	Foreign Large Growth	
Benchmark:	FTSE All World Ex-US Index	

Management Team



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Value stocks outperformed growth stocks in the period, and the Buffalo International Fund's growth-oriented focus was a hindrance to performance, especially vs. the FTSE All-World ex US Index which has a larger allocation to value stocks. In terms of sector selection, the Fund's overweight position in Technology was a drag, as that area was the largest underperforming sector in the quarter. On the other hand, Energy was a better performing sector in the quarter, but the Fund is generally underweight this deep cyclical area. Regarding country exposure, the Fund's overweight position in the underperforming European markets weighed on relative performance, as did the underweight position to the better performing Hong Kong and China markets. Stock selection played a minor role in underperformance, while the Fund's cash position helped temper steeper declines.

↑ Top Contributors

Top contributors in the period included BAE Systems Plc, Hong Kong Exchanges and Clearing Ltd., and Astrazeneca Plc. BAE Systems, a multinational provider of defense and aerospace systems, based in the U.K., is benefiting from plans to increase defense spending in the Eurozone. Next, Hong Kong Exchanges, the operator of HKEX, saw its stock price increase, as investors returned to the Hong Kong market in the quarter. Prior concerns related to both the mainland and Hong Kong's management of coronavirus infections began to ease. Hong Kong Exchanges is expected to be a beneficiary of future initial public offerings (IPOs) and programs to connect Hong Kong markets with mainland China. Finally, Astrazeneca, one of the largest multinational pharmaceutical companies, presented positive data for a key pipeline drug to treat breast cancer.

↓ Top Detractors

Top detractors in the quarter were Ashtead Group Plc, Schneider Electric SE, and Hexagon AB.

Ashtead, an equipment rental company that operates in the U.S. and the U.K., continued to decline in the quarter on fears of a weakening economy in the U.S. and a softer construction outlook. We continue to like the company's growth prospects from increased rental penetration and market share gains from smaller peers, but we are keeping an eye on U.S. construction markets, an important end market for their business. The increasing cost of owning, operating, and complying with laws surrounding new equipment makes rental preferable, thus growth in outsourcing equipment rentals should be an ongoing long-term trend.

Schneider Electric, a global manufacturer of electrical power products, saw its stock decline along with other companies in the industrial sector, due to fears of a recession, signs of a slowdown in European construction, and the negative impact from the COVID lockdowns in China. We expect that Schneider's growth could moderate over the next year or two as a result but remain positive on the company's prospects for growth longer-term, due to its exposure to secular trends in energy efficiency, industrial automation, and Internet of Things (IoT).

Hexagon, a global provider of design, measurement, and visualization technologies, declined for similar reasons as Schneider Electric. While Hexagon operates in cyclical end markets, we continue to believe that a majority of the business is fueled by secular growth trends, such as industrial automation or digitalization, Industrial Internet of Things (IoT) and digital twins, the transition to renewables, and autonomous vehicles. Nearly 60% of Hexagon's revenues are from software and services, and a product portfolio that is geared to drive efficiency improvements for clients. This makes such spend a less attractive place to cut for corporates in difficult times. We expect Hexagon's business to be more resilient in a slowdown relative to other industrial peers.

Outlook

With the war in Ukraine continuing to put upward pressure on energy and food prices and central banks around the world raising interest rates to combat continued inflation, it is clear that the world economy is weakening, and many countries are facing the probability of recession.

Given our overweight position in Europe, we are most concerned about the economic impacts on the Eurozone, and here we find that the situation has deteriorated. While a few months ago the signs of wage inflation were scant, there are now more clear signs of upward pressure on wages. The most worrisome situation in Europe, however, is the ongoing energy crisis, where the region could be facing a future with even higher prices and potential supply rationing. The European community is understandably concerned that Russia could fail to resume the flow of gas once the current shut-down for maintenance is completed. If the gas flow stops indefinitely, recession seems an inevitable outcome for the Eurozone, particularly in Germany. Either way Germany is determined to move as quickly as possible toward developing other sources of energy. We expect to see increased investment in alternative energy sources and increased spending with many companies to prepare for the potential loss of Russian gas.

In China the situation is somewhat different. The Chinese government has announced it is determined to maintain a "COVID zero" policy on the mainland, which will most likely continue to weigh on economic growth as restrictions on activity wax and wane. However, China is the one country in the world where monetary policy is loosening rather than tightening, and inflation remains under control. We remain cautious about the risks associated with investing in China due to government regulation, a weakening economy, and ongoing pandemic-related restrictions. However, we will seek out opportunities that fit our investment strategy and have fewer of these country specific risks.

The economic and geopolitical uncertainty around the world has driven a flight to quality, which includes the U.S. dollar, that has helped to strengthen the U.S. currency making it more challenging for international investors. As other central banks around the world catch up to the U.S. Federal Reserve in raising rates, it could alleviate some of the relative downward pressure on their currencies. However, we would imagine that the perceived safety of the U.S. dollar could nonetheless continue if the outlook abroad appears more uncertain than inside the United States.

Despite the challenges, we also look for positive takeaways. Supply shortages are finally easing around the globe, and consumers in many countries are spending their pandemic savings. Given the parity of the euro and U.S. dollar, now is certainly a good time for Americans to travel to Europe, and while our portfolio companies have considerable revenues in the U.S., a higher cost base in Europe will be a benefit. China's weak economy is alleviating some of the pressure on commodity prices, and we foresee inflation peaking in the next quarter or two if energy inflation does not worsen considerably. Finally, as equity markets have declined considerably, we believe stock prices are already pricing in a mild recession for many of our portfolio holdings.

While it is impossible to know where the bottom of this bear market may be, we continue our long-term focused investment strategy. Our emphasis is on high-quality companies that have sound, sustainable business models, competitive advantages, and could benefit from secular growth drivers that drive growth throughout the business cycle. We thus prefer businesses that have strong balance sheets that generate strong free cash flow. In this inflationary environment we also favor companies that have the means to pass off cost pressures, such as those with high recurring revenues or companies whose products make up a small cost of a larger product. Faced with a potential recession, we prefer companies that can preserve margins even in a weaker economic environment. This includes businesses that are asset light, have low fixed costs, or possess the ability to drive efficiency improvements through a downturn. We pay close attention to the valuations of the companies in the portfolio, and seek out opportunities during periods of market weakness, or volatility, to buy high quality growth companies at attractive valuations. We believe that by continuing our disciplined strategy we should be able to post superior risk-adjusted returns over the long term.

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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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