Buffalo Large Cap Fund

QUARTERLY
COMMENTARY

June 30, 2020

Capital Market Overview

Equity markets rebounded sharply in the 2nd quarter following steep losses in the previous period. The S&P 500 Index produced a return of 20.54%, marking the best quarterly performance results in 20 years. Stimulus efforts by the Federal Reserve (the "Fed") and the U.S. Treasury Department to limit COVID-related economic damage helped equity markets find a floor in late March. Declining COVID-19 case counts, optimism about treatment and potential vaccines, along with better-than-expected economic data also contributed to improved investor sentiment during the period. Although confirmed virus cases began spiking again in the final days of June, it was not enough to undo the best quarterly market results since the dot-com boom.

The broad market Russell 3000 Index advanced 22.03% in the quarter, and Growth outperformed Value as the Russell 3000 Growth Index moved up 27.99% during the period, compared to the Russell 3000 Value Index's advance of 14.55%. Relative performance was inversely-correlated by market cap as the Russell Micro Cap Index advanced 30.54%, well above the large cap Russell 1000 Index's return of 21.82%. Meanwhile the small cap Russell 2000 Index and the Russell Mid Cap Index were up 25.42% and 24.61%, respectively. The best performing sectors were Technology, Consumer Discretionary, and Energy while the less cyclically exposed, more defensive areas like Utilities, Telecommunication, and Consumer Staples lagged in the quarter.

Performance Commentary

The Buffalo Large Cap Fund (BUFEX) returned 24.25% during the quarter, but lagged the Morningstar U.S. Large Growth Index's gain of 26.60%. Poor stock selection in the Consumer Discretionary and Financials sectors was the leading cause of underperformance compared to our benchmark, which was offset, in part, by strong Fund results in Information Technology. While large cap growth stocks outperformed small cap growth stocks during the broad market selloff of the 1st quarter, this trend reversed itself in the 2nd quarter, and large cap growth underperformed small cap growth by about 7%. However, large cap growth outperformed large cap value by a wide margin in both of the first two quarters of this year. Within the Index, Materials, Consumer Discretionary, and IT were the strongest sectors, all reversing sharp declines from the 1st quarter, reflecting investor optimism about a potential economic rebound and recovery.

Average Annualized Performance (%)

As of 6/30/20	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
Investor Class - *BUFEX*	14.55	14.16	13.01	15.03	9.94	9.98
Institutional Class - *BUIEX*[1]	14.74	14.34	13.18	15.20	10.10	10.15
Morningstar U.S. Large Growth Index	23.28	20.46	16.00	17.71	11.06	-
Lipper Large Cap Growth Index	21.75	18.37	14.60	15.91	10.14	8.94

[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:	BUFEX	BUIEX
Inception Date:	5/19/95	7/1/19
Expense Ratio:	0.94%	0.79%
Fund Assets:	$90.11 Million	
Category:	Large Cap Growth	
Benchmark:	Morningstar U.S. Large Growth Index	

Management Team

Alex Hancock, CFA
Manager since 2018
B.A. – Dartmouth College

↑ Top Contributors

Microsoft was the top-contributing stock for the Fund during the quarter, with the stock returning 29%. The company's business has been insulated from COVID-19 slowdowns, amidst the increase in remote work and learning. Growth in its cloud services and Office 365 products also remained strong. We believe the company's growth outlook over the next several quarters is solid regardless of the trajectory of the COVID-19 pandemic.

Amazon was another top contributor, with shares increasing by 41%. Demand for Amazon's delivery services accelerated as consumers avoided brick-and-mortar stores in the pandemic environment. The company's web services division was also well positioned for continued growth, driven by the need for cloud computing in a remote work environment.

↓ Top Detractors

Biogen underperformed during the quarter, after losing a courtroom decision in June that could lead to the loss of patent protection for Tecfidera, a key drug treatment for multiple sclerosis. There is also significant uncertainty regarding the potential approval of its Alzheimer's drug Acucanumab, but we expect more clarity on this in coming quarters. While the risk/reward tradeoff for the stock appears favorable at current levels, Biogen remains a relatively small position in the Fund, given our expectation that upcoming news flow will drive significant volatility in the company's shares.

Outlook

The first two quarters of 2020 were turbulent for investors, and we expect the trend of elevated volatility to continue into the 2nd half of the year. We believe the trajectory of the COVID-19 pandemic will be a key driver of market direction. The gradual reopening of the U.S. economy has coincided with a surge of virus cases in Sunbelt states and California. Investors will closely watch evolving data on infection rates, hospitalization rates, and deaths, and, while we believe that state and federal governments will resist shutting down economies again, any signs that the U.S. is returning to broad-based quarantines would likely lead the stock market downward.

We are also closely watching for news on treatments, as well as indications of a promising vaccine, and expect to see more data within the next several months. Any sign that an effective vaccine could be rolled out in the near term would be a binary event, and we would expect the market, especially the value stocks that have lagged growth in the 1st half of 2020, to rerate and trade sharply upward.

The trajectory of the U.S. economy and potential recovery in the job market remains another question mark. While jobless claims in June have pointed to a sharp recovery in the U.S. job market, employment remains far below pre-pandemic levels, and any efforts to reinstate quarantines could derail the recovery.

We are also paying close attention to the upcoming elections in November. Recent signs suggest larger Democratic Party gains than what we would have predicted at the start of 2020. Large Democratic gains could lead to factors such as higher corporate taxes, an increased focus on prescription drug prices, and regulatory pressure on the business models of the mega-cap technology companies that have been market leaders in recent years.

Other factors that could drive market volatility in coming months include: (i) the extension or expiration of various government stimulus efforts this summer and fall; (ii) expansion of the protest movements that swept across numerous large cities in June; and (iii) the upcoming earnings season. Earnings announcements will give us a better sense of the declines and balance sheet stress experienced by corporate America due to the pandemic-related shutdowns.

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Within the framework above, we are cautiously optimistic about the prospects for economic recovery in the U.S., but expect significant volatility in large cap growth stocks in coming months.

We finished the June quarter with 54 holdings, up from 52 at the start of the quarter. During the period, we sold out of two positions, and initiated four new ones. We are continuing to manage the Fund actively, allocating capital to ideas we believe have the best risk/reward tradeoffs, and reducing those that are less favorable. We also continue to invest in companies whose organic growth is pressured in the near-term by pandemic-driven slowdown, but whose business models and balance sheets are strong. We believe many of these businesses can use the downturn as an opportunity to operate more efficiently, gain market share, and find new opportunities for growth. We expect many of these holdings to emerge from the downturn with stronger, higher-margin businesses after the U.S. economy returns to more normalized levels.

Our time-tested strategy of investing in premier large cap growth companies, which could benefit from long-term trends and trade at attractive valuations, remains the cornerstone of our work, and we appreciate your continued confidence in our efforts.

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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