

Buffalo Mid Cap Fund

QUARTERLY
COMMENTARY

December 31, 2019

Capital Market Overview

The combination of a U.S. Federal Reserve (Fed) interest rate cut, an improving economic outlook, and easing trade tensions, sent equity markets sharply higher in the 4th quarter. The S&P 500 Index advanced 9.10% during the period, which brought the full-year (2019) gain to 31.49%. The Fed cut interest rates three times in 2019, erasing the brief yield curve inversion and assuaging fears of a recession. The economy continued to add new jobs at a strong pace and unemployment declined to 3.5%. Consumer spending remained healthy, and there is optimism for better business investment following the announced "phase one" trade deal with China.

Similar to the S&P 500 Index, the broad-based Russell 3000 Index returned 9.04% during the quarter. Growth outperformed value, as the Russell 3000 Growth Index returned 10.62% compared to a return of 7.41% for the Russell 3000 Value Index. Smaller companies outperformed larger companies, as one would expect in a "risk-on" period. The Russell Microcap Index surged 13.45% and the Russell 2000 Index advanced 9.94%. Large company benchmarks such as the Russell 1000 Index advanced 9.04% while the Russell Midcap Index produced a return of 7.06%. Technology and Health Care were the best performing sectors in the quarter, while more defensive areas of the market lagged such as Real Estate and Utilities. Higher long-term interest rates weighed on high-quality bond proxies – the safe haven 10-year U.S. Treasury Bond produced a return of -1.74% during the quarter.

Performance Commentary

In the 4th quarter of 2019, the Buffalo Mid Cap Growth Fund returned 5.89%, lagging the benchmark Morningstar U.S. Mid Growth Index return of 8.31%. The Fund's under-performance was due to selection in the Health Care, Consumer Discretionary, and Industrial sectors.

Average Annualized Performance (%)

As of 12/31/19	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
Investor Class - <i>BUF</i> MX	37.98	13.28	8.90	10.83	8.36	8.51
Institutional Class - <i>BU</i> IMX ¹	38.16	13.45	9.06	10.99	8.52	8.67
Morningstar U.S. Mid Growth Index	36.01	18.29	11.84	14.04	10.27	9.02
Lipper Mid Cap Growth Index	33.83	17.58	11.33	13.02	9.70	8.72

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.

↑ Top Contributors

Among the top contributors during the quarter were **MSCI**, **Lam Research**, and **IHS Markit**. MSCI was boosted by earnings that beat investor expectations, the announcement of a 10-year contract renewal with BlackRock, and in response to the strong performance of international equities (which drives a large percentage of their asset-based fees). Lam Research shares gained on a stronger earnings outlook and the belief that the semiconductor capital spending cycle has bottomed. IHS Markit presented a 2020 outlook that was well received by investors, as was their capital allocation plan. The company expects to generate increasing amounts of free cash flow and plans to initiate a dividend and increase share repurchases.

Fund Facts

	Investor	Institutional
Ticker:	BUFMX	BUIMX
Inception Date:	5/19/95	7/1/19
Expense Ratio:	1.02%	0.87%
Fund Assets:	\$175.04 Million	
Category:	Mid Cap Growth	
Benchmark:	Morningstar U.S. Mid Growth Index	

Management Team



Chris Carter, CFA

Co-Manager since 2017
M.B.A. – Univ. of WI-Madison
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↓ Top Detractors

The biggest detractors in the period were **Expedia**, **RealPage**, and **Verisk Analytics**.

Expedia shares traded lower when management's outlook for growth and margins were reduced, citing Google's increasing competition in travel as a primary cause. In a stunning move, the company's board differed with management's assessment of the company's growth potential, leading to the resignation of the CEO and CFO, which, given the board's more optimistic view of growth, led to a partial recovery in the stock.

RealPage also detracted from performance during the quarter as project implementation delays continue to cause revenues to slip into future periods. We believe these delays are driven by larger, more complicated deals and better product penetration into their clients and not by any lack of demand or competitive issues. Eventually, they should be able to convert pipeline into revenues quicker, boosting revenue growth and rewarding shareholders.

Verisk reported solid earnings during the period, but company management also announced a negative verdict in a patent infringement lawsuit. They plan to appeal the ruling and look for alternative, non-infringing ways to continue offering customers a similar product. Given that the affected aerial imagery / roof reports represented about 1% of revenues, we do not consider the setback to be material even in a worst case scenario.

Outlook

At the start of 2019 the market was coming off a significant sell-off from the 4th quarter of 2018. Federal Reserve interest rate increases and rising trade tensions with China drove fears of decelerating economic growth. However, the Fed reversed course by cutting interest rates three times over the last year. While the tensions with China did result in a trade war of sorts, it was deescalated with a "Phase One" trade deal agreement near the end of the year. In 2020, trade relations with China and the negotiation of a more comprehensive trade deal will continue to be a risk. In addition, the Manufacturing PMI Index has recorded several consecutive readings below 50, which has historically been a good warning indicator of weaker economic growth and a possible recession in the near future. However, it is possible that the interest rate cuts by the Federal Reserve and "Phase One" trade resolution between the U.S. and China will help the economy avoid recession. This backdrop, combined with robust investment returns in 2019, has sharpened our focus on the health of the economy and sustainability of earnings growth in 2020. ▲

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 9/30/19 Buffalo Mid Cap Fund top 10 equity holdings were CoStar Group 3.17%, IHS Markit 2.98%, MSCI 2.82%, Verisk Analytics 2.70%, ServiceNow 2.58%, Palo Alto Networks 2.32%, CBRE Group 2.26%, AMETEK 2.20%, RealPage 2.16%, Tyler Technologies 2.08%. 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 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 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 Microcap Index is an unmanaged capitalization weighted index of 2,000 small cap and micro cap companies. 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 1000 Index is a subset of the Russell 3000 Index, which 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 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. The Lipper Mid Cap Growth Index is an unmanaged, equally weighted performance index of the 30 largest qualifying mutual funds (based on net assets) in the Lipper Mid-Cap classification. One cannot invest directly in an index. Cash flow is a measure of the cash produced by the firm in a given period on behalf of equity holders. The true measure of the value of a firm's equity is considered to be the present value of all free cash flows. The Purchasing Managers' Index (PMI) is an index of the prevailing direction of economic trends in the manufacturing and service sectors. The Index is on a scale from 0 to 100; a PMI above 50 represents an expansion when compared with the previous month, and a PMI reading under 50 represents a contraction.

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.

