

# Mid Cap Fund

PM Commentary as of September 30, 2017



## Average Annualized Performance (%)

As of 9/30/17	1 YR	3 YR	5 YR	10 YR	Since Inception
<b>Buffalo Mid Cap Fund</b>	10.62	6.19	10.59	6.07	7.82
<b>Russell Midcap Growth Index</b>	17.82	9.96	14.18	8.20	8.73

Expense ratio 1.02%. Inception date 12/17/01. 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](http://buffalofunds.com).

## CAPITAL MARKET OVERVIEW

Equity markets continued their strong start to the year during the 2nd quarter, primarily driven by strong corporate earnings growth. The Russell 3000 Index advanced 3.02% in the 2nd quarter. As reported during the June 30 period, earnings from S&P 500 Index companies were up 14% year-over-year in the 1st quarter, the strongest growth reading since 2011.

Broadly speaking, growth stocks continued their outperformance relative to value stocks, while cyclical stocks, that rallied to end 2016, underperformed as investors continued to discount the likelihood of government infrastructure spending and comprehensive tax reform. The yield on the U.S. 10-year Treasury ended the June 30 period at 2.298%, a decline from its recent high of 2.609% in March, due in large part to weaker inflation readings. In contrast, the outlook for growth and interest rate expectations improved in much of the rest of the world, which has driven the trade-weighted U.S. dollar down 5.6% year to date. Oil entered bear market territory, with crude prices declining 9% during the quarter in response to stronger than expected inventory levels and rising U.S. production.

As mentioned above, investors continued to favor growth over value, and the Russell 3000 Growth Index climbed 4.65% during the period, compared to the more modest gain of 1.29% for the Russell 3000 Value Index. By size, microcaps were the best performers with the Russell Microcap Index gaining 3.83%. Meanwhile the large cap Russell 1000 Index gained 3.06%, followed by the Russell Midcap Index at 2.70% and the Russell 2000 Index finishing with a gain of 2.46% during the period.

In general health care was the best performing sector as the chances for legislation to repeal or reform the Affordable Care Act appeared to diminish, and investors reacted by bidding up health care stocks. The technology sector was also a strong performer as the market continued to reward the strong earnings growth produced in this area. Conversely, energy was the worst performing sector, driven by the decline in oil prices mentioned above.

## PERFORMANCE COMMENTARY

The Buffalo Mid Cap Fund generated a return of 2.31% for the quarter, which underperformed the Russell Midcap Growth Index return of 5.28%. The Index was primarily driven higher by contributions from the information technology and industrials sectors. The majority of the Fund's relative underperformance was the result of both difficult stock selection and an unfavorable sector allocation effect.

## PORTFOLIO MANAGEMENT TEAM



### Bob Male, CFA

Manager since Inception  
M.B.A. – Southern Methodist Univ.  
B.S. – University of Kansas



### Dave Carlsen, CFA

Co-Manager since 2015  
B.A. – Univ. of Wisconsin - Madison



### Scott Moore, CFA

Co-Manager since 2017  
M.B.A. – Univ. of Missouri - Columbia  
B.S. – Univ. of Missouri - Kansas City

Stock selection and an underweight allocation in information technology had the biggest negative impact on the Fund's relative performance. Stocks the Fund owned that underperformed included **Sabre Corporation**, which declined about 15.5% during the quarter. The company disappointed when they announced a slowdown in their airline solutions business due to the halting of an implementation at Air Berlin, Alitalia's bankruptcy, and the loss of a Southwest Airlines domestic contract. These developments, coupled with increased investments in new products and technology, are expected to weigh on growth and margins in the near term.

Other large relative detractors from the information technology area were companies or sub-industries within the index that the Fund did not own or was underweight. Most notably was the Fund's underweight exposure to semiconductor and semiconductor equipment companies as well as IT services, both areas that negatively affected relative performance of the Fund. Within semiconductors and semiconductor equipment, the Fund's non-ownership of Lam Research was a large relative detractor as the stock advanced 31.6% for the quarter. Despite temptations to chase this year's benchmark leaders such as Lam Research, we continue to deploy capital to where we see a more favorable long-term risk/reward tradeoff.

Stock selection within the consumer discretionary sector was another area that negatively impacted relative performance during the period. **AMC Entertainment** was the largest detractor within our portfolio as the company's shares declined just over 40% during the quarter. The decline in AMC reflects investor concerns surrounding premium video on demand (PVOD) and its potential impact on theater industry revenues, as well as a weaker than expected box office.

On a constructive note, stock selection among the Fund's industrials companies was positive during the quarter. Shares of **Trex** and **FMC Corp** advanced 33% and 23%, respectively. Trex's revenues continued to benefit from healthy repair and remodel activity, as well as increased market share of wood alternatives. Additionally, the company's focus on efficient manufacturing, cost cutting initiatives, and capacity utilization boded well for margins. Meanwhile FMC, the 2nd largest producer of lithium batteries by revenue, continued to benefit from strong demand from electronics and automobile manufactures. In addition, the company is buying a portion of DuPont's crop protection unit which should make FMC the 5th largest crop protection company in the world, and potentially provides some upside accretion relative to original expectations.

## OUTLOOK

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We believe the market could experience more volatility in the coming quarters as the Federal Reserve continues to normalize interest rates, along with a focus on the ability of the Trump administration to enact infrastructure spending, deregulation, and corporate tax reform. Prospective tailwinds for the economy include further job growth, wage increases, lower tax rates, and simply more optimism from both businesses and consumers; all of which could lead to higher Gross Domestic Product (GDP) growth. On the other hand, potential headwinds include potential strengthening of the U.S. dollar, further increases in interest rates, and valuation metrics that are above historical market averages, leading us to believe that the stock market may have a hard time achieving further multiple expansion.

Despite the expectation of more volatility, we continue to spend considerable time analyzing companies that could provide greater risk-adjusted return potential to the portfolio. In addition, we remain true to our process of identifying companies that should potentially benefit from identified long-term trends that pass our disciplined valuation criteria. Going forward, we will continue to reduce positions with unfavorable risk-reward scenarios. We appreciate your continued support and confidence in our investment capabilities 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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*The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the investment company, and can be obtained by calling (800) 49-BUFFALO or visiting [buffalofunds.com](http://buffalofunds.com). Read it carefully before investing.*

As of 6/30/17 the Buffalo Mid Cap Fund's top ten equity holdings were: Kansas City Southern 2.25%, Zoetis, Inc. 2.00%, Equinix, Inc. 1.95%, Verisk Analytics, Inc. 1.93%, AmerisourceBergen Corp. 1.92%, Bio-Techne Corp. 1.88%, Air Products & Chemicals, Inc. 1.81%, MSCI, Inc. 1.75%, Nielsen Holdings Plc 1.74%, & CME Group, Inc. 1.67%.

Top 10 holdings for the quarter are not disclosed until 60 days after quarter end. Those listed are for the previous quarter.

The opinions expressed are those of the Portfolio Manager(s) 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 free-float capitalization-weighted index published since 1957 of the prices of 500 large-cap common stocks actively traded in the United States. Treasury bonds are debt obligations issued by the United States government. The Russell 3000 Index measures the performance of the 3,000 largest publically 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 a small-cap and micro-cap stock market index of the smallest 2,000 companies in the Russell 3000E Index incorporated in the U.S. based on market capitalization. The Russell 2000 Index is a small-cap stock market index of the smallest 2,000 stocks in the Russell 3000 Index based on market capitalization. The Russell Midcap Index measures performance of the 800 smallest companies in the Russell 1000 Index. The Russell 1000 Index is a subset of the Russell 3000 Index, which measures the performance of the 1,000 largest publically-held companies incorporated in the U.S. based on market capitalization. The Russell Midcap Growth Index measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth rates. You can not invest directly in an index.

#### **Earnings growth is not representative of the fund's future performance.**

Market capitalization is the total value of the shares outstanding of a publically traded company.

**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 include additional risk such as greater volatility, and political, economic, and currency risks, as well as difference 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.