

# Mid Cap Fund

PM Commentary as of December 31, 2017



## CAPITAL MARKET OVERVIEW

Equity markets ended 2017 on a strong note. The 4th quarter saw a continuation of trends that have influenced the market all year. Investor optimism about improving global economic growth and strong corporate earnings led to another quarter of higher stock prices and low volatility. Strong holiday sales and the passage of tax reform legislation also provided tailwinds to equity markets. The CBOE Volatility Index continued to hover near record lows, and, for the first time since 1958, U.S. equities delivered positive returns in every single month of the year.

The Russell 3000 Index produced a total return of 6.34% in the 4th quarter. Growth continued to outperform value, with the Russell 3000 Growth Index up 7.61%, beating the 5.08% return from the Russell 3000 Value. Large companies generally outperformed smaller companies during the quarter. The Russell 1000 returned 6.59%, the Russell Midcap Index returned 6.07%, the Russell 2000 returned 3.34%, and the Russell Microcap Index returned 1.80%. Consumer Discretionary and Technology were the best performing sectors in the 4th quarter. Consumer Staples, Health Care, and Utilities underperformed.

## PORTFOLIO MANAGEMENT TEAM



### Chris Carter, CFA

Co-Manager since 2017  
M.B.A. – Univ. of WI-Madison  
B.S. – Santa Clara University



### Josh West, CFA

Co-Manager since 2017  
M.B.A. – Univ. of MO-Columbia  
B.S. – Univ. of MO-Columbia

## PERFORMANCE COMMENTARY

In the 4th quarter the Buffalo Mid Cap Growth Fund returned 3.88%, trailing the benchmark Russell Midcap Growth Index return of 6.81%. The fund's underperformance was driven by unfavorable selection within the consumer discretionary, health care, and financials sectors.

Among the top contributors during the quarter were **Cavium**, **Verisk Analytics**, and **Dollar Tree**. Cavium shares traded higher on a buyout offer from Marvell that was accepted by the board. The acquisition is expected to close in the middle of 2018. For Marvell, the deal provides it with exposure to higher growth markets and diversifies its revenue away from the mature hard disk drive market.

Next, Verisk Analytics reported a favorable surprise in earnings that was a result of an inflection in growth. Its largest business segment, insurance analytics, was helped by hurricanes in Q3. Financial services and energy segments also contributed better results, marking the 1st time in several years all segments outperformed.

Finally, Dollar Tree shares were also driven higher by stronger than expected earnings. Sales growth exceeded expectations both at the flagship Dollar Tree stores and the recently acquired Family Dollar helping to drive operating margin leverage that resulted in earnings outperformance.

### Average Annualized Performance (%)

As of 12/31/17	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
<b>Buffalo Mid Cap Fund</b>	13.66	6.20	10.38	7.02	10.32	7.95
<b>Russell Midcap Growth Index</b>	25.27	10.30	15.30	9.10	11.96	9.04

*Expense ratio 1.02%. Inception Date 12/17/2001. 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).*

Detractors in the period were **Nevro**, **Twilio**, and **Expedia**. While Nevro revenues exceeded expectations for the quarter, the results were not enough to sustain shareholder optimism as shares traded lower. Nevro is taking significant market share with a clinically superior product in spinal cord stimulation, but deeper pocketed competitors have been successful in slowing share loss. Next, Twilio reported strong revenue results but gross margin disappointed leading investors to question its ability to reach its profit margin targets and drive earnings growth in the future. Finally, Expedia shares were under pressure during the quarter as the outlook for 2018 called for higher marketing spend that led analysts to revise earnings growth lower for the year.

## OUTLOOK

We are coming off a banner year for equity markets in 2017. Looking towards the near future, the economic outlook continues to support equity markets by providing an environment ripe for growth. Inflation and unemployment remain at low levels, while interest rates are expected to rise at a modest pace. In addition, the new tax code includes a tax cut for corporations, which should result in additional investment to support future growth. Many large corporations have also announced special bonuses or increased pay as a result of the tax break, which will support consumer spending growth as well.

While the economic outlook is robust, we are monitoring several potential risks to the markets. First, the threat of a potential military confrontation with North Korea remains as the U.S. seeks to prevent the development of nuclear weapons. Second, trade agreements such as NAFTA (*North American Free Trade Agreement*) may be dissolved or renegotiated, and abrupt changes would be impactful for many companies with operations in Mexico. Finally, valuations reflect a long standing bull market and represent a risk should investors turn pessimistic. Despite these risks, our outlook for 2018 remains positive. ◀

**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:

**Scott Johnson**  
sjohnson@buffalofunds.com  
(913) 754-1537

**Joe Pickert**  
jpickert@buffalofunds.com  
(913) 647-9875

*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. Read it carefully before investing.*

As of 9/30/17 the Buffalo Mid Cap Fund's top ten equity holdings were: Zoetis 2.02%, Verisk Analytics 1.92%, CME Group 1.83%, Equinix 1.81%, Bio-Techne 1.75%, FMC 1.67%, Xylem 1.60%, Air Products & Chemicals 1.55%, Nielsen Holdings 1.55%, Kansas City Southern 1.54%. 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 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 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 1000 Growth Index measures the performance of those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values. The Russell Midcap Index measures performance of the 800 smallest companies in the Russell 1000 Index. The Chicago Board of Options Exchange Volatility (CBOE) Index measures the market expectations of near-term volatility conveyed by S&P 500 stock index option prices. The Russell Microcap Index is a capitalization weighted index of 2,000 small cap and micro cap companies. You cannot invest directly in an index.

**Mutual fund investing involves risk. Principal loss is possible. The Fund invests in U.S. based companies with substantial interests outside of the U.S. which may involve additional risk such as greater volatility and political, economic and/or currency risks. This risk is greater in emerging markets. Earnings growth is not representative of the fund's future performance.**

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