

Capital Market Overview

The stock market extended year-to-date losses during the 2nd quarter. Inflation, rising interest rates, and economic uncertainty continued to be major headwinds for investors as recession talks gained traction. The S&P 500 Index fell -16.10% during the quarter, bringing the total return for the first half of the year to -19.96%. News headlines, which included energy shortages, the war in Ukraine, China's COVID lockdowns, and the potential for softer corporate earnings next quarter, added to the pessimistic market sentiment. However, the Federal Reserve's hawkish stance on inflation, expectations for additional interest rate increases, and a reduction in the size of its balance sheet, continued to signal confidence in the U.S. economy moving forward.

The broad-based Russell 3000 Index declined -16.70% in the quarter. Value stocks fell less than growth stocks as the Russell 3000 Value Index returned -12.41%, versus a return of -20.83% for the Russell 3000 Growth Index. Relative performance slightly favored market cap size as large caps outperformed small caps in the quarter. Larger cap stocks, as measured by the Russell 1000 Index, returned -16.67% compared to the smaller cap Russell 2000 Index return of -17.20% and the Russell Microcap Index return of -18.96%. There were no advancing economic sectors for the quarter, but Consumer Staples, Energy, Utilities, and Healthcare held up better on a relative basis. Consumer Discretionary, Information Technology and Communication Services areas lagged.

Small cap stocks were led lower by weakness in all sectors, though Information Technology stocks, Real Estate, and the Consumer Discretionary areas were hit harder, as those sectors all dropped more than 20% in the quarter. Meanwhile, the Energy and Materials sectors continued to outperform the Russell 2000 Growth Index, while more defensive sectors like Consumer Staples and Utilities predictably outperformed.

Fund Facts

| | Investor | Institutional |
|-----------------|---------------------------|---------------|
| Ticker: | BUFSX | BUISX |
| Inception Date: | 4/14/98 | 7/1/19 |
| Expense Ratio: | 1.01% | 0.86% |
| Fund Assets: | \$774.29 Million | |
| Category: | Small Cap Growth | |
| Benchmark: | Russell 2000 Growth Index | |

Management Team



Jamie Cuellar, CFA

Co-Manager since 2015
M.B.A. – Southern Methodist
B.B.A. – Univ. of San Diego



Bob Male, CFA

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

Performance Commentary

The Buffalo Small Cap Fund (BUFSX) produced a return of -19.18% in the quarter, a result that was in-line with the Russell 2000 Growth Index return of -19.25%. The Fund produced solid relative performance in Healthcare, Industrials, and Financials, while Technology, Consumer Discretionary, and Materials underperformed.

Average Annualized Performance (%)

| As of 6/30/22 | 1 YR | 3 YR | 5 YR | 10 YR | 15 YR | Since Inception |
|--|--------|-------|-------|-------|-------|-----------------|
| Investor Class - BUFSX | -38.09 | 8.87 | 11.44 | 11.16 | 8.02 | 11.40 |
| Institutional Class - BUISX ¹ | -38.00 | 9.04 | 11.61 | 11.33 | 8.18 | 11.57 |
| Russell 2000 Growth Index | -33.43 | 1.40 | 4.80 | 9.30 | 6.80 | 5.57 |
| Morningstar U.S. Small Growth Index | -36.23 | -0.14 | 4.97 | 9.05 | 6.84 | – |
| Lipper Small Cap Growth Fund Index | -27.91 | 4.53 | 9.06 | 10.76 | 7.32 | 6.90 |

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 Institutional 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

The largest contributor to Fund performance for the quarter was **Transmedics**, a healthcare equipment company with burgeoning product cycles around its Organ Containment System (“OCS”). OCS is used to transport hearts, livers, and lungs for organ transplants, and its National OCS Program (“NOP”), which provides organ explant and logistics services using its OCS product. The company is seeing excellent uptake of its product and services and remains in the early stages of its growth potential, by our analysis.

Privia Health was also a contributor to performance results. Privia, a healthcare services provider that partners with practitioners and helps them move to a value-based care model from fee for service, continued to differentiate itself from its peers due to its capital-light model and higher cash flow margins. The move to value-based care is still in its infancy, and we believe Privia will be a solid player in this growing industry.

↓ Top Detractors

Technology weakness was largely due to the underperformance of **TaskUs**, a Business Process Outsource (BPO) company that provides outsourced services, largely for other technology companies. The company reported better than expected results for the March quarter but failed to raise full year estimates due to an offshore transition from its largest customer, which lowers revenues in the near term. We believe the TaskUs offering can help companies looking to lower their costs by moving these functions offshore and should eventually garner more attention due to the weaker macroeconomic environment. As a result of the share price pullback, we believe the stock is undervalued and remains in the portfolio.

Outlook

With the worst first half performance for small cap stocks since 1973 now in the books, we believe that investors are close to pricing in a recessionary scenario for small companies that may or may not happen over the next 12 months. Historically, small caps underperform large caps going into a recession and outperform coming out of one. If small cap stocks have indeed nearly priced in a recession, as the historical data suggests, we could be entering a period where allocators might want to warm up to the asset class.

According to data from Jefferies (the investment banking and financial services firm), the small cap market as a percent of the total market is now less than 4% -- a level unseen since the 1930s and a sharp contrast from the peak of nearly 14% in 1984/1985. When relative performance between small caps and large caps has been this low, it is typically followed by a five-year period where the small cap asset class outperforms. Additionally, according to BofA Securities, the Russell 2000 Index's price-to-earnings ratio (P/E) is at 11.6x, the lowest since the market bottom of the global financial crisis in February/March of 2009.

There has also been a severe correction in high valuation areas such as medical technology and software. As a result, our investment opportunity universe has increased as many of those companies are now trading at more reasonable price levels. We believe near-term market volatility will remain high, especially entering the second quarter reporting period, where estimates for many companies will need to come down. For patient capital, willing and able to ride out near-term volatility, the market could be setting up a nice entry point into the small cap asset class.

At the portfolio level, we continue to focus on companies that benefit from long-term trends with a focus on higher quality characteristics, as measured by return on equity and balance sheet strength, that can withstand a period where access to capital may be constrained. We continue to look for companies with unique product cycles, pricing power, and those that can take market share, which should produce additional opportunities for growth.

As always, thank you for your continued trust and conviction in our capabilities over the long haul. We look forward to proving updates on better times. ▲

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 3/31/22 the Buffalo Small Cap Fund top 10 equity holdings were ICF Intl 2.55%, Air Transport Services Group 2.31%, Halozyme Therapeutics 2.23%, TaskUs 2.23%, Everi Holdings 2.18%, Privia Health Group 2.18%, MasTec 2.13%, Tenable Holdings 2.08%, NV5 Global 2.07%, FTI Consulting 2.00%. 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 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 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 1000 Index is a subset of the Russell 3000 Index and measures the performance of the 1,000 largest publicly-held companies incorporated in the U.S. based on market capitalization. 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 Microcap Index is an unmanaged capitalization weighted index of 2,000 small cap and micro cap companies. The Russell Midcap Index measures performance of the 800 smallest companies in the Russell 1000 Index. The Morningstar U.S. Small Growth Index measures the performance of U.S. small-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 Small Cap Growth Fund Index is an unmanaged, equally weighted performance index of the 30 largest qualifying mutual funds (based on net assets) in the Lipper Small-Cap classification. One cannot invest directly in an index. Price-Earnings Ratio or P/E Ratio is a ratio for valuing a company that measures its current share price relative to its per-share earnings.

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 involve greater volatility and political, economic and currency risks and differences 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.

