Buffalo Discovery Fund

QUARTERLY
COMMENTARY

June 30, 2023

Performance Commentary

The Buffalo Discovery Fund produced a return of 4.51% for the quarter versus an increase of 6.23% for the Russell Midcap Growth Index. Outperformance in the Industrials and Materials sectors was offset by underperformance in Technology and Consumer Discretionary. While we were expecting the market to gravitate towards growth stocks as the economy cooled and interest rates peaked, the magnitude of the rotation into the most expensive parts of the market was a significant headwind for the fund. Specifically, not owning four of the benchmark's most expensive technology stocks cost the fund more than 1.1% in relative performance during the quarter. The market also rotated into cyclicals as evidenced by strong performance from the Industrials sector. Airlines, automakers, homebuilders, and building products companies all continued a strong year-to-date performance run during the second quarter.

The market has clearly acquired an increased appetite for risk as of late. For the first time in more than a year, equity markets moved higher despite a meaningful rise in long-term interest rates. The 10-year Treasury yield jumped 30 basis points during the second quarter, yet the most expensive and cyclical parts of the market also moved higher. Defensive sectors—including Consumer Staples, Health Care, and Utilities—meaningfully underperformed. This suggests that investors are optimistic about a soft landing for the economy. In other words, markets believe the Federal Reserve can effectively tame inflation without inflicting too much economic damage due to the resilience of wage growth and employment, as well as multiyear benefits from the Infrastructure Investment & Jobs Act.

The expectation is that any recession will be short-lived, inflation will continue to trend lower, and the Fed will pivot to cutting short-term rates in 2024. This is certainly possible, but we are expecting management teams to offer cautious guidance for the back half of 2023 as consumers are still pinched by inflation and higher interest rates, labor costs remain elevated, and student loan payments are scheduled to resume in the fall. The focus of our strategy is unchanged: we invest in high-quality companies with fundamental competitive advantages that benefit from disruptive innovation. We manage risk by paying reasonable prices and analyzing potential downside risks. Given how far stocks have moved against a slowing macro backdrop, we would not be surprised to see increased volatility in the coming quarters.

Average Annualized Performance (%)

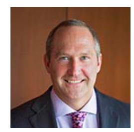
As of 6/30/23	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
Investor Class - *BUFTX*	19.47	6.63	7.61	11.23	11.48	8.99
Institutional Class - *BUITX*[1]	19.67	6.79	7.78	11.39	11.65	9.16
Russell Midcap Growth Index	23.13	7.63	9.71	11.53	10.21	9.03
Morningstar U.S. Mid Growth Index	19.57	5.91	10.01	11.70	9.62	8.37
Morningstar Mid-Cap Growth Category	17.25	6.99	8.35	10.61	9.33	7.17

[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. Each Morningstar category average represents a universe of funds with similar objectives.

Fund Facts

	Investor	Institutional
Ticker:	BUFTX	BUITX
Inception Date:	4/16/01	7/1/19
Expense Ratio:	1.00%	0.86%
Fund Assets:	$882.19 Million	
Category:	Mid Cap Growth	
Benchmark:	Russell Midcap Growth Index	

Management



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BUFFALO FUNDS

↑ Top Contributors

Copart, Inc. (CPRT) was the largest contributor to performance during the quarter. Copart is a leading provider of auction services for the automotive industry. Values for used vehicles spiked following the COVID pandemic due to supply chain disruption and strong consumer demand, and that negatively impacted the number of "total loss" vehicles being brought to auction by insurance companies. That dynamic is now reversing as auto production rebounds and used vehicle prices normalize. Copart is now projecting healthy volume growth with improving margins in 2023. Longer term, we see opportunities for international expansion and believe domestic salvage auction volumes will continue to rise as advanced vehicle technology and rising repair costs drive up total loss rates for insurers.

DoubleVerify (DV) was another top contributor for the quarter. The company is a leading software platform for digital media measurement and analytics. Channel checks on digital ad spend now indicate the category has stabilized following a challenging period that was negatively impacted by economic uncertainty and changes to Apple's consumer privacy policies. Despite these headwinds, DoubleVerify has continued to generate 20%-plus revenue growth. It is picking up new clients and expanding its product portfolio in digital media verticals such as social, streaming video, and retail. The largest opportunity for expansion remains at Meta Platforms, the parent company of Facebook and Instagram. Meta announced it will allow DoubleVerify to use its audience measurement and brand safety tools within its News Feed and Reels products. This gives us confidence in our projection for robust growth over the next few years. Consumer mindshare is shifting from traditional media outlets to online platforms, and marketers are increasingly demanding independent analysis of advertising ROI (return on investment) and brand safety.

↓ Top Detractors

MSCI Inc. (MSCI) was the top detractor from performance for the quarter. MSCI provides products and services to asset managers and financial advisors that enable them to analyze their holdings and make more informed decisions regarding risk and portfolio construction. Products include market indexes, environmental, social and corporate governance (ESG) solutions, and various tools related to portfolio construction, asset allocation, and risk management. Shares traded 15% lower after management gave full-year guidance that implied a slowdown in the company's ESG solutions business. The absolute decline in the stock price typically would not make it a top detractor, but it is a large position for the fund and occurred during a quarter when investors rotated away from stable subscription businesses into cyclicals and A.I. technology beneficiaries. While the move in the stock price was disappointing, MSCI remains a best-in-class financial services company that we believe can compound earnings at a double-digit clip for many years, driven by product innovation and pricing power.

Bio-Rad Laboratories (BIO) was also a detractor during the quarter. The company is a supplier of products and services to the life sciences industry, including reagents, consumables, diagnostic testing systems, and software. The company cut its earnings forecast following the release of first-quarter earnings. It is clear the life sciences and biopharma industries have not been immune from macroeconomic uncertainty and supply chain disruption, and some of the inventory stockpiling that took place during the pandemic is now being worked down. We believe the slowdown is temporary, though, and valuation is now compelling. After giving Bio-Rad Laboratories credit for its net cash position and stake in German bioprocess leader Sartorius, the company trades at roughly half the valuation of industry leaders Danaher and Thermo Fisher.

Outlook

2023 has started off with a bang for equity markets. While that seems counterintuitive for many investors given the outlook for slower economic growth, it hasn't been for us. We've been writing in these pieces for several quarters that inflation was peaking, the Fed's tightening cycle was approaching its latter innings, valuations were reasonable, and markets had already digested numerous headwinds in 2021 and 2022. Those headwinds include COVID, the launch of the Ukraine war, decades-high inflation, supply chain disruption, tight labor markets, and lapping more than $1 trillion of stimulus payments. We previously noted that periods of weaker economic expansion are often great times to invest in innovative growth stocks, as the best companies get smarter on expenses while still driving top-line growth and taking market share.

Looking forward, we must acknowledge that valuations are no longer as attractive given the market's recent run. Inflation is peaking, but the combination of tight labor markets and the Fed's "quantitative tightening" will likely keep interest rates elevated for several quarters. We also expect cautious guidance from most companies this earnings season. Consumers are dealing with high interest rates, elevated inflation, decelerating wage gains, and will soon have to begin repaying student loan payments. Surveys of small business hiring intentions have also rolled over, a potential prelude to rising unemployment. In short, we are expecting a choppy environment.

Against this backdrop, our strategy is to focus on our favorite innovative growth companies with a heightened awareness of potential cyclical risks. We are looking for industry-leading franchises with strong balance sheets and scalable business models trading at reasonable prices. This long-term, risk-aware view has served us well and we believe it will lead to a continued compounding of attractive returns over time. Thank you for your continued trust and support.

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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As of 3/31/23 the Buffalo Discovery Fund top 10 equity holdings were MSCI 2.88%, Copart 2.53%, Aptiv 2.07%, Natera 2.04%, DoubleVerify Holdings 1.89%, AMETEK 1.87%, Bio-Rad Laboratories 1.84%, Calix 1.79%, MGM Resorts International 1.76%, Ingersoll Rand 1.75%. Top 10 holdings for the quarter are not disclosed until 60 days after quarter end.

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 Nasdaq Composite Index is a market capitalization-weighted index of more than 3,700 stocks listed on the Nasdaq stock exchange. 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 Russel Microcap Index is a n 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. 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. 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. A basis point is one hundredth of a percentage point (0.01%). Yield is the income return on an investment. Refers to the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost, its current market value or its face value. A drawdown is a peak-to-trough decline during a specific period for an investment, trading account, or fund. The Bloomberg US Aggregate Bond Index is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States. Environmental, Social, and Corporate Governance (ESG) refers to the three central factors in measuring the sustainability and societal impact of an investment in a company.