

Buffalo Early Stage Growth Fund

QUARTERLY
COMMENTARY

December 31, 2023

Capital Market Commentary

2023 concluded with capital markets moving higher in the final quarter of the year. The S&P 500 Index gained 11.69% and the Bloomberg Aggregate Bond Index advanced 6.82%. A big pivot in expectations for the Federal Reserve's monetary policy drove the market advance during the period, as investors now anticipate a decline in interest rates for 2024. The yield of the U.S. Treasury 10-year note finished the quarter at 3.88%, a significant drop from its peak of nearly 5% in mid-October.

Recapping broad-based index results, the Russell 3000 Index gained 12.07% during the period. Growth stocks outperformed value stocks as the Russell 3000 Growth Index advanced 14.09% compared to a gain of 9.83% for the Russell 3000 Value Index. In typical "risk-on" fashion, relative performance improved going down in market capitalization (size) during the quarter as small caps advanced more than large caps. Larger cap stocks produced a return of 11.96%, as measured by the Russell 1000 Index, compared to the smaller cap Russell 2000 Index return of 14.03%. The even smaller market cap Russell Microcap Index rallied 16.06% in the quarter.

The stock market recorded impressive gains for 2023 with the S&P 500 Index advancing 26.29%. However, it was a "narrow" market as the "magnificent seven" technology and artificial intelligence (AI) stocks accounted for approximate 80% of the S&P 500's gains in 2023, versus a broad market advance where hundreds of stocks propel the index higher. In terms of economic sectors, technology, communication services, and consumer discretionary stocks were the brightest spots while the utilities and energy sectors declined in 2023.

Performance Commentary

The Buffalo Early Stage Growth Fund generated a return of 9.75% for the quarter compared to the Russell 2000 Growth Index return of 12.75% during the period. For calendar year 2023, the fund returned 9.83%. Small caps trailed their large cap counterparts significantly in 2023 with the Russell 1000 Growth (Large Cap) Index leading the way up 42.68%, the Russell Midcap Growth Index advanced 25.87% and the Russell 2000 Growth (Small Cap) climbed 18.66%. Further on down the market cap spectrum, the Russell Microcap Growth Index produced a return of 9.11% in 2023.

Average Annualized Performance (%)

As of 12/31/23	1 YR	3 YR	5 YR	10 YR	15 YR	Since Inception
Investor Class - BUFOX	9.83	-6.41	10.16	6.33	14.42	8.26
Institutional Class - BUIOX¹	9.98	-6.28	10.33	6.48	14.59	8.42
Russell 2000 Growth Index	18.66	-3.50	9.22	7.16	12.07	8.55

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.

The fund is positioned at the smaller end of the small cap spectrum as measured by the portfolio's weighted average market cap. This presented a consistent headwind in 2023 given the underperformance of smaller companies in the index.

On a sector basis, the fund underperformed in both the Healthcare and Technology sectors in the quarter. This was partially offset by outperformance in the fund's Industrials holdings.

In terms of individual stock detractors in the quarter, Establishment Labs again represented a material contributor to underperformance in the quarter. Establishment Labs (ESTA) is a long-time holding of the fund that came under significant pressure in the second half of calendar 2023. The company is an innovator in the Healthcare sector, bringing innovation to the breast augmentation and reconstruction space that

Fund Facts

	Investor	Institutional
Ticker:	BUFOX	BUIOX
Inception Date:	5/21/04	7/1/19
Expense Ratio:	1.50%	1.35%
Fund Assets:	\$80.21 Million	
Category:	Small Cap Growth	
Benchmark:	Russell 2000 Growth Index	

Management Team



Craig Richard, CFA

Co-Manager since 2013
M.B.A. – Univ. of Kansas
B.S. – Kansas State Univ.



Doug Cartwright, CFA

Co-Manager since 2015
M.B.A. – Univ. of WI-Madison
B.S. – Baylor University

Top 10 Holdings*

Kinsale Capital Group, Inc.	3.45%
Calix, Inc.	3.28%
Transcat, Inc.	2.94%
Compass Diversified Holdings	2.82%
Cadre Holdings, Inc.	2.82%
Federal Signal Corporation	2.76%
ICF International, Inc.	2.73%
Bowman Consulting Group, Ltd.	2.65%
Hamilton Lane Inc. Class A	2.63%
Verra Mobility Corp. Class A	2.58%
Top 10 Holdings Total	28.64%



has not had material innovation for close to 20 years. The company is currently in 80 countries, establishing leading market shares of greater than 30%, and most importantly, has a superior safety profile to legacy breast implant manufacturers. The incremental pressure on the shares in the quarter was due to significant slowing of demand for breast augmentation procedures in foreign geographies. Over half of all revenue comes from distributors who serve plastic surgeon practices. As the consumer showed some signs of weakness and economic conditions tightened, distributors put the brakes on orders and started to draw down existing inventories versus continuing to replenish. Additionally, the approval of the company's breast implants into the Chinese market remained delayed. The shares have rallied in early 2024 on the news of approval to enter the Chinese market and indications that distributor inventory destocking is behind them. Additionally, investors are refocused on the pending approval to enter the U.S. market which represents over half the global opportunity.

Kinsale Capital Group was another large individual drag to performance during the quarter. Kinsale is a specialty insurer focused solely on excess and surplus (E&S) lines. Gross premiums written grew 34% in the third quarter, which disappointed investors who had become accustomed to growth in the 40% and 50%. While the business will inevitably show signs of cyclical over time, we expect the company's technology platform and focus on E&S policies will allow them to continue to outperform in the segment. Kinsale enjoys a significant cost advantage over its peers which should allow it to continue to capture market share. In the E&S space, Kinsale has a 1-2% market share and continues to grow aggressively with the largest players in the space having 15% market share. There remains plenty of runway to allow Kinsale to continue to grow at an attractive rate as the E&S market continues to grow as a percentage of the overall property and casualty insurance marketplace.

On the positive side, Shift4 Payments was a recent addition to the Fund in the fourth quarter that performed well and was one of the top individual contributors. Shift4 is an integrated payments company with a legacy of providing payment solutions to the hospitality sector (hotels/restaurants). They have expanded into professional sports venues and are near agreements to launch ticketing solutions to go along with concessions. Additionally, they are just beginning international expansion through a recent acquisition. Along with delivering strong growth in the third quarter, the shares were bolstered by potential takeout interest given what we felt was a disconnect between the valuation and the results the company has been producing.

Outlook

While the employment environment remains strong, excess household savings accumulated during the pandemic are closer to being exhausted. In the fourth quarter, the Fed signaled a more dovish outlook and paused its aggressive interest rate hikes that began in March of 2022. As a result, small cap stocks experienced a sharp rebound intra fourth quarter with the Russell 2000 Growth Index rising approximately 25% from late October through the calendar year end.

As the economy shows continuing signs of growth and the Fed moves to a position of lowering interest rates and halts quantitative tightening, we are becoming increasingly more positive on the outlook for small cap stocks. Valuation levels of small caps relative to large caps remain at historically attractive levels. Additionally, the performance gap between small cap stocks and large cap stocks remains wide relative to historical levels, and we believe this performance gap will compress.

Our job remains to find and hold attractive small cap companies that have not been fully appreciated by the market or are mispriced due to recent results or events. We believe less investor interest in this segment of the market creates an opportunity for us to uncover value over the long term.

The fund typically invests at the smaller end of the small cap growth spectrum and the managers continue to seek companies with sustainable growth due to secular growth trends or innovative, disruptive products. The Buffalo Early Stage Growth Fund is focused primarily on identifying innovation within U.S. companies with primarily North American revenue bases. With an active share of greater than 90%, a lower turnover strategy with 50-70 holdings, the fund aims to continue to offer a distinct offering from the Index and category peers. ▀

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.

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 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 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 3000 Growth Index is an unmanaged index comprised of those Russell 3000 companies with higher price-to-book ratios and higher forecasted growth values. The stocks in this index are also members of either the Russell 1000 Growth or the Russell 2000 Growth indices. The Russell 3000 Value Index is an unmanaged index with a market-capitalization weighted equity based on the Russell 3000 Index, which measures how U.S. stocks in the equity value segment perform. The Russell Midcap Growth Index is an unmanaged index that measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values. One cannot invest directly in an index. Active share is a measure of the percentage of stock holdings in a manager's portfolio that differs from the benchmark index. Alpha is a risk-adjusted measure of the so-called active return on an investment. It is the return in excess of the compensation for the risk. An alpha of 1 means the investment's return on investment over a selected period of time was 1% better than the market during that same period; an alpha of -1 means the investment underperformed the market. 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. The Russell Microcap Index measures the performance of the microcap segment of the U.S. equity market. The Russell 2000 Growth Index is an unmanaged index that measures the performance of those Russell 2000 Index companies with higher price-to-book ratios and higher forecasted growth values. The Russell 1000 Growth is an unmanaged index that measures the performance of those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values. The price-to-earnings (P/E) ratio is a ratio for valuing a company that measures its current share price relative to its per-share earnings. Active share is a measure of the percentage of stock holdings in a manager's portfolio that differs from the benchmark index. Turnover is a measure of the fund's trading activity computed by taking the lesser of purchases or sales (excluding all securities with maturities of less than one year) and dividing by average monthly net assets. A turnover ratio of 100% or more does not necessarily suggest that all securities in the portfolio have been traded. In practical terms, the resulting percentage loosely represents the percentage of the portfolio's holdings that have changed over the past year. Benefits: A low turnover figure (20% to 30%) would indicate a buy-and-hold strategy. The Magnificent Seven is a term used to describe the technology-oriented, highly influential companies of Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla.

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.

*Top Ten Holdings for the quarter are not disclosed until 60 days after quarter end. Those listed are as of 9/30/23. Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any securities.

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

