

Specialty Finance BDC • Alternative Investment Strategies

The Specialty Finance BDC strategy is focused on a niche of the financial sector known as business development companies, or BDCs. BDCs lend to and invest in the private debt and equity markets. The majority, if not all, of the portfolio holdings are in BDCs, typically involving 20-30 positions with a moderate level of turnover. This strategy is appropriate for clients seeking alternative investment exposure to the private markets, one that involves high levels of income from an equity portfolio with above-average volatility. Most of the portfolio income will be in the form of non-qualified dividends.

Market & Strategy Commentary

The Confluence Specialty Finance BDC strategy had a total return of 2.8% (gross of fees) in the first quarter of 2022, which was below the benchmark total return of 3.9%. Across multi-year time frames, annualized gross portfolio returns are generally in line with the benchmark. [*The net-of-fees return for the same period was +2.0% QTD. See disclosures on p.3 for fee description; actual investment advisory fees may vary.*]

Although the economy and society continue to progress forward from the pandemic, the first quarter of 2022 was one characterized by a variety of concerns for investors. Inflation continued at levels not experienced for decades and equity investors fretted over how it might affect consumers and the economy. In addition, the financial markets kept a close eye on the Fed, which distanced itself from statements it had made in 2020, when it characterized inflation as “transitory.” Addressing inflation has become a top priority for the Fed, evidenced by a 0.25% increase in the fed funds rate in March, a move that included guidance of further rate hikes as well as quantitative tightening. Add to these concerns the war in Ukraine and a significant rise in interest rates, and it’s not surprising that equities struggled quite a bit in the first quarter.

In contrast, BDCs delivered relatively steady performance during the quarter. BDC stocks weren’t able to defy the gravity of big stock market downdrafts during the quarter; however, declines were milder, volatility was generally lower, and total return was helped by substantial dividend income. Operating fundamentals remained in good form and the industry reported record levels of new originations from the year-end period. The solid results helped BDCs extend the high dividend growth rates experienced in 2021. In the first quarter of 2022, nine BDCs in the Confluence Specialty Finance BDC portfolio increased their quarterly dividends and six paid special dividends. No dividend reductions took place during the first quarter.

As we look forward into 2022, we remain cautiously optimistic. Inflation, tighter Fed policy, and higher interest rates can all increase the likelihood of a recession. Furthermore, geopolitical risks are likely to remain elevated and this trend could weigh on equity investor sentiment and increase the volatility of stocks. Of course, BDC stocks are not immune from the risks of a recession, declining equity valuations, or rising volatility. However, BDC loan portfolios are generally in good shape and BDC managers have been prudent in managing their capital. Accordingly, we believe BDCs can continue to provide differentiated returns relative to other equity sectors, with a good proportion coming from dividends. At the end of the first quarter, the portfolio yield was 8.1%.

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5 Largest Holdings (as of 3/31/22)

Company	Market Capitalization <i>(\$ millions)</i>	Portfolio Weight
Sixth Street Specialty Lending, Inc.	1,770.2	6.6%
Barings BDC, Inc.	1,150.9	6.4%
Main Street Capital Corporation	3,057.0	6.0%
BlackRock TCP Capital Corp.	826.1	5.9%
Goldman Sachs BDC, Inc.	1,998.0	5.9%

Performance Composite Returns (For Periods Ending March 31, 2022)

	Since Inception**	5-Year*	3-Year*	1-Year	YTD	QTD
Pure Gross-of-Fees⁴	9.9%	7.7%	11.7%	19.4%	2.8%	2.8%
Net-of-Fees⁵	6.6%	4.5%	8.4%	15.9%	2.0%	2.0%
Benchmark (MVBIZDTG)	9.5%	6.9%	11.9%	20.4%	3.9%	3.9%

Calendar Year	Pure Gross-of-Fees ⁴	Net-of-Fees ⁵	Benchmark (MVBIZDTG)	Difference (Gross-Benchmark)	# of Portfolios	Composite Assets (000s)	Total Strategy Assets (000s) ^{***}	Total Firm Assets (000s)	Composite 3yr Std Dev	Benchmark 3yr Std Dev	Composite Dispersion
2011**	1.1%	0.9%	(0.7%)	1.8%	1	\$104	\$6,645	\$937,487	N/A	N/A	N/A
2012	27.9%	24.1%	34.5%	(6.6%)	1	\$133	\$34,748	\$1,272,265	N/A	N/A	N/A
2013	15.8%	12.4%	16.3%	(0.5%)	2	\$1,459	\$42,929	\$1,955,915	N/A	N/A	N/A
2014	(4.4%)	(7.2%)	(7.8%)	3.4%	18	\$3,644	\$51,015	\$2,589,024	9.7%	11.4%	0.0%
2015	(3.3%)	(6.2%)	(4.1%)	0.8%	25	\$4,621	\$51,912	\$3,175,419	12.0%	12.7%	0.3%
2016	22.1%	18.4%	24.4%	(2.4%)	21	\$3,857	\$64,970	\$4,413,659	13.1%	13.7%	0.8%
2017	0.9%	(2.1%)	0.1%	0.8%	19	\$2,905	\$55,878	\$5,944,479	12.4%	13.6%	0.3%
2018	(1.7%)	(4.6%)	(6.6%)	4.8%	24	\$3,702	\$54,037	\$5,486,737	11.1%	12.9%	0.2%
2019	25.0%	21.3%	27.3%	(2.3%)	35	\$7,179	\$57,964	\$7,044,708	10.9%	13.1%	0.5%
2020	(6.8%)	(9.6%)	(11.2%)	4.4%	33	\$6,782	\$27,280	\$6,889,798	31.6%	30.8%	1.0%
2021	32.0%	28.1%	36.4%	(4.5%)	38	\$9,856	\$20,805	\$7,761,687	31.4%	30.5%	0.7%

*Average annualized returns

**Inception is 12/1/2011

See performance disclosures on next page.

Portfolio Benchmark

MVIS U.S. Business Development Companies Index (MVBIZDTG) – A total return index that measures the performance of the largest and most liquid companies which are classified as BDCs in the U.S. The index is reviewed on a quarterly basis, is modified float market cap-weighted, and the maximum component weight is 20%.

(Source: Bloomberg)

The benchmark was changed prospectively starting 7/1/2021 as the prior benchmark, the Wells Fargo BDC Index (WFBDC), was discontinued in July 2021.

Disclosures

Market & Strategy Commentary—Information is presented as supplemental information to the disclosures required by GIPS® standards. Individual holding performance and contribution methodology as well as a list of every holding's contribution to the strategy can be obtained by contacting Confluence. Material is published solely for informational purposes and is not an offer to buy or sell or a solicitation of an offer to buy or sell any security or investment product. Opinions and estimates are as of a certain date and subject to change without notice. Past performance is no guarantee of future results.

Investment or investment services mentioned may not be suitable to an investor and the investor should seek advice from an investment professional, if applicable. It is important to review your investment objectives, risk tolerance, and liquidity needs before choosing an investment style or manager. All investments carry a certain degree of risk, including possible loss of principal, that investors should be prepared to bear. Equity securities are subject to market risk and may decline in value due to adverse company, industry, or general economic conditions. There can be no assurance that any investment objective will be achieved or that any investment will be profitable or avoid incurring losses.

Indices: The MVIS U.S. Business Development Companies Index is shown as additional information. This index is unmanaged. An investor cannot invest directly in an index. It is shown for illustrative purposes only & does not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance.

¹Largest Holdings—The listing of "5 Largest Holdings" is not a complete list of all stocks in the portfolio or which Confluence may be currently recommending. Application of the investment strategy as of a later date will likely result in changes to the listing. Individual client portfolios in the program may differ, sometimes significantly, from these listings. Contact Confluence for a complete list of holdings.

²Performance Composite Returns—Confluence Investment Management LLC claims compliance with the Global investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Confluence Investment Management LLC has been independently verified for the periods August 1, 2008, through December 31, 2020. The verification report is available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards.

Verification provides assurance on whether the firm's policies and procedures related to composite maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report.

GIPS® is a registered trademark of CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein. The Specialty Finance BDC strategy was inceptioned on December 1, 2011, and the current Specialty Finance BDC Composite was created on February 1, 2013. Confluence Investment Management LLC is an independent registered investment adviser. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

³ Pure gross returns are shown as supplemental information to the disclosures required by the GIPS® standards.

⁴ Net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite is as follows: 1.00% on the first \$500,000; 0.90% on the next \$500,000; and 0.75% over \$1,000,000. There are no incentive fees. Clients pay an all-inclusive fee based on a percentage of assets under management. The collection of fees produces a compounding effect on the total rate of return net of fees. Subsequent to February 1, 2013, bundled fee accounts make up 100% of the composite. Actual investment advisory fees incurred by clients may vary. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor.

Performance prior to February 1, 2013, is based on the Specialty Finance BDC—Direct Composite which was created on December 1, 2011. The Specialty Finance BDC—Direct Composite includes accounts that pursue the Specialty Finance BDC strategy, but do not have bundled fees. Gross returns from the Specialty Finance BDC—Direct Composite include transaction costs and net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly.

A complete list of composite descriptions is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. The annual composite dispersion is an equal-weighted standard deviation, using gross-of-fee returns, calculated for the accounts in the composite for the entire year. The three-year annualized standard deviation measures the variability of the composite gross returns over the preceding 36-month period. The Specialty Finance BDC Composite contains fully discretionary Specialty Finance BDC wrap accounts. The Specialty Finance BDC portfolio invests primarily in Business Development Companies (BDCs) to earn current income with potential long-term capital appreciation. **Results shown for the year 2011 represent partial period performance from December 1, 2011, through December 31, 2011. ***Total Strategy Assets are shown as supplemental information. N/A-Composite Dispersion: Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. N/A-3yr Std Dev: Composite does not have 3 years of monthly performance history.

A BDC's portfolio typically will include a substantial amount of securities purchased in private placements, and its portfolio may carry risks similar to those of a private equity or private debt fund. Securities that are not publicly registered may be difficult to value and may be difficult to sell at a price representative of their intrinsic value. To the extent a BDC focuses its investments in a specific sector, the BDC will be susceptible to adverse conditions and economic or regulatory occurrences affecting the specific sector or industry group, which tends to increase volatility and result in higher risk. BDCs may employ the use of leverage in their portfolios through borrowings or the issuance of preferred stock. While leverage often serves to increase the yield of a BDC, this leverage also subjects the BDC to increased risks, including the likelihood of increased volatility and the possibility that the BDC's common share income may fall if the interest rate on any borrowings rises.

About Confluence Investment Management LLC

Confluence Investment Management is an independent Registered Investment Advisor located in St. Louis, Missouri, that provides professional portfolio management and advisory services to institutional and individual clients. Confluence's investment philosophy is based upon independent, fundamental research that integrates evaluation of market cycles, macroeconomics and geopolitical analysis with the firm's value-driven, company-specific approach. The portfolio management philosophy begins by assessing risk and follows through by positioning clients to achieve their income and growth objectives.

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