



Specialty Finance BDC

Alternative Investment Strategies



First Quarter 2026

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, and most of the portfolio income will be in the form of non-qualified dividends. 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.

Market & Strategy Commentary

The Confluence Specialty Finance BDC strategy declined 9.5% (gross of fees) in the first quarter of 2026 compared to the benchmark's decline of 8.6%. Over multi-year periods, the strategy's gross returns have been roughly in line with the benchmark. [*The strategy's net-of-fees return over the same period was -10.2% QTD. See disclosures on last page for fee description; actual investment advisory fees may vary.*]

BDC valuations remained under pressure in the first quarter of 2026 as investor concerns regarding problems in private credit spilled into the new year. Those worries intensified during the quarter as speculation grew that artificial intelligence (AI) might disrupt software companies. As private credit lenders who often work with software borrowers, BDCs have been caught in the crosshairs of these anxieties.

Our view is that apprehensions surrounding the private credit markets have generally been misplaced and exaggerated. Granted, there have been some high-profile defaults and a modest amount of credit erosion; however, we aren't seeing widespread problems or degradations in borrower operating fundamentals. Certain software companies are struggling, although many of their challenges aren't related to AI. Furthermore, many other software borrowers are growing revenue and cash flow in healthy form. From our perspective, the exodus from BDC investments – especially among investors in private, non-listed BDCs, which are not included in our portfolio – reflects outsized concern with regard to potential credit problems. Valuations for publicly traded BDCs, in which the portfolio is invested, are well below long-term averages, while operating fundamentals remain generally intact.

For a granular evaluation of the first quarter, we note the biggest contributors to portfolio returns came from Capital Southwest, Trinity, MidCap, Kayne Anderson, and Nuveen Churchill. These BDCs are relatively small in the industry, with the exception of Capital Southwest. All of these names have experienced the industry's decline in valuation, although their movement during the first quarter was generally more mild. At the other end of the spectrum, some larger positions in the portfolio detracted more from return, including FS KKR, Hercules, Sixth Street, Main Street, and New Mountain. FS KKR and New Mountain have had challenges in their loan portfolios, though New Mountain was able to address many concerns by selling certain holdings. The other three BDCs maintained stable operating fundamentals, even as their valuations declined.

With the broad decline in BDC valuations, we opted to exit certain names and reallocate into existing positions that we expect to more successfully navigate the current environment. We sold relatively small positions in PennantPark and BCP, while adding to Kayne Anderson and MSC. As is normally the case, we were also able to reinvest dividends in many accounts, thereby adding to existing positions and building the long-term cash flow-generating profile of the portfolio.

As we look forward, we believe BDC valuations are likely to recover as further clarity on their operating fundamentals should help address widespread fears about the private credit market. Accordingly, we believe there is an attractive opportunity to invest in BDCs at current valuations. We do recognize that short-term interest rates have declined over the past year, and this environment may pressure BDC income lower as their floating rate loans decline in coupon. Still, this headwind may be offset by rising M&A volume, improvements in lending terms, and better pricing.

On the whole, we believe BDCs can continue to play an important role for investors, delivering a high level of income derived from an alternative investment asset class. Concerns regarding private credit are likely to continue, although we are already starting to see that reporting headlines are becoming a bit more balanced. In turn, investor response to these headlines has also become more measured. BDC valuations have lifted off low levels set in the first quarter and we believe there is a pathway forward for them to continue improving.

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Contribution¹

(YTD as of 3/31/2026)

The portfolio's top contributors and detractors thus far in 2026 are shown in this table:

Security	Avg Weight (%)	Contribution (%)
Top 5		
Capital Southwest Corp.	4.63	0.12
Trinity Capital Inc.	0.93	0.05
MidCap Financial Investment Corp.	1.65	0.03
Kayne Anderson BDC	2.02	(0.02)
Nuveen Churchill Direct Lending Corp.	1.59	(0.03)
Bottom 5		
New Mountain Finance Corp.	5.30	(0.66)
Main Street Capital Corp.	7.15	(0.78)
Sixth Street Specialty Lending Inc.	7.85	(1.06)
Hercules Capital Inc.	5.78	(1.12)
FS KKR Capital Corp.	3.49	(1.23)

(Contribution data shown from a sample account, based on individual stock performance and portfolio weighting)

Performance Composite Returns² (For Periods Ending March 31, 2026)

	Since Inception**	10-Year*	5-Year*	3-Year*	1-Year	YTD	QTD
Specialty Finance BDC							
<i>Pure Gross-of-Fees³</i>	7.9%	7.5%	5.9%	7.2%	(11.4%)	(9.5%)	(9.5%)
<i>Max Net-of-Fees⁴</i>	4.7%	4.3%	2.8%	4.0%	(14.0%)	(10.2%)	(10.2%)
MVIS US BDC Index (MVBIZDTG)	7.7%	7.2%	6.3%	6.8%	(12.9%)	(8.6%)	(8.6%)

Calendar Year	Pure Gross-of-Fees ³	Max Net-of-Fees ⁴	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%
2022	(10.2%)	(12.9%)	(8.6%)	(1.7%)	42	\$9,231	\$18,086	\$6,931,635	33.2%	32.7%	0.3%
2023	25.8%	22.1%	27.3%	(1.5%)	42	\$10,797	\$13,104	\$7,200,019	16.1%	17.6%	0.5%
2024	13.2%	9.8%	13.7%	(0.6%)	45	\$11,907	\$16,214	\$7,280,773	14.9%	16.5%	0.3%
2025	(0.7%)	(3.7%)	(3.5%)	2.8%	55	\$12,623	\$17,185	\$6,769,052	11.6%	11.7%	0.2%

*Average annualized returns

**Inception is 12/1/2011

See performance disclosures on last page.

Portfolio Benchmark

MVIS US 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)

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See [Territory Map](#) on the Confluence website for sales coverage.

Disclosures

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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.

Index: The MVIS US BDC 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.

¹ Contribution—Table showing the top 5 contributors/detractors reflects the strategy's best and worst performers (net), based on each holding's contribution to the sample account for the period stated. Individual holding performance and contribution methodology can be obtained by contacting Confluence.

² Performance 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, 2024. 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.

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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 US 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: 0.80% on the first \$500,000; 0.70% on the next \$500,000; and 0.60% 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.

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

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.