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 7.4% (gross of fees) in the second quarter of 2021, which was lower than the Wells Fargo BDC Index total return of 8.3%. For the year-to-date period, the strategy returned 21.9% (gross of fees) versus the benchmark return of 27.5%. The Confluence BDC strategy ended the first quarter with a dividend yield of 8.1%. [*Net-of-fees returns for the same periods were +6.6% QTD and +20.1% YTD. See disclosures on p.2 for fee description; actual investment advisory fees may vary.*]

Part of the disparity of returns between the strategy composite and the benchmark in 2021 reflects the strong relative returns being delivered by BDCs that are either not owned in the portfolio or are underweight relative to the benchmark. Many of these names rallied much later in the post-pandemic recovery period relative to many BDCs owned in the portfolio, which delivered high relative returns early in the recovery. On a cumulative basis, since the end of Q1 2020 through the end of Q2 2021, the strategy and benchmark have had similar returns.

BDC operating fundamentals remain in stable form. Many small to mid-sized businesses are still recovering, but the trends are positive, which generally extends into BDC loan metrics. With credit trends stable to improving, most BDCs are ramping up origination and taking advantage of growing loan demand among middle market borrowers. While these trends present good opportunities, an enormous volume of capital continues to flow into lending markets. As this capital looks for a home, it can compress lending spreads and tilt loan terms in favor of borrowers and away from lenders. As a result, we expect BDCs should continue to find good lending opportunities, but capital conditions could increasingly become more challenging.

One particularly bright spot has come from BDCs focusing on venture lending, which involves loans to venture capital companies. This industry seemingly didn't miss a beat during the pandemic and venture lending-oriented BDCs, including two in the portfolio, have had few credit problems. In addition, some loans have included equity investments and many of these had significant value accretion in recent quarters. The result has helped improved NAV for these BDCs and positioned them to increase distributions.

Looking forward, we are optimistic with regard to opportunities in BDC investments. BDCs successfully navigated the pandemic and are well-positioned to participate in the ongoing economic recovery. With valuations near long-term averages, we expect much of the total return from BDCs may be derived from dividends as opposed to capital appreciation, which is our expectation most of the time, meaning that BDCs can continue to fit into portfolios where current yield is an investment objective.

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5 Largest Holdings (as of 6/30/21)

Company	Market Capitalization	Portfolio Weight
	($ millions)	
Ares Capital Corporation	8,638.1	6.9%
SLR Investment Corp.	787.7	6.9%
Barings BDC, Inc.	689.7	6.5%
Sixth Street Specialty Lending, Inc.	1,611.4	6.4%
Main Street Capital Corporation	2,803.4	6.3%

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.

All investments carry a certain degree of risk, including possible loss of principal. It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager. Equity securities are subject to market risk and may decline in value due to adverse company, industry or general economic conditions.

Performance Composite Returns (For Periods Ending June 30, 2021)

	Pure Gross-of-Fees[1]	Net-of-Fees[2]	Benchmark (WFBDC)
Since Inception**	9.5%	6.2%	9.1%
5-Year*	9.7%	6.5%	9.0%
3-Year*	10.7%	7.4%	9.7%
1-Year	55.9%	51.3%	56.7%
YTD	21.9%	20.1%	27.5%
QTD	7.4%	6.6%	8.3%

**Average annualized returns*

***Inception is 12/1/2011*

Calendar Year	Pure Gross-of-Fees[1]	Net-of-Fees[2]	Benchmark (WFBDC)	Difference (Gross-WFBDC)	# 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%

Portfolio Benchmark

Wells Fargo BDC Index – A total return index that measures the performance of all Business Development Companies (BDCs) listed on the NYSE or NASDAQ that satisfy market capitalization and other eligibility requirements. *(Source: Bloomberg)*

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, 2019. 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 incepted 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.

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

[2] 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.

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. Holdings identified do not represent all of the securities purchased, sold or recommended. Information is presented as supplemental information to the disclosures required by GIPS® standards. Opinions and estimates are as of a certain date and subject to change without notice. Investment or investment services mentioned may not be suitable to an investor and the investor should seek advice from an investment professional, if applicable. Past performance is no guarantee of future results. Investing in securities involves the risk of loss of the amount invested that investors should be prepared to bear. 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 Wells Fargo 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.*