Third Quarter

2022

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 -7.5% (gross of fees) in the third quarter of 2022, which was slightly higher than the benchmark total return of -7.9%. Year-to-date, the portfolio gross return was -17.7%, slightly below the benchmark total return of -17.5%. Across multi-year time frames, gross portfolio returns are higher than the benchmark. [*The strategy net-of-fees returns for the same periods were -8.2% QTD and -19.5% YTD. See disclosures on last page for fee description; actual investment advisory fees may vary.*]

Although equity returns in the third quarter were negative, the broad decline wasn't nearly as acute as the second quarter trends. Equity markets have come to accept the consequences of tighter monetary policy, including the rising possibility of a recession. Second quarter downdrafts often involved a ray of hope that inflation and future Fed rate hikes might be abating, which would be dashed by ongoing inflationary trends, with no obvious end in sight. Small caps generally performed better than large caps and the Financials sector declined less than the broader market.

In this chart, we normalize the trend for BDCs (blue), the S&P 500 Index (white) and the Russell 2000 Index (red) year-to-date. It's apparent that all three followed similar trends at the same time, a condition reflecting a common response among equities to inflation and Fed policy. BDCs entered the third quarter having experienced less downside return compared to other equities and therefore had "a bit more to lose." As a result, BDC returns during the third quarter were below those of large and small caps, although on a year-to-date basis, the BDC industry maintains better performance.

Year-to-Date Performance of BDCs, S&P 500, and Russell 2000

(Source: Bloomberg)

Total Return	Q3 2022	YTD
S&P 500	(16.11%)	(19.97%)
S&P 500 Financials	(17.50%)	(18.73%)
Russell 2000	(17.21%)	(23.45%)
S&P Small Cap Financials	(13.18%)	(17.71%)
MVIS U.S. BDC Index	(13.81%)	(10.49%)
S&P LSTA Leveraged Loan Index	(6.21%)	(7.21%)
ML High Yield Master Index	(9.97%)	(14.04%)

(Source: Bloomberg, Confluence)

Market & Strategy Commentary continued...

Although BDC returns in the third quarter and over the course of the last year have been negative, the industry's operating fundamentals remain in good shape. BDCs managed to make it through the pandemic without serious problems and were able to take advantage of the low interest rate environment by issuing multi-year, fixed-rate bonds that locked in low borrowing costs. At the same time, BDCs positioned most of their assets in floating rate loans, a decision that has created a rising income stream as short-term interest rates have risen. And perhaps most importantly, BDC loan portfolios continue to have low levels of credit problems, with the weighted average non-accrual rate for the benchmark at 2.2%. For the Confluence Specialty Finance BDC portfolio, holdings at the end of the third quarter had a weighted average nonaccrual rate of only 1.9%.With portfolio loan credit in good condition, BDC managers are able to underwrite new loans with higher yields, taking advantage of higher interest rates and underwriting conditions that have moved in favor of lenders.

Stable operating fundamentals are likely to be important as we enter a period when economic growth could decline, and the likelihood of a recession is rather high. Low or declining growth conditions often create credit stress among borrowers, and we feel that pattern could be likely in the coming quarters. BDCs are unlikely to completely avoid the risk of rising corporate defaults. To address that risk, the portfolio remains focused on BDCs led by managers with strong track records, derived from time frames that include challenging economic and lending environments.

The positive dividend trend from the first half of 2022 continued into the third quarter, where eight BDCs in the portfolio increased their quarterly dividends and the seven paid special dividend distributions. Thirteen BDCs held their quarterly dividends steady, while one BDC reduced its dividend (this BDC has had a variable dividend distribution policy). These dividend increases reflect positive operating fundamentals and the rising portfolio income is helpful to address the challenges that come from higher inflation and rising interest rates.

We remain cautiously optimistic for positive results from the Specialty Finance BDC strategy. We believe experienced BDC managers can take advantage of dislocations in the credit and financial markets, while also managing credit risk in the private debt markets. It is our view that the income and gains from BDCs should remain differentiated relative to the broader equity and bond markets, providing important diversification to investors where income is an objective.

5 Largest Holdings[1] (as of 9/30/22)

Company	Market Capitalization ($ millions)	Portfolio Weight
Barings BDC Inc.	903.3	7.5%
Golub Capital BDC Inc.	2,117.4	7.3%
Sixth Street Specialty Lending Inc.	1,323.4	6.9%
SLR Investment Corp.	674.8	6.1%
Ares Capital Corp.	8,531.8	6.0%

Performance Composite Returns[2] (For Periods Ending September 30, 2022)

	Since Inception**	5-Year*	3-Year*	1-Year	YTD	QTD
Specialty Finance BDC *Pure Gross-of-Fees[3]*	7.2%	3.5%	1.5%	(13.8%)	(17.7%)	(7.5%)
Max Net-of-Fees[4]	4.0%	0.4%	(1.5%)	(16.3%)	(19.5%)	(8.2%)
MVIS U.S. BDC Index (MVBIZDTG)	6.8%	2.8%	1.2%	(13.5%)	(17.5%)	(7.9%)

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%

**Average annualized returns*
***Inception is 12/1/2011*
See performance disclosures on last 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.

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Disclosures

Market & Strategy Commentary—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.

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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.

[1] **Largest 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.

[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, 2021. 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.

[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.