Specialty Finance BDC Portfolio

as of 3/31/19

Portfolio Objective: The Specialty Finance Business Development Company (BDC) portfolio is focused on a niche of the financial sector where companies lend to and invest in the private debt and equity markets. The primary objective is income with growth as a secondary objective.

Portfolio Overview

This portfolio 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. Their corporate structure is one that avoids taxation at the corporate level as long as taxable income is distributed to shareholders. This structure, which shares similarities to Real Estate Investment Trusts (REITs), creates stocks with typically substantial dividend payments. The majority, if not all, of holdings in this portfolio are in BDCs, typically involving 20-30 positions with a moderate level of turnover. The BDC portfolio is suitable 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.

Investment Process

Although BDCs share a common organizational structure, they are varied in their focus and strategy. Some may be focused on particular industries, while others apply a more generalized approach. The companies can specialize in senior loans, or incorporate more exposure to junior loans or equity. Depending upon their size, BDCs may work with issuers that are larger with more liquid debt securities, or ones that are smaller with less liquid securities. The different approaches play a role in forming a variety of return/risk tradeoffs. Members of the Confluence team have analyzed and invested in BDCs since 2001 and our process evaluates BDCs individually and within the context of a complete portfolio. Over time, we believe this approach should generate substantial dividend income, while also positioning investors to participate in potential dividend growth and capital appreciation.

Security Selection – Management Skill and Valuations

- The capability of management to properly underwrite attractive private debt and equity investments is a critical part of a BDC's ability to deliver shareholder returns. Identifying managers with proven track records of successful underwriting is an important part of security selection.
- Valuations fluctuate over time and security selection involves buying BDCs where low valuations can create attractive return/risk opportunities.
- Yields vary across BDCs and security selection drives the construction of a portfolio where current yields, dividend growth, and capital appreciation potential are balanced with the various industry exposures.

Sell Discipline

To help preserve capital, portfolio positions are continually reviewed. A company's stock may be sold if:

- The share price reaches or exceeds our estimate of full valuation.
- More attractive opportunities are identified.
- The company's fundamentals deteriorate.
- The desired portfolio posture changes and necessitates rebalancing.

About Confluence Investment Management LLC

Confluence Investment Management LLC is an independent Registered Investment Advisor located in St. Louis, Missouri that was founded in 2007. Confluence provides professional portfolio management and advisory services to institutional and individual clients. The firm's investment philosophy is based upon independent, fundamental research that integrates our evaluation of market cycles, macroeconomics and geopolitical analysis with our value-driven, fundamental company-specific approach. Confluence's portfolio management philosophy begins by assessing risk, and follows through by positioning clients to achieve their income and growth objectives. The Confluence team has over 500 years of combined financial experience and 300 years of portfolio management experience.

Portfolio Characteristics[1]

	Portfolio
Wtd. Avg. Market Cap. ($B)	1.27
Median Market Cap. ($B)	0.78
Dividend Yield	8.9%
Number of Securities	20-30
Estimated Annual Turnover	20-30%

Yield data source: FactSet. Weighted average dividend yield of holdings in the portfolio, calculated based on annualized current dividends.

5 Largest Holdings[1]

New Mountain Finance Corporation	7.7%
Golub Capital BDC, Inc.	7.6%
Ares Capital Corporation	7.0%
TCP Capital Corp.	7.0%
Solar Capital Ltd.	6.9%

The listing of "5 Largest Holdings" is not a complete list of all stocks in the portfolio or which Confluence may be currently recommending. Furthermore, application of the investment strategy as of a later date will likely result in changes to the listing. Contact Confluence for a complete list of holdings.

There can be no assurance that a purchase of the stocks in this portfolio will be profitable, either individually or in the aggregate, or that such purchase will be more profitable than alternative investments.

[1]This information is presented as supplemental information to the disclosures required by the GIPS ® standards.

Firm Overview

The Confluence Mission

Our mission is to provide our clients with superior investment solutions and exceptional client service with the highest standards of ethics and integrity. Our team of investment professionals is committed to delivering innovative products and sound, practical advice to enable investors to achieve their investment objectives.

Confluence INVESTMENT MANAGEMENT

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as of 3/31/19

Composite Returns

For Periods Ending 3/31/19

	Pure Gross-of-Fees[1]	Net-of-Fees[2]	Benchmark (WFBDC)
QTD	13.3%	12.5%	14.3%
YTD	13.3%	12.5%	14.3%
1-Year	14.0%	10.6%	9.7%
3-Year Annualized	9.8%	6.5%	8.4%
5-Year Annualized	5.1%	2.0%	3.5%
Since Inception* Annualized	9.1%	5.9%	8.5%

	Pure Gross-of-Fees[1]	Net-of-Fees[2]	Benchmark (WFBDC)
2018	(1.7%)	(4.6%)	(6.6%)
2017	0.9%	(2.1%)	0.1%
2016	22.1%	18.4%	24.4%
2015	(3.3%)	(6.2%)	(4.1%)
2014	(4.4%)	(7.2%)	(7.8%)
2013	15.8%	12.4%	16.3%
2012	27.9%	24.1%	34.5%
Dec 2011*	1.1%	0.9%	(0.7%)

**Inception is 12/1/11*

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.

What is a BDC?

BDCs are Business Development Companies and were formed under Congressional amendments to the 1940 Investment Company Act, which were made in 1980. The formation of BDCs was intended to help facilitate the flow of capital into companies whose small size precluded access to the broader public markets. Accordingly, public BDCs are companies that lend to and invest in the private debt and equity markets. Their structure is somewhat similar to that of Real Estate Investment Trusts (REITs) in that they generally do not pay income taxes at the corporate level, so long as their taxable income is distributed to shareholders.

Because BDCs are regulated by the 1940 Act, there are additional requirements that are mandated in their capital structure. One of the most important ones is related to the amount of debt a BDC may carry. In most instances, a BDC is limited to 1:1 debt/equity; this limitation means that BDCs operate with substantially less leverage relative to other financial industries, where debt proportions are often several multiples of equity. Regulations also determine the kinds of eligible investments and require certain levels of diversification.

While some BDCs focus on private equity, most BDC portfolios are oriented toward private debt. Interest is collected on these portfolios, operating and management fees are paid, and the residual net interest income is distributed to shareholders. This structure means that most BDCs have substantial dividends. BDC yields are generally much higher than other equities (most BDC dividends are not qualified dividends) and income from these stocks typically represents a substantial portion of the total return of the security.

Although the BDC industry was damaged by the financial crisis of 2008, the relatively low level of leverage helped it survive better than many other industries in the financial sector. Furthermore, because BDCs did not receive special direct government assistance, they have not faced a punitive environment afterward. The recovery of the BDC industry happened much earlier relative to other financial industries. In recent quarters, many new BDCs have entered the public markets, while most existing ones have been able to raise debt and equity capital and grow.

We believe the BDC industry has an attractive growth profile. Because this growth opportunity is derived from loans and investments made in the private debt and equity markets, it may have an “alternative asset” profile that is somewhat differentiated from other more traditional investments. Still, companies in this industry are generally quite small. Volatility can be very high, while liquidity may be low. Furthermore, BDCs are often damaged by recessions and downturns in credit markets. We believe a partial allocation to this industry may be constructive for risk-tolerant investors seeking total return with a substantial proportion derived from current yield.

Confluence claims compliance with the Global Investment Performance Standards (GIPS®).

[1]This information is presented as supplemental information to the disclosures required by the GIPS ® standards.
The Specialty Finance BDC strategy was incepted on December 1, 2011 and the current Specialty Finance BDC Composite was created on February 1, 2013. 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-of-fees and net-of-fees and include the reinvestment of all income. Pure gross-of-fees returns are shown as supplemental information. 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.

[2] Net-of-fees 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 2/1/13, 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.

A complete list and description of composites and/or fully compliant GIPS® presentations are available upon request. Additional information regarding policies for calculating and reporting returns is available upon request. The Specialty Finance BDC Composite contains fully discretionary Specialty Finance BDC direct accounts. The Specialty Finance BDC portfolio invests primarily in Business Development Companies (BDCs) to earn current income with potential long-term capital appreciation.

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