RADNOR
FINANCIAL ADVISORS

QUARTERLY MARKET COMMENTARY

First Quarter 2021

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Committed to Positively Impacting Our Clients' Lives

Enclosed is our March quarterly commentary. 2021 has started off positively, with markets buoyed by vaccinations, continued accommodative monetary policy and a new round of fiscal stimulus. Expectations are for a strong economic recovery, especially in the second half of 2021 as we (hopefully) move past the pandemic and release pent-up demand.

As the economy re-starts, we recognize this may be a more unusual economic cycle. We are emerging from a recession driven by pandemic measures (shutdowns, social distancing, etc.) rather than the more traditional economic and financial difficulties. Therefore, there is likely a higher amount of uncertainty in the outlook.

While vaccine distributions are proceeding, the progress is uneven across states/countries. We also continue to face new variants, which appear to be more contagious. This may result in some fits and starts to the economic recovery.

Globally, governments passed large fiscal stimulus packages in the wake of the pandemic. Given the dovish monetary policy, increased fiscal stimulus and re-starting of the economy, inflation concerns are surfacing. As activity ramps ups, we are likely to see some upward pressure on prices. The question is whether the bump up in inflation will be temporary or more persistent (and thus requiring Fed action).

Fixed income investments have already started to react to the potential higher inflation environment. The yield on the 10-year Treasury Bond increased from 0.93% at the beginning of the year to 1.74% at the end of March. If inflation turns out to be transitory, fixed income markets should settle down.

Equity markets have continued their astonishing recovery, up some 80% from the March 23rd, 2020 lows. Clearly, it paid not to panic and get out of the markets last spring, despite the natural fear and uncertainty everyone was feeling at the time. As we noted previously, markets are resilient, but require patience.

Looking forward, the primary variables that will determine the direction of the economy and markets remain Covid-19 developments and fiscal/monetary policy. These currently suggest a strong economic rebound. This should continue to support stocks.

However, as we move past the pandemic environment, we are concerned that returns may be more moderate as the benefits from fiscal and monetary stimulus fade. This is especially concerning for fixed income markets, where it will be difficult to generate attractive returns as rates begin to normalize. As such, we expect to continue to seek non-traditional investments that we can add to portfolios to provide attractive base returns and provide some inflation protection.

We continue to seek to build balanced portfolios that can be resilient across a range of potential scenarios, while providing the opportunity to generate attractive returns over time. In doing so, we will remain patient and disciplined, with a longer-term focus. As always, we remain available to assist if you, your family, or friends have any questions or concerns.

- As we look back over past year, much has changed. We experienced a global pandemic which shut down economies and resulted in a short, but severe global recession. Governments undertook unprecedented action, we endured stormy elections, we witnessed social and racial injustice, and we suffered an unimagined death toll from Covid-19.

- From a market perspective, the shutdown of the economy resulted in the quickest decline into a bear market in history (16 days) and saw the S&P 500 decline 34% from peak to trough. We then experienced the quickest recovery in history. In the span of 6-months, we went from a market peak, to a sharp bear market drawdown, to new market highs. The resiliency and anticipatory nature of markets is truly remarkable.

- In the first quarter of 2021, equity investors experienced another quarter of attractive returns, with the S&P 500 up 6.2%, the Russell 2000 up 12.7%, and the MSCI EAFE up 3.5%. Bonds didn't fare as well, falling -3.4% given rising interest rates.

- During the pandemic, the US lost about 22 million jobs, resulting in an unemployment rate of 14.7%. We have since recovered more than half the jobs lost and the unemployment rate has declined to 6.0%.

- Substantial progress is being made with the vaccine rollout. At the current vaccination rate, experts estimate that the United States may achieve herd immunity this summer. While we are not out of the woods yet, there certainly seems to be a light at the end of the pandemic tunnel.

Investment Performance (Total Return) 03/21

	1Q	1-Year	3-Year	5-Year	10-Year	15-Year
S&P 500	6.2	56.4	16.8	16.3	13.9	10.0
Russell 1000 Growth	0.9	62.7	22.8	21.1	16.6	12.4
Russell 1000 Value	11.3	56.1	11.0	11.7	11.0	7.7
Russell 2000	12.7	94.9	14.8	16.4	11.7	8.8
Russell 2000 Growth	4.9	90.2	17.2	18.6	13.0	10.1
Russell 2000 Value	21.2	97.1	11.6	13.6	10.1	7.4
MSCI EAFE	3.5	44.6	6.0	8.9	5.5	4.1
MSCI EAFE SC	4.5	62.0	6.3	10.5	8.0	5.7
MSCI EME	2.3	58.4	6.5	12.1	3.7	6.0
Wilshire REIT	8.8	34.7	9.0	5.0	8.5	5.8
HFR Fund-of-Funds Comp	2.5	24.6	5.6	5.7	3.5	2.9
Barcap Aggregate Bond	-3.4	0.7	4.7	3.1	3.4	4.3
Barcap Muncipal	-0.4	5.5	4.9	3.5	4.5	4.4
Bloomberg Commodity	6.9	35.0	-0.2	2.3	-6.3	-3.4

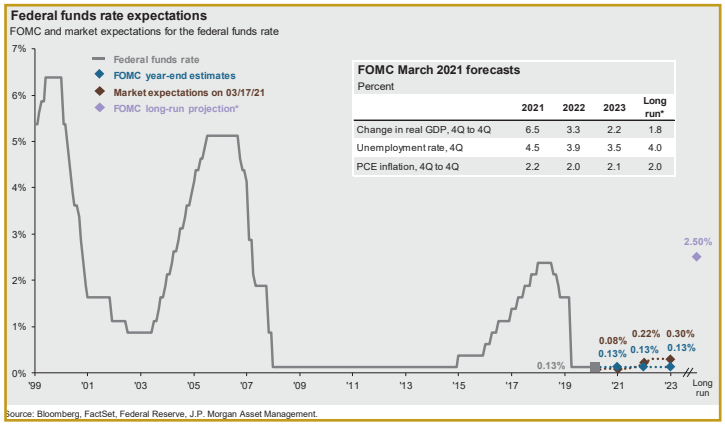
- With Democrats in control of the Executive and Legislative branches, we saw passage of the $1.9 trillion American Rescue Plan and the Biden administration recently proposed a $2 trillion infrastructure plan (which includes increases in spending and in taxes).

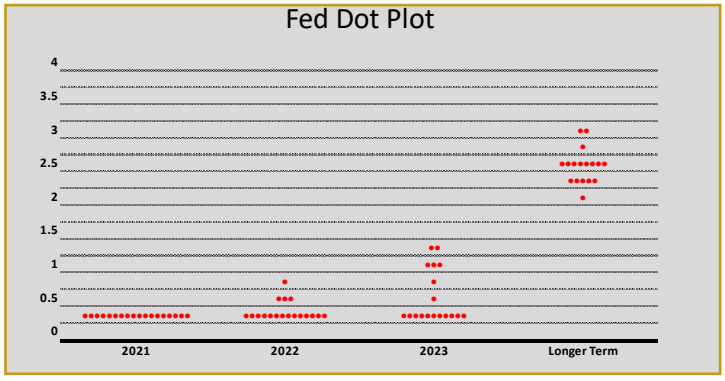
- As we look forward, the underlying conditions for a recession seem a long way off, as tightening credit conditions seem unlikely in 2021 and 2022. We could certainly see periods of market volatility, but there are powerful tailwinds moving the economy (and likely equities) forward.

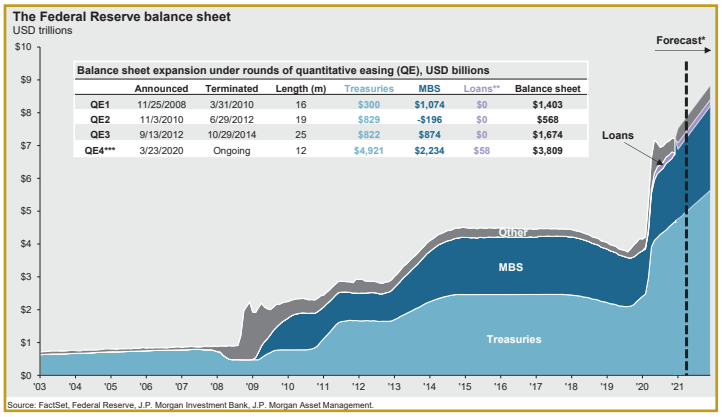
- Sticking to a long-term investment plan in the case of extreme uncertainty is difficult. We were all stressed out last March (both for investment market reasons and for the uncertainty associated with Covid 19 health concerns). Every crisis is different, and the pandemic was especially unusual. We can't control a crisis, but we can control how we respond. We seek to maintain an even keel and focus on the basic investment principles: be patient, diversify, rebalance, and focus longer-term.

FEDERAL RESERVE: SUPPORT AS LONG AS IT TAKES

- The Fed continues to signal that it intends to remain supportive of the economy. Following the March FOMC meeting, the Fed maintained the federal funds rate at a target range of 0.0% - 0.25% and continued to suggest they expect rates will remain near zero through 2023 (see dot plot chart).
- The Fed also indicated it would continue bond purchases at a pace of $120 billion per month until substantial further progress is made in the recovery. As such, the Fed's balance sheet will continue to expand.
- The Fed has reiterated its average inflation targeting framework. Under inflation targeting, the Fed will allow inflation to run moderately above its 2% target for some time to make up for periods where inflation undershoots this target, such that inflation averages 2% over time. While the Fed expects to see some upward pressure on prices in the short-term, they don't expect the effect on inflation to be particularly large nor persistent.
- Federal Reserve Chairman Powell recently indicated the Fed is not worried about the federal debt given the current low level of interest rates. However, he noted that when the economy is back to full employment and we are in a strong economy again it will be appropriate to get back on track to a sustainable fiscal path.
- Chairman Powell also recently indicated "the recovery has progressed more quickly than generally expected and looks to be strengthening. But the recovery is far from complete, so, at the Fed, we will continue to provide the economy the support that it needs for as long as it takes."

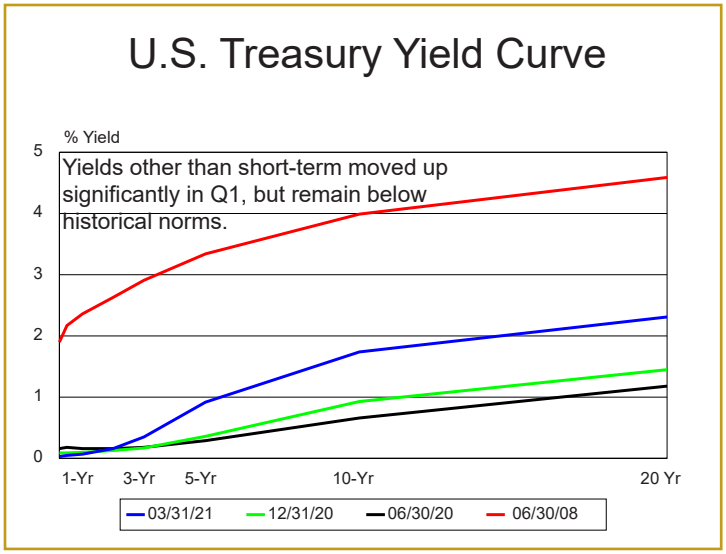


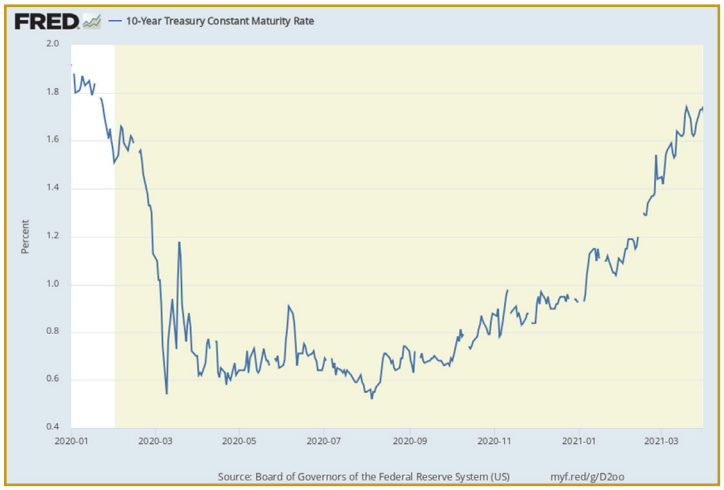




FIXED INCOME: YIELD RECALIBRATION

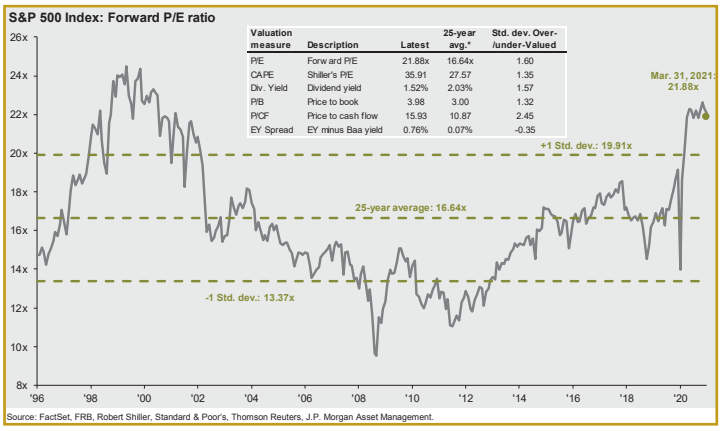
- The Bloomberg Barclays US Aggregate Bond Index was down -3.4% in Q1, reflecting the rising rate environment in response to a more promising economic outlook.
- The BofA High Yield Index was up 0.9% in Q1, while the S&P Levered Loan Index was up 1.8% and the JP Morgan EM Bond Index was down -4.5%.
- The yield on the 10-year Treasury bond ended the quarter at 1.74%, substantially higher than the 0.93% yield at year-end and the 0.52% low in August of 2020.
- Thus far, 2021 has been a challenging year for bond investors. With the economy expected to recover significantly in the second half of 2021, inflation is likely to rise. The Fed expects this increase to be transitory. If it is not, we could see increased pressure on the prices of goods and services.
- Within balanced portfolios, we remain concerned that generating attractive returns from traditional fixed income investments will be challenging. Bond yields remain one of the best measures of their return over time, and current low yields suggest low-return potential.
- Despite the low return expectations for bonds, they can continue to play an important role in portfolios, providing stability to offset the volatility of equities.
- Given the expected challenging environment for fixed income, we continue to prefer flexible bond funds and stable value funds (where available). Flexible bond funds can invest in a broader opportunity set and structure their instruments to reduce interest rate risk. We also continue to look to add non-traditional, less liquid fixed income investments, which can provide attractive returns with low correlation.





US EQUITIES: ANTICIPATORY NATURE OF EQUITIES

- Stocks saw some volatility but powered through in Q1, with the S&P 500 up 6.2%. US small-cap stocks performed even better, up 12.7%, reflecting some rotation in the markets.
- Value stocks have outperformed growth stocks thus far in 2021, continuing the positive performance since September of 2020. Small-cap value stocks performed exceptionally well in Q1, up 21.2%.
- Even with the recent rally, value stocks appear to remain cheap vs. growth stocks and can continue to outperform in the near-term. However, once we get past the pandemic recovery, growth is likely to revert to a slower pace, and growth stocks have traditionally performed better in a slow growth environment. As such, we are likely to maintain a balanced approach.
- Stock prices based on forward PE ratios appear elevated. However, earnings are likely to grow significantly in 2021, which should lead to some compression in the ratios. In addition, the low interest rate environment may justify a higher valuation above historical averages.
- However, there may be headwinds for equities going forward from rising interest rates, higher tax rates, and potential wage pressures. As such, we expect returns may be more modest over the next 5-years.

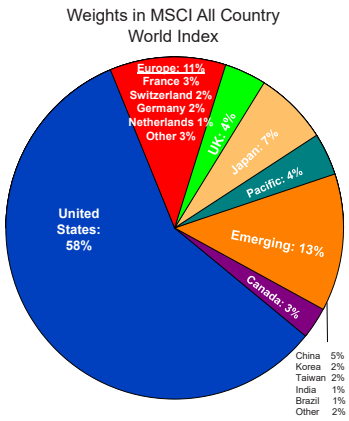


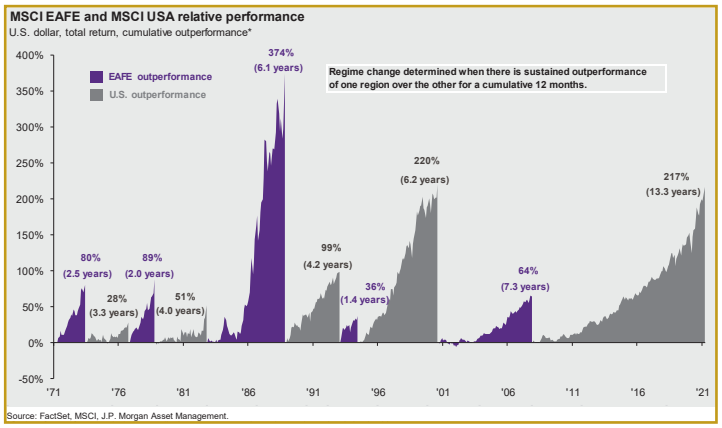
INTERNATIONAL STOCKS: CYCLES OF PERFORMANCE

- Developed international stocks were up 3.5% in Q1, with international small-cap stocks doing a little better (+4.5%) and emerging market stocks doing a little worse (+2.3%).
- Of the 23 developed markets countries in the MSCI EAFE Index, all but two were positive in Q1 (Portugal and New Zealand).
- The US dollar made modest gains in Q1, rising +7.1% vs. the Yen, +4.1% vs. the Euro and +2.2% vs. the world basket.
- The timing and pace of Fed policy normalization relative to other central banks will influence future dollar movements, although increased deficits lead many to expect a weaking dollar over time.
- The economic outlook in Europe is shakier, as delays in rolling out vaccinations have led to another round of lockdowns, thus delaying economic reopening.
- The European Central Bank has pledged ongoing support via the Pandemic Emergency Purchase Programme (PEPP), seeking to assure that financial conditions don't tighten too soon or too much.
- Japan has introduced policies on corporate governance. Given that the Government Pension Investment Fund and Bank of Japan are large corporate investors, it will be interesting to see how this plays out.
- US stocks have outperformed international stocks for over 13 years; an incredibly long period given that past cycles of outperformance have generally been less than half of that. Recognizing that outperformance has been cyclical, perhaps we are nearing a period where international stocks will begin to outperform.

International Returns: Local Currency vs. U.S. Dollars

	Q1 2021		2020	
	Local	US Dollars	Local	US Dollars
USA (S&P 500)		6.2		18.4
MSCI EAFE	7.6	3.5	0.8	7.8
MSCI EAFE Growth	3.8	-0.6	10.4	18.3
MSCI EAFE Value	11.3	7.4	-8.7	-2.6
MSCI EAFE Small Cap	8.4	4.5	5.1	12.3
MSCI EAFE Europe	7.6	4.1	-2.2	5.4
MSCI EAFE Pacific	7.8	2.5	6.2	11.9
MSCI Emerging Markets	4.0	2.3	19.1	18.3

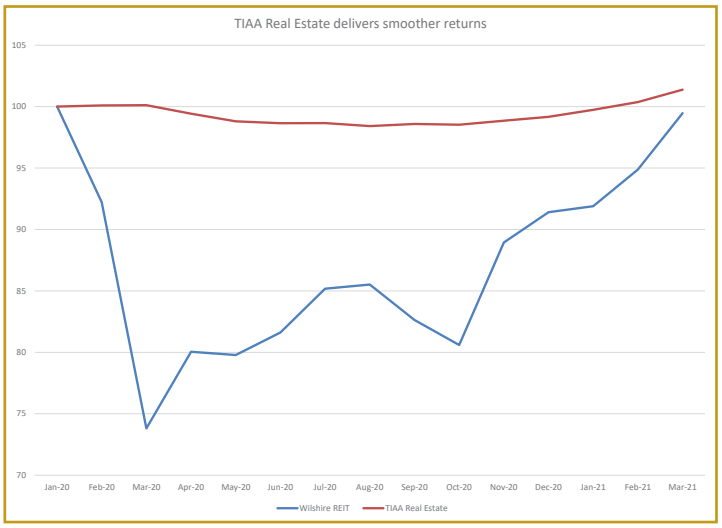




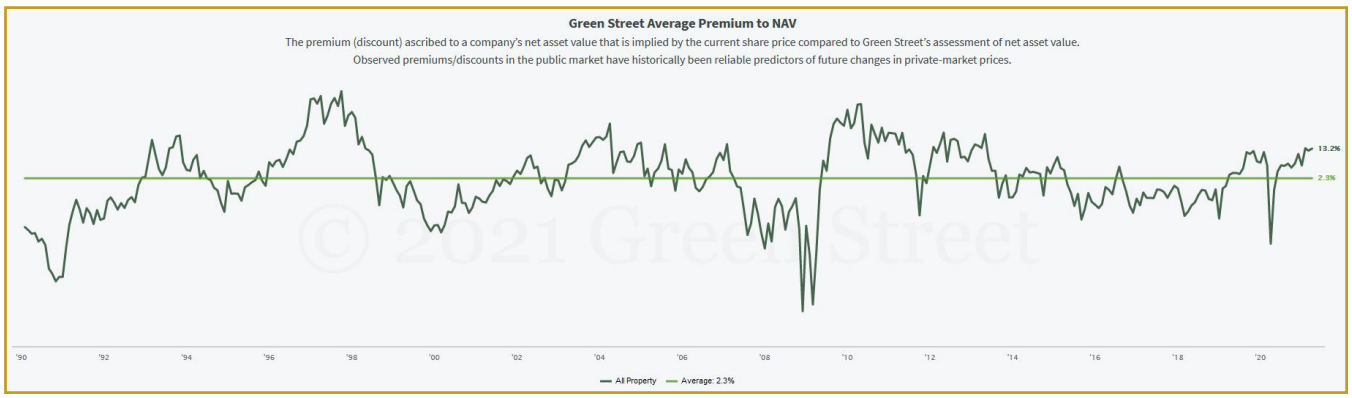
- Overall, we continue to believe international equities should remain a core component of a well-diversified portfolio. International equities provide exposure to different economic conditions, currencies, and demographics, thereby expanding the universe of investments and potential returns.

REAL ESTATE: REGAINING LOST GROUND

- REITs had a good start to the year, up 8.8% in Q1, recovering back to pre-Covid levels. Direct real estate (Green Street CPPI) was up 2.5% in Q1, but still down about 5% from pre-covid levels.
- Commercial real estate is going through a period of greater uncertainty as owners, renters and lenders navigate the Covid environment. While real estate values are well above their pandemic lows of last spring, uncertainty persists.
- The pandemic is having a significant impact on both commercial and residential real estate. For institutional investors, exposure to traditional office and retail will likely shrink, accelerating trends already in place.
- The progress in the deployment of vaccines should increase the pace and planning of workers returning to the office. However, there will be increased acceptance of remote work, with the likely result a flexible workweek, with some time spent in the office and some time spent remotely. On balance, this should lead to a reduction in office demand.
- Looking ahead, we expect real estate focused on alternative property types to gain wider acceptance. Greater need for healthcare will increase demand for medical offices, life science facilities and senior housing. Similarly, increased use of technology will result in strong demand for data centers and cell towers.

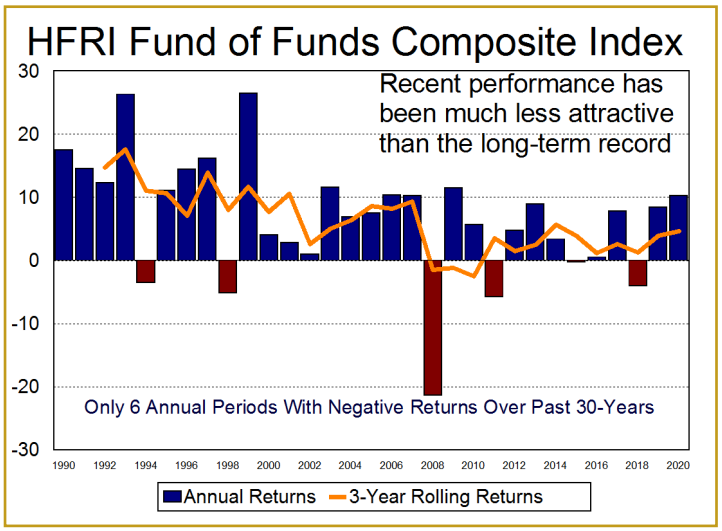


- While there are a number of concerns in the real estate space, yields remain stable and attractive relative to fixed income. A well- diversified real estate portfolio can provide a consistent, tax-efficient income stream.
- We continue to believe that real estate can be an attractive component of a well-diversified portfolio. It provides an attractive source of income, while having a low correlation to traditional stocks and bonds and provides a degree of inflation protection (from rising rental income and property values over time).
- For investment in real estate, we generally prefer private/ direct real-estate as it has tended to exhibit lower volatility historically than publicly traded REITs.



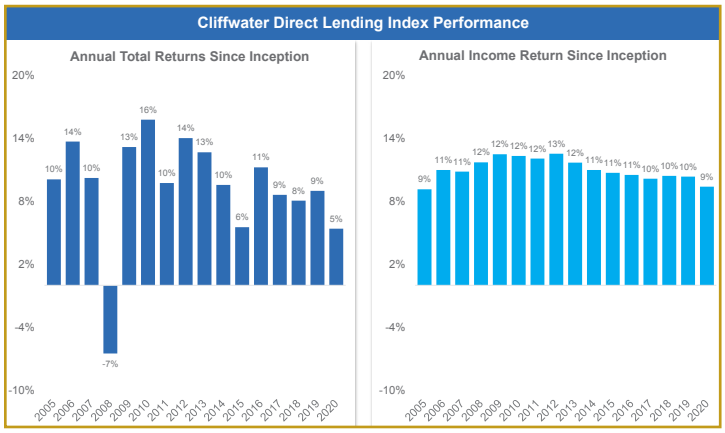
HEDGE FUNDS: FIXED INCOME REPLACEMENT?

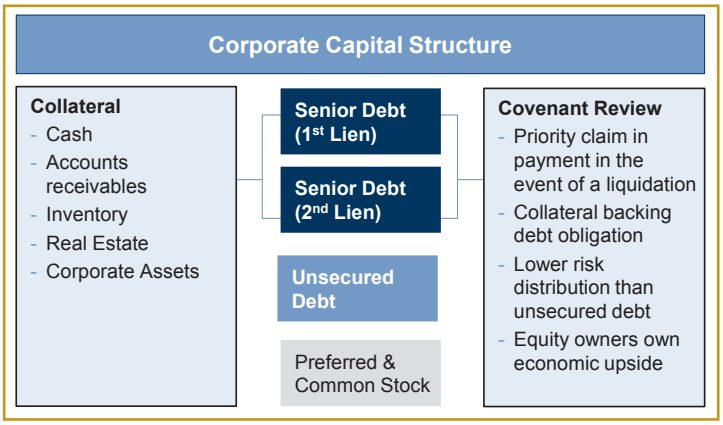
- The HFRI Hedge Fund-of-Funds Composite was up 2.5% in Q1. Despite the continued negative headlines on hedge funds, institutional investors are increasing their use of hedge funds as a replacement for low-returning bond investments.
- In an environment with potentially more modest returns for traditional investments, the appeal of hedge funds remains their potential to generate attractive risk-adjusted returns with low correlation to stocks and bonds.



BDCS: ATTRACTIVE RETURNS; LOW CORRELATION

- The Wells Fargo BDC Index's total return in Q1 was 17.7%, reflecting the continued rebound in middle market loans.
- We continue to find the middle market loan space attractive. As bank lending has retreated, private credit has stepped in to meet the continued borrowing demand.
- Private lenders can negotiate more attractive terms (yields, covenants, etc.) by offering borrowers higher certainty of closure, fast execution, and consistency of terms once set (i.e., less impact from changing market conditions).
- Investing in direct lending provides an opportunity to earn an attractive return while investing in loans that are senior secured and primarily floating rate (thus providing a hedge against rising interest rates and inflation). Middle market loans provide an illiquidity premium, offer attractive yields, and generally have exhibited lower defaults and higher recovery rates. In addition, the quarterly NAV results in more moderate volatility.





QUOTES OF NOTE:

"Productive assets such as farms, real estate and, yes, business ownership produce wealth – lots of it. Most owners of such properties will be rewarded. All that's required is the passage of time, an inner calm, ample diversification, and a minimization of transactions and fees."

- *Warren Buffet, Chairman, Berkshire Hathaway, Annual Letter, 02/27/21*

"The bottom line is this: given current conditions, should investors be at their usual risk position, more defensive or more aggressive? While risk-adjusted returns of most asset classes seem to be at rough equilibrium relative to each other, all absolute returns are ultra-low, commensurate with today's equally low interest rates. On balance, I think it's appropriate to be in one's normal stance, perhaps with a modest bias towards defense. Since the rewards for moving further out on the risk curve – such as yield spreads – aren't lavish, I have trouble seeing this is a time to aggressively chase high returns. Moreover, the surer one is that rates will soon rise meaningfully, the more cautious one should be today."

- *Howard Marks, Co-Chairman Oaktree Capital Management, Memo: 2020 In Review; 03/04/21*

"We don't know what the future holds, and it is possible that we will have a Goldilocks moment – fast and sustained growth, inflation that moves up gently (but not too much) and interest rates that rise (but not too much). A booming economy makes managing the U.S. Debt much easier and makes it much easier for the Fed to reverse QE and begin raising rates – because doing so may cause a little market turmoil, it will not stop a roaring economy."

- *Jamie Dimon, Chairman and CEO, JP Morgan, Annual Letter to Shareholders 04/07/21*

"Policymakers in major economies have pointed to 2023 as the date the stimulus payback may begin. The U.K. has proposed tax hikes in 2023, the Eurozone has suggested that suspended budget rules may be reimposed, and some members of the U.S. Federal Open Market Committee believe they will begin to raise interest rate in 2023. The economic headwind of rising interest rates may not slow growth until 2023."

- *Stimulus Payback: 2023, March 29, 2021, Jeff Kleintop, Chief Global Investment Strategist, Charles Schwab*

COMPANY UPDATES

On the heels of a challenging and unpredictable year, we were happy to welcome the first quarter of 2021 with positive news. While our team grew with the addition of Katie Riesberg as Associate Planner, the extended Radnor family also grew with the birth of Justin Spike's daughter, Zoe Mae. Further, we were pleased to achieve industry honors by being included in Barron's 2021 Top 1200 Financial Advisors List and the Forbes 2021 Annual Best-In-State Advisor Rankings. On the education front, we hosted a successful webinar on Cyber and Personal Security as part of our virtual Speaker Series. It was wonderful to have so many people participate, and we look forward to continued engagement at our upcoming quarterly events.

Please feel free to share our quarterly commentary with anyone that you feel may find it helpful. We would welcome the opportunity to share our expertise and unparalleled service with any of your family members, friends, or colleagues who may be seeking prudent, customized financial advice.

IMPORTANT DISCLOSURE INFORMATION