Chartwell Strategies Current Outlook and Investment Strategy

"Success is a lousy teacher. It seduces smart people into thinking that they can't lose."
-Bill Gates

Summary

- The U.S. economy weathered the COVID-19 induced recession and experienced a sharp rebound in the third and fourth calendar quarters. GDP growth is expected to be above long-term trends in the first half of 2021 as more industries return to normal operating levels.
- The impact of the virus is expected to wane as vaccines from Pfizer and Moderna are being distributed rapidly. Tentatively, the number of new virus cases and deaths peaked on January 8th and 12th, respectively.
- In the fourth quarter, our growth and balanced managed accounts performed in-line with mid-cap value indices, but underperformed small-cap value indices. On an annual basis, both the Chartwell Growth and Balanced Composites scored modest gains for the year. The long-term performance of our managed accounts remains above that of their reference indices.
- The powerful and broad rally, led by small-cap value stocks, that began in March is characteristic of a major bull market whose main adversary is non-productive government regulation and higher taxes.

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Background

The U.S. economy began 2020 from a position of strength, however, in successive periods, the U.S. economy shrank 5.0 percent in the first quarter of the year and 31.4 percent in the second quarter on an inflation adjusted basis. The recession was caused by a worldwide pandemic resulting in the temporary shutdown of many businesses as well as extended shutdowns in many travel and entertainment related businesses. Unfortunately, despite federal and state government assistance, many small businesses in the United States had no choice but to permanently close.

Once health authorities grasped the significance of the scourge, causing the federal government to order a two-week shutdown of non-essential services, the impact upon the U.S. financial markets was immediate and severe. After plummeting in the prior four weeks, on March 23rd, amidst a heightened panic level the major stock indices bottomed. However, with the uncertainties created by the pandemic, many investors remained wary and had taken to the sidelines. At the March bottom, the Dow Jones Industrial Average (DJIA), Standard & Poor's 500 (S&P 500) and NASDAQ had fallen 34.46 percent, 30.43 percent and 23.31 percent, respectively, from the beginning of the year. The Russell 2000 Value Index (RUJ), that had been underperforming for years, fell 44.33 percent. All performance figures in this letter are presented as total returns, which include dividends.

Although the cause of the recession was unrelated to a financial, or economic event, the market rally that ensued since March has been typical of those following past recessions. In this case, the spread of the coronavirus has been the impediment to economic growth as compared to inflation, high interest rates, or supply/demand imbalances in the economy. Consequently, those industries less affected by the virus have bounced back quickly, while other industries may not recover fully until the newly developed vaccines have been widely distributed. Nevertheless, the U.S. economy surged in the third quarter, with Gross Domestic Product rising 33.4 percent, and on a preliminary basis, recorded a 6.0 percent annualized rate of growth in the fourth quarter of 2020.

The ability of the Nation to function during this volatile period is testimony to the inherent strength and flexibility of the free enterprise system which has served us so well in the past. The private health care sector supported government efforts to mitigate the effects of the virus and has now developed effective vaccines in record time that promise to return our country to normal, once fully distributed. Current plans expect this to be accomplished well within this calendar year. At the time of this writing, January 30th, the domestic number of new cases and deaths reported daily, peaked on January 8th and 12th, respectively. While this is encouraging, health officials declare that it is too soon to declare victory over the virus.

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The stock market rally is predicting a broad and substantial increase in the economy's growth. For example, the RUJ and the NASDAQ represent very different parts of the economy, yet both indices have been leaders in the stock market's rebound. Typically, small-cap value stocks have performed their best a few months prior to the end of a recession and for a period-of-time thereafter. In the 2020 post-recession rally, the RUJ has mirrored this historical behavior; since March 23rd of last year, when the market bottomed, until January 29, 2021, the RUJ has rallied 97.78 percent. The NASDAQ, a proxy for the large high technology and social media stocks, had been leading the market higher during the past four years, and has risen 91.88 percent since the market bottom in March. Figures 1 and 2 illustrate the performance of the RUJ and NASDAQ during last year's decline and the subsequent rally through January 29th of this year. In addition to the performance of these two indices, the DJIA and the S&P 500 have rallied 64.14 percent and 68.44 percent, respectively, during the same time frame. Finally, disciples of the Dow Jones Theory should be comforted by the fact that the Dow Jones Transportation Average has been rising in tandem with the DJIA.

Performance of the Russell 2000 Value Over the Past 13 Months 12/31/2019 – 01/29/2021

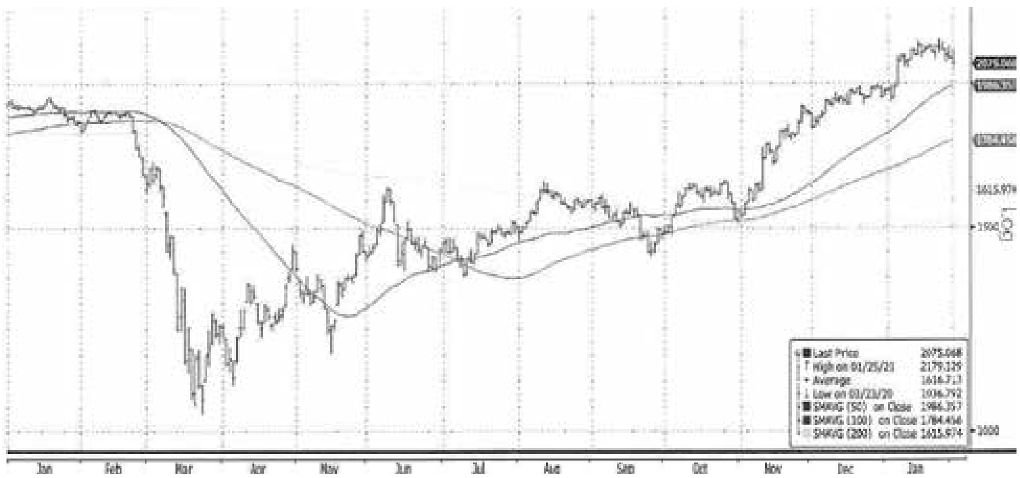

Figure 1. Small-cap Value Stocks were the Top Performing Sector Since the Market Bottom
Source: Bloomberg

Performance of NASDAQ Stocks Over the Past 13 Months 12/31/2019 – 01/29/2021

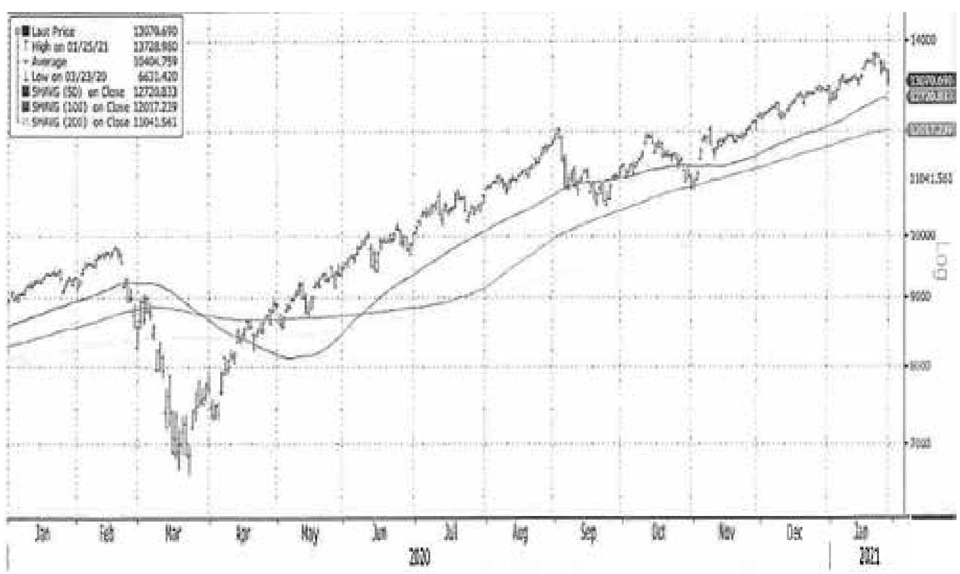

Figure 2. NASDAQ Continued to Perform Strongly in the Market Rally
Source: Bloomberg

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Logic suggests that the bull market, which began at the end of last March, will continue for the following reasons:

-as the COVID-19 vaccines take effect, industries throughout the country should return to "normal." Most notably, the airline, cruise line, entertainment, hotel and restaurant industries can be expected to recover from their currently depressed state and add to the economy's momentum.

- low interest rates should be a positive force to promote corporate investment and consumer borrowing for large purchases such as automobiles and housing.

- figure 3 illustrates the dramatic rise in consumer savings since the pandemic began. As shown in the chart, the personal savings rate had been vacillating between 6.4 percent and 9.1 percent of income for the past five years, prior to the pandemic. However, in April of last year, the savings rate soared to 33.7 percent and has remained well above the historical range since then. As the effects of the virus upon the economy are mitigated by the vaccines, we believe demand should accelerate GDP growth and the personal savings rate should decline to a normal level.

U.S. Personal Savings Rate Over Past 5 Years 01/01/2016-01/01/2021

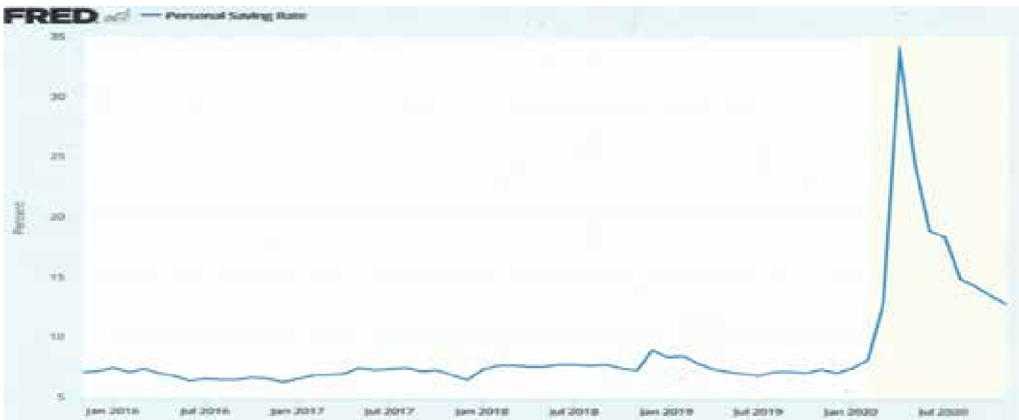

Figure 3. The Consumer Personal Savings Rate has soared since the pandemic began.
Source: U.S. Bureau of Economic Analysis

The three factors listed above are powerful forces that give us encouragement in the bull market's continuation. However, in our last letter, we specified that changes in tax law under a new Administration could present headwinds to the economy and consequently, the stock market. Additional federal regulations and executive orders, such as the cancelling of the Keystone Pipeline and restrictions to drilling for oil and gas on federal lands are also a negative to economic growth, in our opinion. So, as 2021 unfolds, investors need to be sensitive to government interference in the private sector that could hinder an economy that has the potential for above average growth.

Current Strategy

In the fourth quarter, our portfolios took advantage of the "rotation" into value stocks. The Chartwell Growth Composite gained 22.2 percent versus the Russell 2000 Value's (primary benchmark) 33.4 percent gain and the Russell Midcap Value Index (secondary benchmark), which rose 20.4 percent. In recent quarters, the market capitalization of our current portfolios has increased and is showing a closer correlation with the Midcap Index. The Chartwell Balanced Composite rose 15.4 percent as compared to 20.5 percent for its blended benchmark. Finally, our Dividend Equity accounts gained 14.6 percent as compared to the Russell 1000 Value which rose 16.3 percent in the three-month period.

The three best performing stocks in the Growth and Balanced Portfolios were: Lincoln National (LNC)(1.7%)*, up 62.38 percent; Micron Technology (MU)(2.7%), up 60.09 percent and Onto Innovation (ONTO)(1.5%), up 59.67 percent. LNC, a diversified financial services company (asset management, annuities, insurance), whose earnings are anticipated to benefit from an increase in long-term interest rates, has tripled from its March low, yet continued to offer a 3.3 percent dividend yield. MU, is a manufacturer of both dynamic and static random access memory chips, flash memory and other semiconductor components. Based in Boise, Idaho, MU has an enviable long-term record of growth and services in a wide variety of industries including auto, industrial, information systems and telecommunications. Revenue is expected to grow 11 percent in the next year. The third best performing stock was Onto Innovation (ONTO), a company involved in the development of process control solutions and inspection systems used in the fabrication of semiconductors.

*The numbers in parentheses following each company mentioned reflect the percentage of the portfolio's net assets comprised of such securities as of 12/31/2020. Holdings are subject to change. A full listing of portfolio holdings is available upon request.

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The three worst performers in the Growth and Balanced accounts were: PulteGroup (PHM)(2.7%), down 6.54 percent; Horizon Therapeutics (HZNP)(3.6%), down 5.83 percent and PPL Corporation (PPL)(2.3%) up 5.13 percent. PHM a builder of residential properties and communities, based in Atlanta, Georgia, has been a long-term winner, doubling in price since last March. Since the end of 2020, PHM has regained its momentum and is likely to remain in the portfolio at this time. HZNP is another good, long-term performer whose stock performance was negatively affected by a short-term supply disruption for its drug, Tepezza. The supply disruption is being caused by a vendor's inability to provide services to HZNP, due to government mandated priority associated with the COVID-19 Operation Warp Speed. Although PPL advanced for the quarter, it lagged the overall market due to a modestly disappointing third quarter earnings report. PPL, a well-managed electrical utility, offers a generous dividend yield of 5.9 percent.

Our Dividend Equity accounts are designed to provide long-term growth, while reducing the amount of volatility associated with an all-equity growth portfolio, but, having more risk than in our balanced accounts. In this period of low fixed income interest rates, the Dividend Equity strategy has proved to be a viable investment approach. The three best performing Dividend Equity stocks were: Lincoln National (LNC)(2.2%), up 62.38 percent; Assured Guaranty (AGO)(1.0%), up 47.53 percent and Ally Financial (ALLY)(2.8%), up 43.26 percent. It is no coincidence that each of these stocks is in the financial sector, which rallied sharply in the fourth quarter when long-term interest rates, as measured by the 10-year Treasury bond, rose 23 basis points. LNC was profiled above. AGO is the dominant company engaged in providing insurance to bondholders, guaranteeing a stable flow of interest payments. ALLY is a full-service on-line bank that specializes in automobile financing and secondarily, home mortgages. ALLY has been a best performer for two consecutive quarters.

PHM (2.7%), discussed above, was the worst fourth quarter performer in the Dividend Equity accounts. General Mills (GIS) (2.5%), down 3.88 percent and Intel (INTC)(3.6%), down 3.09 percent were the second and third worst performers. GIS, a defensive holding in the consumer staples sector, was relatively stable during the height of the panic and therefore, did not rally as much during the recovery. Like PHM, GIS is off to a strong start in the new year. Unfortunately, INTC has continued to lag the market due to operational problems related to new semiconductor designs and a very competitive environment. However, we have been reluctant to sell this stock due to the company's strong balance sheet, reliable dividend and confidence that a new CEO will be successful.

In the first month of the New Year, the market has been exceptionally volatile, but on balance, positive for our managed accounts. The initiatives announced by the Biden administration regarding climate change are negative for industries related to fossil fuels and consequently, we are not adding to any positions in that sector. However, in the fourth quarter we purchased Brunswick Corporation (BC) in the Chartwell Growth accounts. BC manufactures products for both the outdoor and indoor recreational activities, that include fishing, boating, fitness, bowling and billiards. We also added to our position in PHM during the quarter. Despite the pandemic, PHM's earnings have surged in 2020, yet the stock sells at a single digit earnings valuation. Two stocks were sold in the fourth quarter: Knoll (KNL) and Lions Gate Entertainment (LGF). KNL, a manufacturer of office furniture, has experienced declining sales as a result of the pandemic and its growth prospects appear limited. Similarly, LGF, a producer and distributor of motion picture films and television programming has experienced declining revenues and a near-term turnaround, in our view, seems unlikely. Finally, we reduced our exposure to Arthur J. Gallagher (AJG) a nationwide insurance brokerage firm. AJG has been a solid performer, but, had become overweighted in the portfolios.

In the Dividend Equity composite, six stocks were purchased during the quarter: Broadcom (AVGO), a developer of analog and digital semiconductors; Hasbro (HAS) a manufacturer and marketer of toys, games and interactive software; Seagate Technology (STX), a manufacturer of high capacity disc drives; Chubb (CB), a property and casualty insurance company; Abbvie (ABBV), a researcher and developer of specialty therapeutic pharmaceuticals and Huntington Bancshares (HBAN), a multi-state bank holding company. In our opinion, each of these holdings offers long-term growth prospects at an attractive valuation. Four sales were made in the fourth quarter: Corning Inc. (GLW), a manufacturer of optical fiber for the telecommunications industry, as well as glass products for applications in the home entertainment, mobile phone and automotive industries; Western Digital (WDC), a manufacturer of solid state and disc drive storage products for the computer industry; GlaxoSmithKline (GSK) a multi-national pharmaceutical manufacturer, and KNL, described above.

Long-term Performance

Figure 4 on the next page is a long-term chart that compares the performance of our managed accounts with their reference indices since the year 2000. At the end of 2020, $10,000 invested in the Chartwell Growth and Balanced Composites had grown to $55,573 and $51,317, respectively. This compares with values of $48,745 and $44,906 for their reference indices, the Russell 2000 Index and Balanced Composite Index, respectively. Over the twenty-year history, the S&P 500 has lagged the performance of our Composites, but has outperformed them over the past four years. A change favoring our value-oriented approach may be occurring. The S&P 500 underperformed our Composites since the bull market began, last March and declined in the first month of 2021. We will be working extra hard this year to maintain our relative momentum.

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Comparison of the Change in Value of $10,000 Invested in Chartwell Growth and Balanced Strategy Account Composites 12/31/99-12/31/20

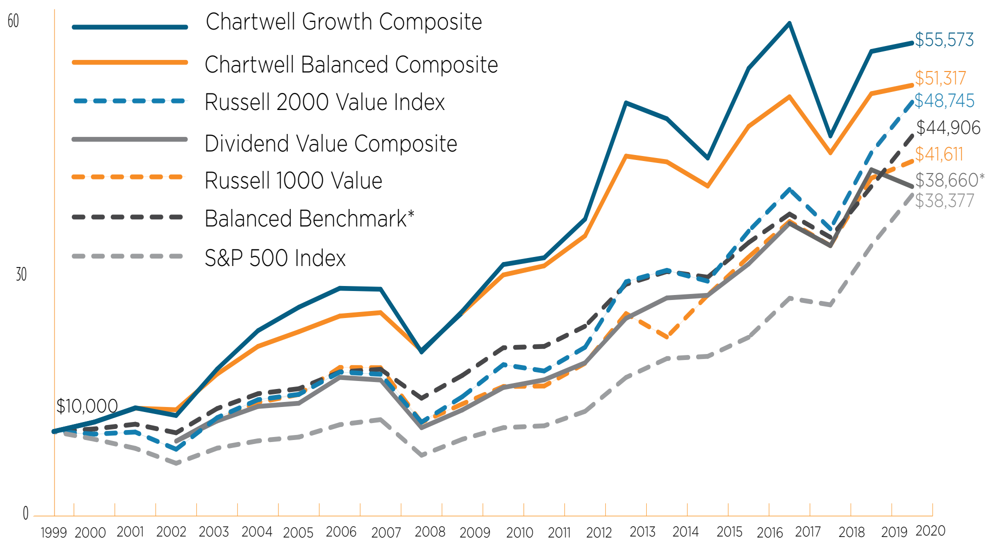

Figure 4. *Source: Chartwell Investment Partners*

All data is as of 12/31/2020.
*The Dividend Value composite incepted on 07/01/2002.
**Effective 03/31/2020, the Russell 2000 Index (Growth Benchmark) changed to the Russell 2000 Value Index, which more closely aligns with the strategy's investments.
Performance results for the Chartwell Growth and Chartwell Balanced strategies include performance results obtained by TKG prior to being acquired by Chartwell in April 2016.
***Growth Benchmark is Russell 2000 Value Index. Balanced Benchmark is 62.5% Russell 2000 Value, 37.5% Citigroup Broad Investment Grade Index. Prior to 4/1/20,the equity index was Russell 2000. The Russell 2000 Value Index refers to a composite of small cap companies located in the United States that also exhibit a value probability. The Russell 2000 Value Index is a subset of the securities found in the Russell 2000 Index.
The S&P 500 measures the performance of market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ.
The Russell 1000 Value Index represents approximately 1,000 of the largest companies in the U.S. equity market.

Chartwell News

As we start a new calendar year, we would like to remind those IRA holders over age 70.5, that while your Required Minimum Distribution ("RMD") was suspended via The Cares Act in 2020, it has been reinstated for 2021. In 2021, the RMD amount(s) need to be taken from your IRA account(s) by December 31st to fully satisfy your RMD. If you have any questions regarding your RMD or account performance, or want to discuss changes in your investment objective, please do not hesitate to call Mike Magee (610.407.4867), Bob Killen (610.420.8650), or Pete Schofield (610.407.4858).

We welcome the opportunity to have a portfolio review with you, as we begin the new year. If interested, please contact us to set up a call.

Past performance is no guarantee of future performance. Investment involves a risk of loss.

This commentary is for informational purposes only. It is not an offer to buy or sell any security and should not be construed as investment advice. The views in this report were those of the Adviser at the time of writing this report and may not reflect our views on the date this report is first published or anytime thereafter.

*The Chartwell Growth Strategy Composite includes all fully discretionary, fee-paying equity accounts with a growth objective whose asset size is $300,000 or greater at the beginning of the measurement period. For individual bond holdings the fee is 5/8 of 1% and for bond mutual funds, including exchange traded funds, the fee is 3/8 of 1%. The fee for these accounts is negotiable.

*The Chartwell Balanced Strategy Composite includes all fully discretionary, fee-paying accounts with a balance between growth and income as a principal objective whose asset size is $300,000 or greater at the beginning of the measurement period. The fee for certain retail and high net worth clients with individually managed accounts is generally 1% of the value of the assets under management. For individual bond holdings the fee is 5/8 of 1% and for bond mutual funds, including exchange traded funds, the fee is 3/8 of 1%. The fee for these accounts is negotiable.

The composites do not include accounts where total cash flows exceed 10% of the account's value during any quarterly period or accounts holding securities purchased by anyone other than the Advisor. No accounts using leverage or short positions are included in the composites. An individual client's account may have performed better or worse than the composites' returns presented above. The composites contain taxable and non-taxable accounts. The returns are before taxes and net of all advisory fees and commission charges. The net performance results for each composite are presented after deducting the actual fee charged to each account in the composite based on the management fee schedule in the Firm's Brochure or the fee negotiated between the account holder and Chartwell. Returns include the reinvestment of dividends and interest (total return). Returns for other Chartwell composites are available upon request.

As of 12/31/2020 Chartwell managed $10.3 billion in assets, $9.2 billion as advisor and $1.1 billion as sub-advisor. During the most recent quarter, the Chartwell Growth Strategy Composite consisted of 5 accounts which represented 7.9% of total Chartwell Strategy Individually Managed Accounts and 0.1% of total Chartwell assets. During the most recent quarter, the Chartwell Balanced Strategy Composite consisted of 23 accounts which represented 43.3% of total Chartwell Strategy Individually Managed Accounts and 0.5% of total Chartwell assets. The Chartwell Growth Dividend Strategy Composite consisted of 3 accounts which represent 1.8% of total Chartwell Strategy Individually Managed Accounts and less than 0.1% of total Chartwell assets.

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