corospondent

The Personal Investments Quarterly

The great endeavour

OCTOBER 2020 SPRING EDITION

CORONATION

TRUST IS EARNED™

IN THIS ISSUE

CORONATION FUND UPDATES AND PERFORMANCE

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On the cover: "Throughout human history, in any great endeavour requiring the common effort of many nations and men and women everywhere, we have learned – it is only through seriousness of purpose and persistence that we ultimately carry the day. We might liken it to riding a bicycle. You stay upright and move forward so long as you keep up the momentum." – Ban Ki-moon

Notes from my inbox

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By **PIETER KOEKEMOER**

Pieter is Head of Personal Investments

THE FIRST TWO quarters of 2020 were so eventful that they necessitated an all-consuming focus on the events of the moment. Thankfully, the past quarter was, at least from an investment perspective, less action-packed. Financial markets mostly continued recovering (albeit at a more muted pace) and the global economy started a fragile recuperation after the sudden stop experienced during the hard lockdowns.

This provides us with the opportunity to focus this edition on what we believe to be the most important wealth creation rule we know: *Invest money in the market as quickly as possible and then wait patiently for compound growth to work its magic, while deploying a disciplined and consistent investment strategy*. This is easier said than done. Endurance athletes will know that it can be very hard to keep going when you hit the proverbial wall. But having the insight and fortitude to know that hydrating, drinking *Steri Stumpies*, the setting of mini-goals and, above all, continuing to move forward – even if it's at a crawl – will eventually get you across the finish line. Investing is no different. The last 20 years provided many challenging moments when you might have been seriously tempted to divest. If you do stay the course, though, the rewards can be significant.

IN THIS EDITION

In our lead story on page 5, we highlight the track records of two Coronation funds that have been in existence for more than two decades. Over time, the Top 20 and Optimum Growth funds have >

out-performed their benchmarks by 3.6% p.a. and 3.3% p.a., respectively. This may not sound like much, but in both cases it more than doubled the value of an investment in the index over the same period. In the case of Top 20, it turned the local equity market's not unimpressive 10-bagger over the last 20 years into a 20-bagger. We also include the second instalment of our Personal Investment team's top wealth-creation tips, which mostly make the point that how you behave is more important than what you know.

Marie Antelme reviews the stark local economic outlook in the context of South Africa's emerging market peers on page 13. While there is no shortage of official economic revival plans, global financial market participants remain sceptical on government's willingness and ability to implement investment-friendly economic policy and to effect the expenditure cuts required to achieve debt stabilisation. These low expectations are baked into the highest real long-bond yields across the world's investable government debt markets, as explained in more detail by Nishan Maharaj in his bond outlook on page 18.

Low expectations often create the conditions for upside surprises. This is part of what drove exceptional recent returns from the locally listed miners. Good outcomes are often counterintuitive. Few casual observers would associate mining activity with green credentials, but as Nicholas Stein and Nicholas Hops argue on page 22, the world will need a lot of metal to achieve the decarbonisation of the economy. Heading back to global emerging markets, on page 27, Lisa Haakman takes a look at the Brazilian e-commerce sector and the fall of a Brazilian duopoly that saw attractive investment opportunities emerge.

HOW MUCH DOES THE US ELECTION MATTER?

We are often asked at times of imminent political change what our view on the outcome will be. Many investors are interested in how portfolios are positioned to benefit from the most likely result. This topic is obviously more relevant in the final weeks before the US presidential election. There are, however, two problems with using this approach in setting investment strategy. First, you need to call the outcome correctly. Secondly, you have to accurately predict the market's response to the outcome. Virtually no-one gave Trump a chance in 2016 and most of the speculation at the time was that if he were to be elected, it would be bad for markets given his maverick approach to policy. It was therefore unsurprising that the US equity market declined as the news of his election broke. Subsequently, however, the market performed strongly, fuelled by Trump's classic Republican business-friendly policies of tax cuts and deregulation.

As it became clear earlier this year that Biden has a strong lead in the polls (now revised to try and correct the forecasting errors made in the last election), the pundits initially focused on how a Democratic blue wave (winning both the Presidency and the Senate) will be bad for markets because of tax hikes and re-regulation. As the election draws closer, the narrative is shifting to the positive implications of a more normal US Presidency for global stability as well as the potential positive effects of his $2 trillion climate plan. The point? The short-term impact of political outcomes is much less important than the long-term business fundamentals when making investment decisions.

I again thank you for the continued trust that you place in us. You have our commitment to focus unceasingly on looking after your hard-earned capital to the best of our abilities.

As always, I invite you to contact us via **clientservice@coronation.com** if any aspect of our service to you is unsatisfactory.

Take care out there.

Pieter

LONG-TERM TRACK RECORD

Two funds, two decades, double the index

A history of consistent alpha generation in local and global markets

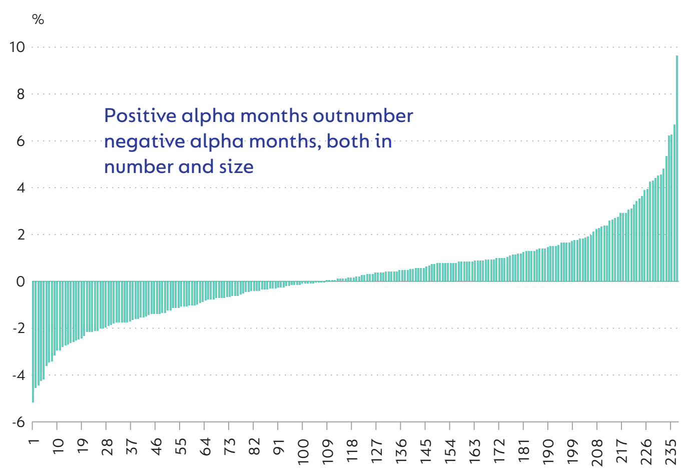
THE QUICK TAKE

- Sterling track records of disciplined long-term investing
- Annualised alpha of >3% over two decades after all fees
- Meaningful long-term wealth creation for investors
- Supported by in-depth research across local and global asset classes

2020 marks a milestone anniversary for both the Coronation Top 20 and Coronation Optimum Growth funds. While the two funds are managed to meet very different investor needs – one to maximise returns within the borders of South Africa and the other by investing across the expanse of the globe – both have outperformed their benchmarks since their launch dates in 2000 and 1999, by 3.6% p.a. and 3.3% p.a., respectively. Over time, this alpha adds up, resulting in meaningful wealth creation for investors.

Figure 1

DISTRIBUTION OF ALPHA (MONTHLY)



Source: IRESS

CORONATION TOP 20: 20 OF OUR BEST IDEAS ON THE JSE

Since its inception in 2000, Top 20 has offered its investors an actively managed and concentrated portfolio of what we believe to be the best opportunities on the JSE. The focused nature of this Fund has called for great discipline from its managers and, at times, true grit from its investors. Because we limit ourselves to no more than 20 investment ideas within the Fund, the potential to outperform the index through disciplined stock selection is greater, but with that comes lumpy returns over the shorter term.

Investing is a long game

The investor's reward for enduring many periods of short-term underperformance (as is clear from the distribution of negative and positive monthly alpha in Figure 1) is exceptional wealth creation in the long run.

>

OUR CLIENTS' SUPPORT HAS BEEN A KEY FACTOR IN TOP 20'S SUCCESS

In rands and cents terms, the Fund's annualised alpha of 3.6% means that R100 000 invested at launch 20 years ago would have grown to more than R2 million as at the end of September 2020 – after all fees. This is double the return of a similar investment in the benchmark index (as illustrated in Figure 2).

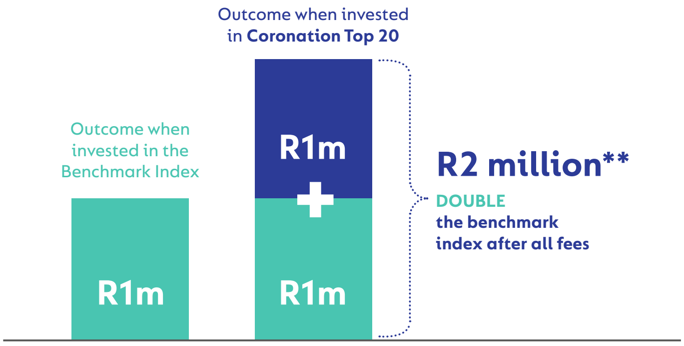
A long-term track record enabled by an incredible research effort, investment philosophy and support from our clients

According to Neville Chester, a manager of Top 20 since 2007, the success of the Fund is a direct result of leveraging the in-depth, proprietary research of Coronation's investment team. "It's their application of our intensive, long-term focused approach that has been crucial in consistently identifying undervalued ideas for the Fund over the past 20 years."

Figure 2

THE POWER OF ALPHA IN AN EQUITY MANDATE

Growth of R100 000 invested in Coronation Top 20 vs Benchmark Index*



Performed quoted net of fees from Morningstar as at 30 September 2020 for a lump sum investment with income distributions reinvested

* Splice of current and historic benchmark indices (The FTSE/JSE Capped All Share Index replaced the FTSE/JSE Top 40 Index from 1 October 2016)

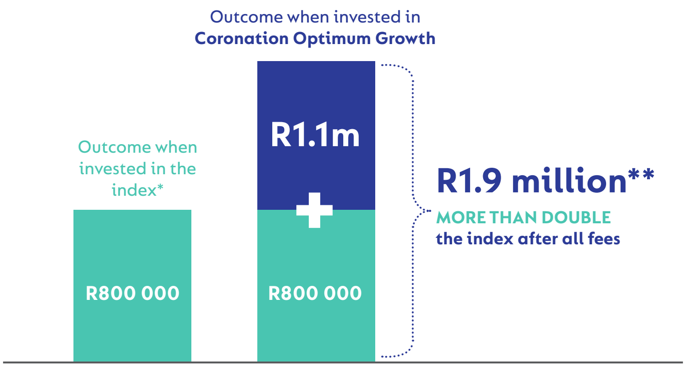
** Since inception of the A-class in October 2000

Source: Coronation

Figure 3

THE POWER OF ALPHA IN A FLEXIBLE MANDATE

Growth of R100 000 invested on 15 March 1999 (Coronation Optimum Growth vs the MSCI World Index)



Performed fees quoted net of fees from Morningstar as at 30 September 2020 for a lump sum investment with income distributions reinvested

* MSCI World Index

** Since inception of the A-class in March 1999

Source: Coronation

However, staying the course in a fund such as Top 20 requires clients to embrace our investment approach and be willing to back the Fund through periods of short-term volatility and underperformance. "This support has been a key factor in making the Fund the success that it is today."

CORONATION OPTIMUM GROWTH: A BLEND OF OUR BEST IDEAS FROM ACROSS THE GLOBE

In 1999, we pioneered the uniquely flexible worldwide multi-asset mandate by launching Optimum Growth. Its founding purpose, and still its driving force today, is to provide investors with a long-term portfolio of the best investment ideas we can find around the world, while aiming to deliver healthy long-term real returns.

The Fund is unconstrained, so it can invest anywhere in the world and across all available listed asset classes. Its fund managers decide on the optimal allocation between both growth and income as well as domestic and foreign assets. Optimum Growth's investors therefore benefit from our full global research effort, comprising 70 investment professionals, across all the investable asset classes.

As with Top 20, the long-term reward for staying invested in the Fund has been exceptional. It has outperformed global equities (as measured by the MSCI World Index) by 4.6% p.a. since inception, resulting in a current investment value more than double that of an investment in the index (as illustrated in Figure 3). And given the benefit of wider diversification in a fund such as Optimum Growth, we delivered this performance with significantly less volatility than that of the index.

Can we repeat these outcomes for investors over the next two decades?

According to Gavin Joubert, a manager of Optimum Growth since 2005, the Fund benefits from ideas being generated by a team of 18 investment professionals who provide detailed coverage of global developed and global emerging market stocks. "Besides being a well-resourced and experienced team by global standards, our knowledge of global stocks has continued to increase year after year, which places Optimum Growth in a strong position to continue to deliver attractive risk-adjusted returns for its investors."

Regarding Coronation Top 20, Chester adds that the same factors that have driven the remarkable performance of the Fund remain in place at Coronation. "Today, we are as excited as we have ever been about the opportunities that are available in the market and that we are currently taking advantage of in the [Top 20] Fund."

ARE THESE FUNDS FOR YOU?

Regardless of the Coronation fund you choose, all benefit from our in-depth research, rigorous analysis and commitment to a philosophy of investing with a long time horizon. This enables us to look through the noise and identify the very best investment ideas for our investors.

	TOP 20	OPTIMUM GROWTH
Fund description	An aggressive long-term portfolio that invests in 20 of our top stock picks on the JSE. *Ideally you should blend this Fund with other equity funds. If you prefer to own just one equity fund, you can consider the more broadly diversified Coronation Equity Fund.*	An aggressive long-term portfolio that invests in the best opportunities in both local and international markets.
Recommended investment period	10 years +	10 years +
Suitable for investors who	• are looking to maximise long-term returns and able to withstand short-term market turbulence; • are in their wealth build-up phase and require little income in the short-term; • are looking for an alternative to a stockbroker-managed direct share portfolio. *The Fund is not appropriate for investors who are concerned about short-term capital losses or who want to generate consistent income, nor is it suitable for those who seek an equity investment that tracks the returns of the market.*	• are looking for balanced exposure to both domestic and international assets; • are comfortable to grant Coronation a wide degree of discretion; • are in their wealth build-up phase and require little income yield in the short term; • are able to withstand short-term market and currency fluctuations in pursuit of maximum total returns over the long term; • intend following a core/satellite approach, using this Fund as a core fund.

For more information, see the detailed fund commentaries on pages 36 and 44.

20 tips for the 2020s

PART 2

"Financial success is a soft skill. How you behave is more important than what you know." – Morgan Housel, author of *The Psychology of Money*

To set the tone for the start of the new decade, we asked our Personal Investments team to share their top investment insights. Herewith the second instalment, to complement the first 10 tips shared in the January edition of *Corospondent*.

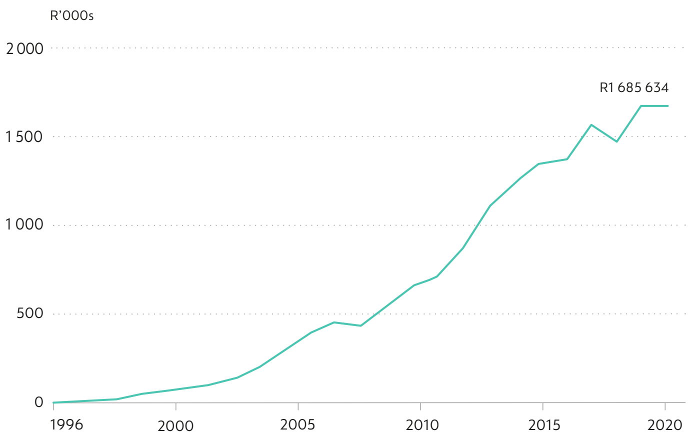
Live below your means – *Petronella Nkobe*

Don't spend more than you earn. As simple as it sounds, it's easy to fall into the trap of relying on your credit cards to acquire the 'finer things' in life, maintain a desired lifestyle or to keep up appearances. Spending less doesn't mean you can't enjoy life, and trading immediate pleasures for the sake of long-term gains brings its own rewards. The rule of thumb is to save at least 10% of your income – if your monthly income is R10 000, your monthly savings should be at least R1 000.

If you had invested R1 000 per month into the Coronation Balanced Plus Fund since its launch in April 1996, your investment would now be worth nearly R1.7 million, as shown in Figure 1. This is the outcome of an annualised return of 12.4% earned for 24.5 years. The earlier you start, the better, as the compounded growth over time is what makes living below your means so worthwhile. Give it a try; you will be surprised how hard your money and investments can work for you.

Figure 1

COMPOUNDING IN THE CORONATION BALANCED FUND R1 000 MONTHLY DEBIT ORDER INVESTED SINCE INCEPTION



Source: Coronation

Set aside an emergency fund and keep separate investment accounts for different goals – *Ndapwa Kwedhi*

How resilient is your current investment plan to financial emergencies? Many investors struggle to realise their goals when they are derailed by unforeseen expenses. You can prepare for contingencies by maintaining an emergency fund and preserving your safety net savings in a conservative investment vehicle. The Coronation Strategic Income Fund is liquid and easily accessible on 'rainy days'. How much to keep in your emergency fund will depend on your lifestyle and circumstances, but three to six months of your regular expense budget is a good starting point.

You can further enhance your investment outcomes by keeping separate accounts for your different financial goals. This creates a clearer sense of direction, as it enables you to track progress for each goal and makes it a little harder to access money earmarked for a specific purpose.

Although the ultimate objective of investing remains to maximise returns within your unique set of constraints, maintaining separate goal-based investment accounts ensures that the respective portfolios are invested optimally – each driven by a distinct set of objectives that are bound by their respective time horizons, making it easier to optimise risk and return levels.

Build your balance sheet: invest automatically and regularly – *Liezel Greeff*

"Little by little, a little becomes a lot" – Tanzanian proverb

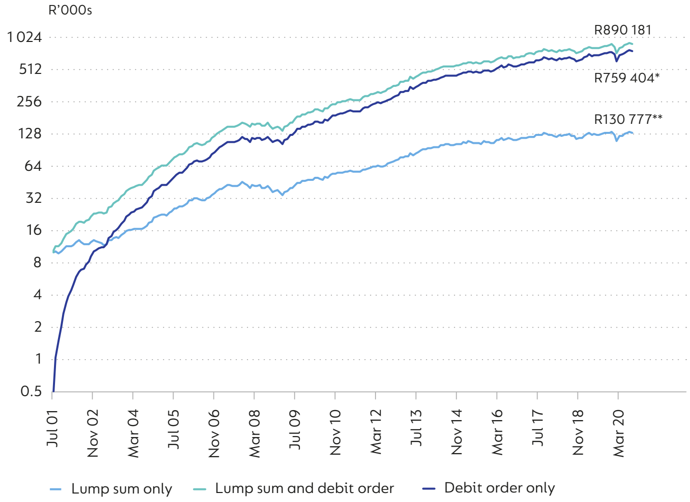
It's so much easier to stay disciplined with saving when it happens automatically. Investing R500 per month might require some tweaks to your budget initially, but once you get it going you will soon forget all about it, as it leaves your bank account before you get the chance to spend it on something you might not need.

By investing a smaller monthly amount more regularly, you are investing when the market goes up as well as when the market goes down, thereby averaging out the price of each unit, something we call rand cost averaging.

Monthly investments really start to make sense when you earn a return on your return made by the previous return – you get the point. Put in a fancier jacket, it's called compound growth. It starts small and slowly, but once it picks up momentum, it's quite a force. As Figure 2 shows, a picture is worth a thousand words. The moral of the story, you ask? What are you still waiting for?

Figure 2

LUMP SUMS, DEBIT ORDERS AND COMPOUNDING CORONATION MARKET PLUS FUND



* R500 initial debit order escalating at 10% p.a.
** R10 000 initial lump sum

Source: Coronation

Those annual tax-free contributions add up – *Jasantha Mari*

We all pay tax on our hard-earned money, and if we manage to save some of it, we again pay tax on the returns our savings produce. The only exceptions are retirement savings through, for example, retirement annuities (RAs) or tax-free investment accounts (TFIs). While RAs have attractive tax benefits, they come with limitations to how you can structure your investment portfolio.

TFIs have become increasingly popular since the government introduced them five years ago to encourage saving without paying tax on income earned or on capital gains. Individuals can contribute up to R36 000 within a tax year without being penalised. Your lifetime contributions may not exceed R500 000, and that can be achieved in under 14 years. The added benefit of a TFI is that there are no investment restrictions as in the case of RAs.

In a recent study, using the actual returns produced by the Coronation Market Plus Fund since launch in 2001 and hypothetical tax-free contributions to get to the maximum R500 000 contribution as quickly as possible, we found that the TFI tax benefits increased the investment programme's terminal value by 29% (from R2.1 million to R2.7 million).

So, why not start today by taking advantage of this opportunity? Find the right fund for you, start contributing and the benefits will continue to add up. >

How much should I invest offshore? – *Lerato Ried*

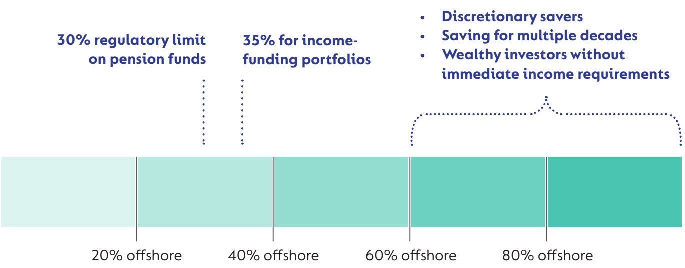
The short and maybe frustrating answer is that it depends. The appropriate allocation will differ for every person, because we all have different return expectations, risk parameters, spending profiles and time horizons. Although research has shown that all investors should aim to have a minimum of 25% of their investment portfolio offshore, your answer may be very different. The best way to optimise exposure is to consult with a credible financial adviser who will be able to do a comprehensive assessment.

However, there are general guidelines that you can follow:

1. If the purpose of your investment portfolio is to draw an income from it, especially if the income rate is more than 5%, you should generally aim to have no more than 35% direct offshore exposure in your portfolio.
2. Long-term investors who will not be using their investment to supplement their immediate income can invest up to 100% of their portfolio offshore, depending on their risk appetite and financial goals.

Figure 3

HOW MUCH SHOULD I INVEST OFFSHORE?



Source: Coronation

Do not move the goalposts too often – *Frederick Greeff*

Clear goal setting (your personal investment goalposts) is the first and arguably most important step in the investment planning process. If you do not know what you want to achieve with your hard-earned money, you won't be able to choose the right investment strategy.

To use a simple analogy: if you plan to explore our beautiful continent on a 4x4 trip to Botswana, you need to match the 'vehicle' to the goal – a Toyota Corolla simply won't do the job given the need. You'll need a Fortuner with 4x4 capabilities, or better yet, a rugged Land Cruiser, otherwise you'll just get stuck in the sand. The same is true for reaching your investment destination. The bottom line – choosing the right investment strategy upfront is key, and then sticking to it is just as critical, even when markets take a turn for the worse. If you move the goalposts halfway through the journey and change your investment strategy, you risk interrupting the powerful effect of compounding that is firmly embedded within your investment portfolio.

Think carefully about your personal circumstances and preferences when setting your goals. Commit to targeting that investment goal and then stick to the investment strategy that is tailored to help you reach it. Simple, but not easy. This will largely determine your investment outcome.

Coronation has a range of flagship funds that is designed to reach most investor targets. To assist you in making the right investment choice, visit our fund centre on www.coronation.com and *select the need* that best suits your current circumstances.

Your retirement crib sheet – *Christo Lineveldt*

No function can fully solve the complex equation of retirement, but there are three key numbers to keep in mind when considering your retirement plan: 75, 5 and 15.

75%	How much of your final annual salary you will likely need to replace at retirement to maintain your lifestyle.
5%	The generally accepted maximum annual initial drawdown rate that a well-constructed retirement portfolio can sustainably accommodate over two or more decades.
15x	The multiple of your final annual salary required at retirement given the 75% replacement ratio and 5% maximum annual drawdown.
15%	The recommended minimum portion of your pre-tax income that should be set aside for retirement throughout your working life to make the above numbers achievable.

It goes without saying that the above is a simple guideline and that we recommend consulting a qualified financial adviser for a tailored retirement plan.

Successful investors make many mistakes along the way – *Jared Williams*

Not all heroes wear capes. Mine is a fiery Scot with a penchant for black zip-up cardigans, chewing gum and 'the hairdryer treatment'. A serial winner who is widely regarded as the most successful football manager ever – Sir Alex Ferguson. Is it surprising, then, that Fergie only won just under 60% of his 1 500 games during an illustrious 27-year spell managing Manchester United? For every three matches where he got his tactics right, there were two games where one of the greatest managers of sporting talent did not succeed.

"Losing is a powerful management tool so long as it does not become a habit." – Alex Ferguson

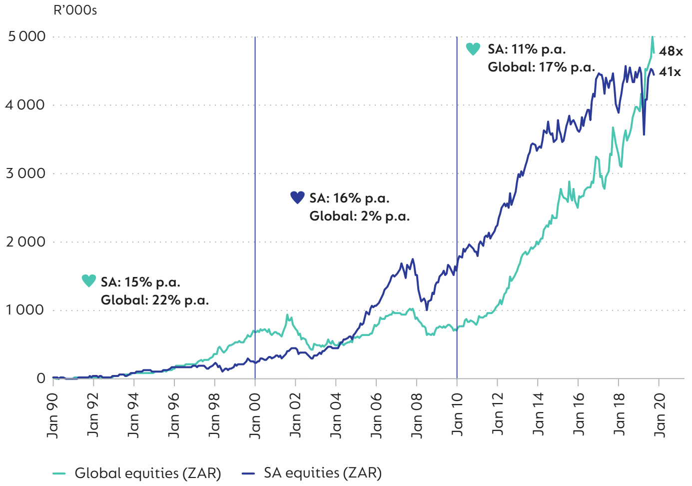
Like a football manager erring when selecting the 11 players to start a match, investors will inevitably make mistakes in their investment decisions. Perhaps you picked the wrong manager or, borrowing a football term, scored an own goal by attempting to time the market and it moved against you. A disciplined investor endeavours not to repeat their mistakes, but also knows they are unavoidable.

Ferguson averaged just one *Manager of the Month* award per season. Over short periods, his teams were not always the best, but over the course of the season they almost inevitably won the title. The key to his team's success is accredited, in his words, to the "consistent application of discipline".

Successful investors make mistakes often but with a disciplined approach to investing they learn and correct. Making just slightly more good decisions than bad ones compounds over time and can produce meaningful long-term outperformance.

Figure 4

DOMESTIC VERSUS OFFSHORE INVESTING SHOULDN'T BE BINARY



Source: Coronation

Don't chase the trend – *Suzanne de Wet*

At our core, humans are social beings. In times of stress and uncertainty (much like what we face today) people are afraid and it is human instinct to rely on our group to help us when we're afraid. We make decisions that most of our friends, colleagues or family make because we feel safer together. This is known as 'herd behaviour' and can be defined as doing what others do, instead of using your own information to make decisions. In most aspects of life this is a useful strategy and has helped humans survive many ordeals. Unfortunately, this does not hold true for all aspects of life – especially not for your finances or investments.

There are at least two reasons why this behaviour is not recommended for decision making when investing. First, we all have different circumstances. To make a thought-through financial decision, you must consider your own personal needs and not that of the herd. What are *your* current assets and liabilities? What is *your* risk profile? What is the goal of *your* investment? These are the questions you should build your strategy around.

Secondly, following the herd means you are likely to invest where the money already is, rather than where the best opportunities are. Investors often use past performance as their frame of reference (or, put differently, 'what works right now'). This is how asset bubbles are created and only investing in what is already popular creates a high probability of capital loss.

An example of herd behaviour is the desire of many local investors to move all their money offshore after the rand has depreciated in value. In 2001, after the rand depreciated by more than 60% in six months, South African investors flocked to offshore investments only to receive close to 0% return for the following 10 years. Over the same period, local equities had one of the best 10-year periods in history.

You don't have to ignore all information out there, but try to develop an awareness of the factors you use when making your investment decisions. Avoid blindly following a trend 'just because everyone else is doing it'. Try and frame your decisions correctly and don't get carried away with good (or bad) past results; it's only the future events that will count.

The key to successful investing can be summed up in just two words – asset allocation – *Fred Grunewald*

If there's one thing that history teaches us, it's that no one knows what the future may bring. The idea of 'not putting all of your eggs in one basket' is the essence of asset allocation, which involves identifying how your investment portfolio should be distributed between the various asset classes such as equities, bonds, commodities and cash. The objective of asset allocation is to optimise the mix of your investments into different asset classes to *maximise* the return of the investment portfolio while *minimising* the potential risk, based on your time horizon, risk tolerance and long-term investment goals.

History suggests that different asset classes perform better or worse depending on economic conditions, market forces, technogical change and political developments. The goal of an asset allocation strategy is to ensure that you own a robust portfolio that can withstand many different outcomes. It makes sense for many investors to outsource these decisions by investing in an appropriately mandated multi-asset fund with the ability to hold a wide variety of assets. The long track record of the Coronation Optimum Growth Fund (see page 44) is testament to the success of this approach. ✚

ECONOMIC COMMENT

Emerging markets face a fiscal endgame

Vulnerabilities increase the risk of longer-term damage

By **MARIE ANTELME**

THE QUICK TAKE

- Covid-19 was an amplifier of existing systemic risks in emerging markets
- Recovery certainty around the world is waning as second-wave infections threaten
- Emerging markets will suffer painful growth shocks, but governments' fiscal positions will be defining
- SA's economic and fiscal dynamics compare poorly, highlighting the urgency of credible strategies

Marie is an economist with 20 years' experience in financial markets.

IT'S NINE MONTHS since China imposed a national hard lockdown on its economy. Starting in Wuhan in January, and spreading outwards, by the end of March the borders were closed, streets were empty and factories quiet. Most households could have only one person leave, once a day. The skies were empty. Only China was this strict. While containment was not as harsh elsewhere, there has been some form of closure in most countries as the pandemic spread through Asia, into Europe and the US, and then into antipodean emerging markets.

China's economic growth bottomed in the first quarter of 2020 (Q1-20), with GDP growth falling by an unprecedented 6.8% year on year (y/y). Since then, Covid-19 infection data officially show that infections have collapsed (12 new daily infections at the time of writing), which means that China has effectively contained the pandemic for now. Mobility data show that China is broadly back to normal – retail, vehicle and property sales, as well as fixed asset investment, are all recovering. Outside of cross-border travel (but including internal travel), China is returning to pre-Covid levels. China is also benefiting from the re-awakening of demand elsewhere, with export growth supported by demand for personal protective equipment and high-end electronics. Official estimates show GDP accelerated to 3.2% y/y in Q2-20, and available activity data suggest decent momentum has built in Q3-20. This should see China's GDP return to pre-Covid levels by next year, if sustained.

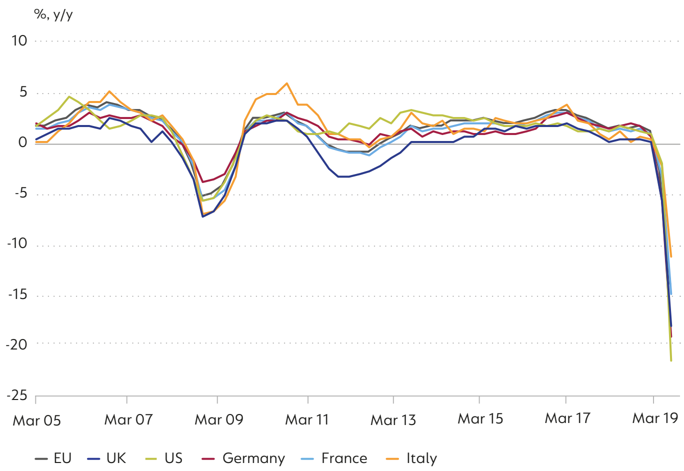
This is not what we see elsewhere. Most advanced economies initially implemented some form of lockdown, and aggressively increased fiscal and monetary support for healthcare systems, households and corporates. Despite this, the severity of lockdown and the associated collapse in activity have resulted in GDP growth contracting 21.5% y/y in the US in Q2-20, 13.9% y/y in Europe and 18% in the UK (Figure 1 overleaf).

While Q2-20 was undoubtedly the nadir of economic activity for most countries outside of China, >

'second waves' of infection in a number of countries have prevented a return to more normal mobility, and economic activity is slowing again. Both the economic damage and fiscal cost of 'wave one' are still unknown as the next wave approaches. Early signs of an economic rebound in the second half of 2020 were relatively good, but momentum has started fading, raising the risk of a Q4-20 'double whammy' as growth falters as containment strategies intensify.

Figure 1

GDP CONTRACTION IN DEVELOPED MARKETS



Source: Haver

EMERGING MARKET VULNERABILITIES INTENSIFIED BY COVID-19

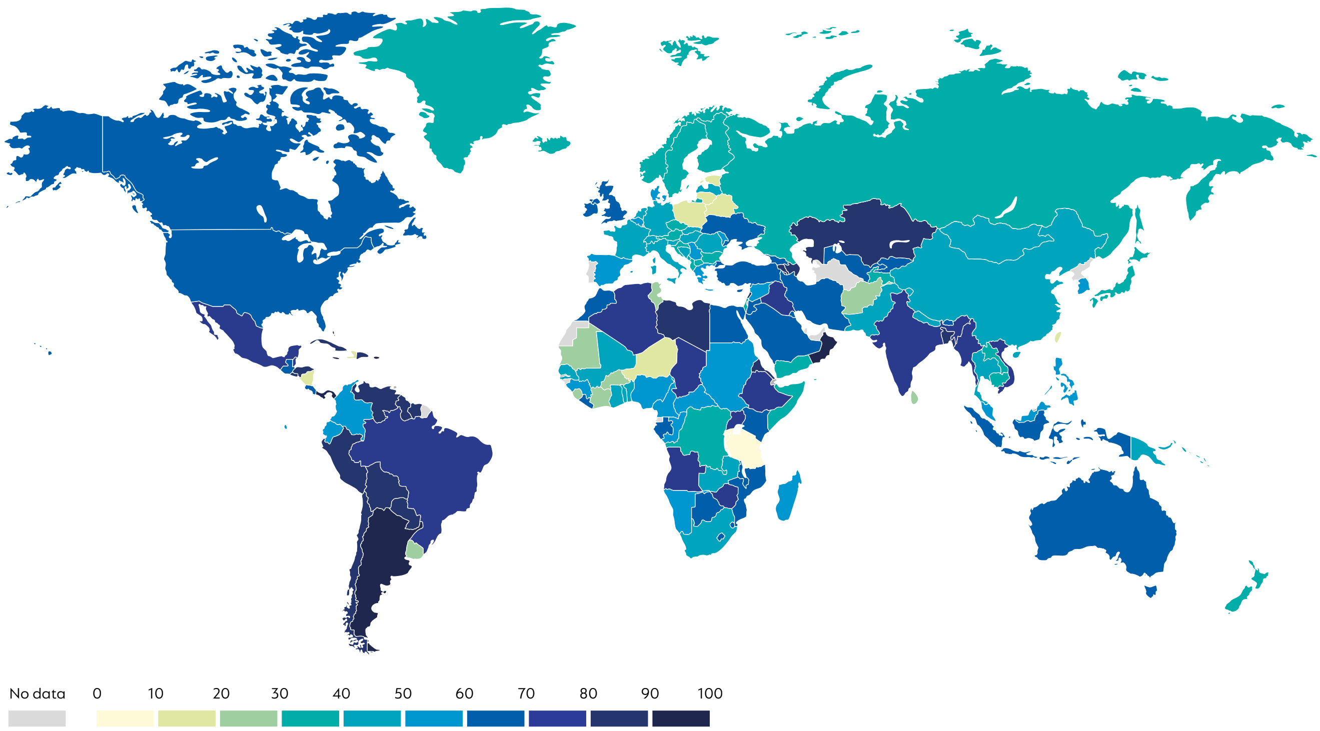
Within emerging markets, things are even more uncertain because the pandemic is not yet contained. While the efficacy of testing regimes varies greatly, available data show daily infection rates are still rising in many emerging markets and under-testing suggests these could be much higher. An inability to contain the pandemic limits the scope for recovery and raises the risk of repetitive lockdowns. The longer this continues, the more it delays any recovery and increases the risk of longer-term damage.

GDP data in emerging markets broadly mirror what has been seen in developed markets, with a record collapse in activity in Q2-20, and some Q3-20 rebound. But the policy tools available to emerging markets to help mitigate the impact of the pandemic on their economies are more limited than those of their advanced peers. So, while the economic impact is likely to last longer and be very painful in emerging markets, with yet-

Figure 2

COVID-19: GOVERNMENT RESPONSE STRINGENCY INDEX

This is a composite measure based on nine response indicators including school closures, workplace closures and travel bans, rescaled to a value from 0 to 100 (100 = strictest). If policies vary at the subnational level, the index is shown as the response level of the strictest subregion.



Sources: Hale, Webster, Petherick, Phillips, and Kira (2020). Oxford Covid-19 Government Response Tracker – last updated 29 September, 15:30 (London time).

Note: This index simply records the number and strictness of government policies, and should not be interpreted as 'scoring' the appropriateness or effectiveness of a country's response.

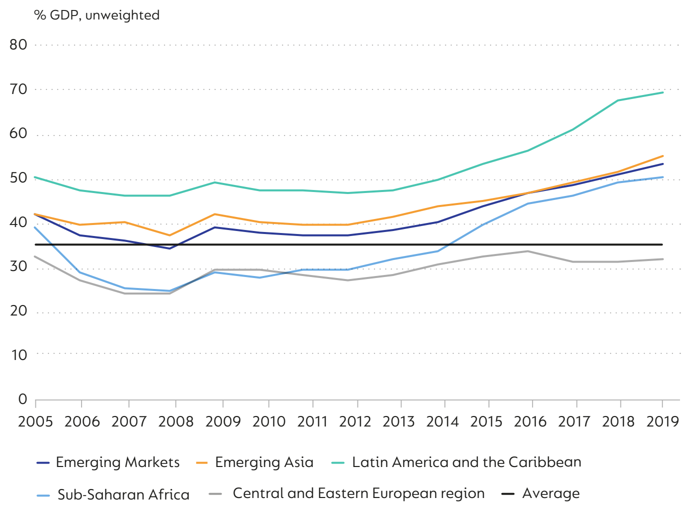
unknown social and political repercussions, the place of lasting vulnerability for most emerging markets will be fiscal policy.

EMERGING MARKET WINNERS AND LOSERS ARE ABOUT RELATIVE FISCAL OUTCOMES

The onset of the Covid-19 pandemic happened when many emerging markets were already fiscally vulnerable – GDP growth was weak throughout 2019 as incomes, profitability and revenues were all under pressure. In many countries, fiscal policy had already turned counter-cyclical, while debt positions were well above pre-Global Financial Crisis levels. Indeed, the IMF estimates that average debt to GDP in emerging markets was 38.8% in 2009, up to 53.3% in 2019, and will add another 20 percentage points of GDP in 2020 as the combination of fiscal support and revenue loss sees deficits balloon and debt ratchet up.

Figure 3

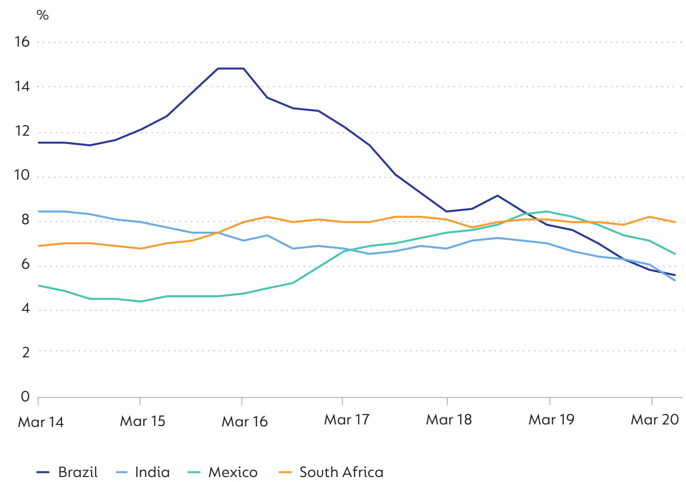
EMERGING MARKET DEBT



Source: UBS

Figure 4

SELECTION OF INTEREST RATES IN EMERGING MARKETS



Source: Haver

Looking ahead, it's hard to see any economic 'winners' emerging from the pandemic. Many economists talk of economic scarring; the idea that the painful economic injury imposed by the pandemic will have lasting, and visible, effects. There are, however, economies that will fare better in relative terms. Broadly, these will be those with shared characteristics that include:

- the realised ability to grow somewhat faster than prevailing borrowing costs;
- those with lower existing debt stock, which will help keep borrowing costs down;
- those with the capacity to ramp up production for manufactured and industrial goods, should demand (internal and external) recover; and
- those with credible governments, and fiscal and monetary authorities.

This may seem like a wish list. However, economies with these areas of resilience will be better able to attract funding and to sustain low interest rates, which will allow for some recovery in nominal growth. Their currencies should benefit from smaller current account deficits, or surpluses, and low inflation should allow policy rates to remain low.

There are relatively few emerging markets that enjoy this happy combination of factors. Among them are China, which for now is already on a path to recovery; some North Asian economies; and Central and Eastern European economies such as Hungary and Poland, which both benefit from their proximity to large markets and access to related supply chains. These countries also have lower starting debt positions and benefit from lower funding costs.

CASE BY CASE

However, for some of the other big emerging markets, the challenges are varied and significant. I discuss a few below:

India has not been able to contain the pandemic, and recent infection statistics put India among the most affected countries currently. India was also already in recession when the pandemic hit. Financial sector fragilities have undermined credit lending and support from the government last year had already helped increase the fiscal deficit. India's starting debt stock was relatively high at 72.2% in 2019, and borrowing costs are being contained by heavy support for the government by >

the national banks. India's ability to see a strong acceleration in economic activity will be key to its recovery, but while the pandemic spreads and lockdown remains tight, the prospect of recovery is further delayed.

Mexico has also had issues with testing, and unofficial estimates suggest both infection and mortality rates may be considerably higher than official data suggest. Here, too, growth was already weak heading into 2020, undermined by a change in domestic economic policy and the trade dispute with the country's biggest external source of growth, the US. While some of this risk has receded with the signing of the United States-Mexico-Canadian Trade Agreement, domestic growth strategies are not yet certain enough to sustain a strong recovery.

President AMLO's commitment to fiscal consolidation, while necessary longer term, has limited fiscal support in the pandemic. This could see Mexico's fiscal position in better relative shape than its emerging market peers listed here, but ongoing support for loss-making state oil company Pemex is a considerable future risk, as is a slow growth recovery.

Brazil also entered the pandemic on a fragile footing, with slow growth and the highest stock of government debt of the countries listed here, at 92% of GDP. Again, infection rates have not been contained, and goverment's pandemic strategy has attracted much criticism. Commitment to pension reform has helped lower borrowing costs, but as growth falters, there is reasonable concern whether this will hold. Here, too, banks have been a considerable support of goverment's borrowing needs.

No economy will emerge from this pandemic in a better position than it went in, and for most, the economic challenges that existed before will be exacerbated by the crisis. However, in all the above countries, as in many developed markets, governments have still been able to continue borrowing from financial markets at relatively low interest rates. This is owed in part to globally low yields, especially in developed markets; in some cases to the direct intervention of the central bank in funding the government; and in other cases, notably in Brazil, India and China, to the State-owned banks buying government bonds.

... WHICH BRINGS US TO SOUTH AFRICA

For now, infection rates have slowed, based on reasonably good testing practice and a hard lockdown early on.

But South Africa does not enjoy the mitigating conditions listed here. Instead, it faces a unique set of economic and policy challenges, and very few have been *caused* by the pandemic:

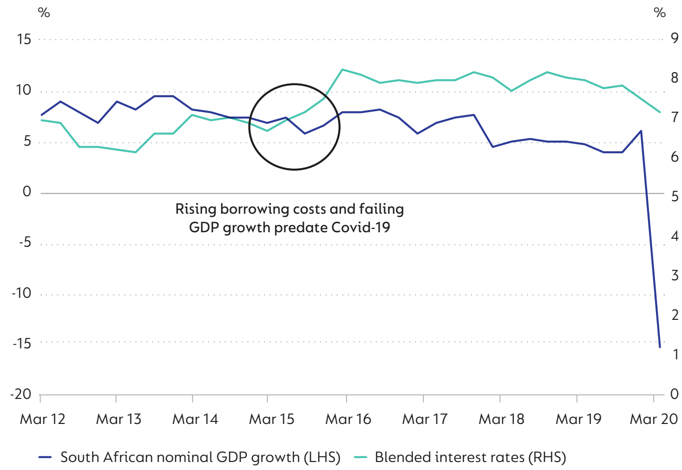
Growth – in real and nominal terms – has been slowing since 2013, when investment started to taper off, undermined by failing confidence, unrest and the reallocation of fiscal resources from investment to wages. As we stand, investment has contracted in real terms in three of the past four years, and took 11.5 percentage points off GDP growth in the Q2-20 crisis depth.

Government's financial position was already vulnerable and increasingly on an unsustainable path, undermined by three things: 1) revenue that was not as resilient as budgeters expected – for the reasons outlined above – and exacerbated by State capture; 2) expenditure, mostly on wages, State-owned enterprise (SOE) bailouts, and increasingly on debt service costs, was unable to adjust fast enough to falling revenues; and 3) economic policy has not been an enabler of economic growth.

In addition, unlike several of its emerging market peers, even the riskier ones highlighted above, South Africa does not enjoy low borrowing costs. Despite aggressive interest rate cuts by the central bank, government bond yields remain very high. In fact, the spread between swaps and government bond yields has widened, which means that domestic corporates can borrow at a lower onshore rate than the (supposedly) 'risk-free' government can.

Figure 5

SOUTH AFRICAN NOMINAL AND REAL GDP GROWTH VERSUS INTEREST RATES



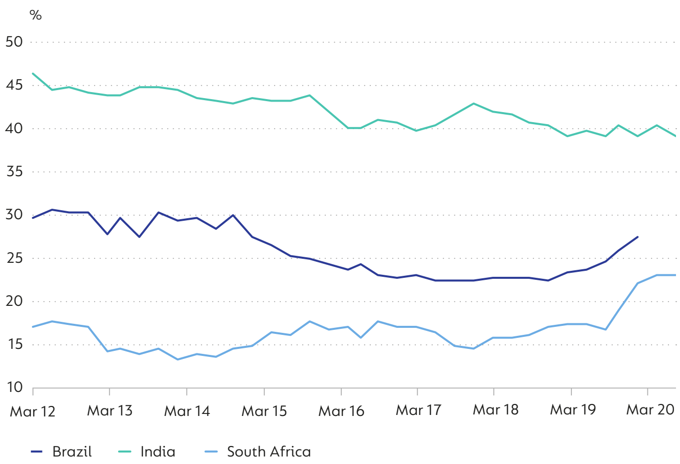
Source: Haver

This in part reflects the fact that in countries like Brazil (as well as India and China), the local banking system is much more supportive of State financing needs – where there are State-owned banks that own a lot more government debt than is seen in South Africa. They also have much less debt held by foreign investors. But it clearly also reflects the market's scepticism about government's ability to put the country and its balance sheet on a more sustainable path. As elsewhere, banks have accumulated government bonds, but they have done so where returns make sense, and they are unlikely to provide the kind of backstop seen elsewhere.

As a result, there have been several calls for the South African Reserve Bank (SARB) to step in and more aggressively accumulate government debt to help alleviate the high cost of borrowing.

Figure 6

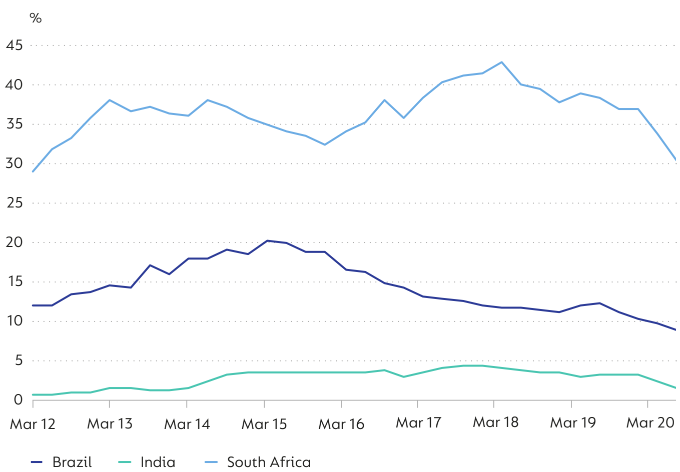
BANK HOLDINGS OF GOVERNMENT DEBT, % TOTAL



Source: Haver

Figure 7

FOREIGN OWNERSHIP OF GOVERNMENT DEBT, %



Source: Haver

The SARB has in fact intervened in the market since March but has been increasingly less present as financial dislocations eased. In August, the SARB bought just R350 million of government bonds. Importantly, the Monetary Policy Committee has been at pains to clearly articulate its view that high market rates reflect a long buildup of fiscal risk that does not have a monetary solution.

The biggest challenge is that the underlying debt dynamics are very problematic. Government needs to change the drivers of these, where possible, to ensure a more sustainable policy trajectory. Without this, any intervention will only yield temporary results, if any. If the SARB intervened aggressively without fiscal commitment to remedy the root causes of its weak position, the risk of foreign investors losing faith is material. South Africa relies on foreign funding, and while holdings have dwindled, they are still significant. In the event that they peter out further, the SARB would have to absorb some or all of the 29.9% of domestic debt foreigners hold, as well as the new issuance. It's hard to see where that would end, and the SARB understands this – heavy intervention could easily become a Pandora's policy box.

The currency would be the main casualty, and ensuing inflation would not only further undermine the SARB's credibility but also efforts to manage long-term rates as the curve reprices. If it's then forced to raise policy rates (or the market reprices short rates), the fiscal impact may be even worse, given the increase in short-term borrowing that would then need to be rolled.

CONCLUSION

A credible, targeted growth strategy, coupled with a sensible and durable commitment to moderating expenditure growth, is needed to reprice government risk. There are signs that government and its social partners in the private sector, including unions, are working towards this. It is not clear that whatever emerges will be enough, soon enough. There is a healthy and deserved scepticism about the government's commitment to implementing new fiscal and economic initiatives because there have simply been too many that were either grossly ineffective, poorly implemented, or mothballed.

It may be that the crisis is yet to come. Government's ability to fund a R700 billion shortfall this year looks as though it will be met. But large consecutive shortfalls in the region of R400 billion to R500 billion will be much more challenging. This reinforces the urgency with which these issues must be addressed, and the steepness of the South African yield curve suggests that within emerging markets, South Africa's case is among the most critical. ✚

SOUTH AFRICAN BONDS

The debt trap continues to beckon

Yet SAGB valuation remains attractive in the longer end of the bond curve

By **NISHAN MAHARAJ**

THE QUICK TAKE

Policy implementation, SOEs and political manoeuvring continue to hamper recovery

Valuation of longer-dated SAGBs offers a significant risk premium

ILBs in the front end of the curve offer an attractive opportunity

Listed credit valuations are still unattractive given underlying fundamentals

Nishan is head of Fixed Interest and has 17 years of investment experience.

THE FIRST CASE of Covid-19 was detected in December 2019, but there was little to suggest how this little microbe would change human history. The world went into differing categories of lockdown to arrest the spread of the virus and allow time for the expansion of healthcare capacity. Ten months later, over 40 million people have been infected, just over a million souls have been laid to rest and the toll on the global economy is still uncertain. Many countries around the world eased lockdown measures as the levels of infection started to recede; however, there is now a rise in second waves of infection, which has heightened uncertainty.

The combination of accommodative monetary policy and fiscal stimulus, the likes of which have never been seen before, helped to soften the recessionary effects of lockdown and keep markets well buoyed. Levels of volatility will remain elevated, due to both the second wave of infections and upcoming geopolitical events (the finalisation of Brexit and the US presidential elections), which have placed big question marks on current valuations.

A PRECARIOUS POSITION

South Africa was precariously placed going into Covid-19, which meant the risk premium in local assets was already lofty. Despite South Africa's early move into lockdown, the poor implementation of policy decisions has highlighted the country's precarious financial situation. Risk premiums increased even further as foreign investors dumped South African assets at a ferocious pace. Local bonds were arguably the most vulnerable, since at the heart of South Africa's problems lay large amounts of debt that needed to be serviced at double-digit yields, amidst very subdued growth.

The All Bond Index (ALBI) is up 3.6% over the last 12 months (1.5% over the last quarter), but is still running behind cash (+5.6% over the last year). This performance was due to the poor showing from bonds with a maturity of greater than seven years. Shorter dated bonds were anchored by the 300-basis point (bp) reduction in the repo rate over the last six months. Only inflation-linked bonds (ILBs) have delivered worse performance, down 2% over the last 12 months (up 1.2% over the last quarter). The total returns of South African bonds (both ILB and nominal) are even poorer when converted to US dollars (approximately -7% for the ALBI in US dollars) and compared to global bonds (6.8% World Government Bond Index return in US dollars), further emphasising how much local bonds have fallen out of favour.

South Africa's fiscal problem is the culmination of many years of poor policy choices. On the expenditure side, the wages of government employees have enjoyed real growth of 3% per annum since 2009, while the economy has only averaged real growth of 1.2% over the same period. This has meant tax revenue has not kept pace, forcing expenditure to be reduced in other, more productive areas.

State-owned enterprises (SOEs) have further crowded out productive expenditure due to their continuous demand for government support, and Eskom remains the biggest risk to the economy. Years of mismanagement have resulted in an unsustainable debt load and unreliable energy supply that place added pressure on the fiscus and reduce the long-term growth potential of the local economy.

Covid-19 has placed a further burden on government finances, as tax revenue will drop by c.R300 billion, which will force hard decisions to be made about further expenditure cuts and other reforms. Interest service costs will skyrocket to around 25% of tax revenue over the next three years, which will place South Africa on the precipice of a debt trap.

Markets have lost faith in policymakers' ability to right the situation. We need to see tangible steps put in place that detail how the bloated wage bill will be reduced, how Eskom will be set on a path to operational and financial stability, and how growth can be reaccelerated. Further disappointments include government's attachment to the beleaguered South African Airways and the scale of misappropriation of government tenders during the Covid-19 crisis.

SOME RAYS OF HOPE

In the past month, there has been some good news. The National Energy Regulator of South Africa has approved a plan to tender almost 12 gigawatts of power generation capacity, predominantly from renewables, and there seems to be consensus on a plan between labour, government and business that will address some of Eskom's problems. In addition, the Independent Communications Authority of South Africa has finally announced that high-demand spectrum will be auctioned this fiscal year, which will introduce between R8 billion and R12 billion of revenue. Another encouraging sign is that there have been some high-profile arrests on the back of the ongoing graft investigations.

South Africa faces yet another watershed budget at the end of October when Finance Minister Tito Mboweni will provide details on how he plans to enact R230 billion worth of savings over the next three years to take South Africa to a primary surplus and pull us back from the brink of a debt trap.

LOCAL BOND OUTLOOK

Despite the poor fundamental overhang, the valuation of South African bonds has adjusted to embed a significant risk premium. In previous publications, we have gone into detail regarding the risk premium embedded in South African government bonds (SAGBs) relative to their emerging market peers, both from a pickup relative to developed market bond yields and an implied real rate perspective. Figure 1 shows the amount bond yields can move before they break even relative to cash. At 100bps to 200bps breakeven, these are extremely attractive. In addition, bonds with a maturity of greater than 10 years offer the most value from this perspective.

In almost all cases where a country falls into a debt trap, the restructuring of debt through a haircut is the first avenue pursued, and these haircuts can vary between 15% and 60%. In the last column in the table, we take a scenario where, after four years, South African debt is haircut by 50%, and we show the total return of the various bonds, including the haircut, up until that point. Due to the higher yields and low cash prices on offer in the long end of the bond curve, once again bonds with a maturity of greater than 10 years outperform, providing further support to keeping duration allocations focused in this area of the curve.

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Figure 1

AVERAGE BREAKEVEN RATES

Bond	Maturity	Yield	1y breakeven (cash @ 4%)	2y breakeven (cash @ 5.25%)	3y breakeven (cash @ 6.25%)	Total return (50% haircut)
R186	21-Dec-26	7.20%	0.82%	1.23%	0.82%	(12.68%)
R2030	31-Jan-30	9.39%	0.96%	1.68%	2.02%	(5.80%)
R2032	31-Mar-32	10.39%	1.02%	1.83%	2.32%	(3.36%)
R2035	28-Feb-35	11.18%	1.06%	1.93%	2.51%	(1.82%)
R2040	31-Jan-40	11.59%	1.03%	1.89%	2.46%	0.06%
R2044	31-Jan-44	11.63%	1.00%	1.82%	2.36%	1.46%
Average breakeven			0.98%	1.73%	2.08%	

Source: Coronation

ILBs have been a poor performer as an asset class, but as with the ALBI, the ILB bond curve is weighted heavily towards longer dated bonds. As is evident in Figure 2, over the last 12 months, ILBs out to seven years have produced decent returns relative to cash, offer an attractive pickup to their nominal bond counterparts and still provide inherent protection against higher inflation. Furthermore, the one-year forward real policy rate (the difference between the repo rate and one-year forward inflation) sits at -1%, which acts as a very strong anchor for short-dated real yields. The risk, which we believe to be negligible at this point, is that the South African Reserve Bank (SARB) moves the real policy rate into a marginally positive area.

LISTED CREDIT VALUATIONS SEEM EXTENDED

The listed credit market was not spared during the Covid-19 selloff; however, the recovery in listed credit spreads has far exceeded the quality of the underlying fundamentals. Once again, the listed corporate market is suffering from a supply/demand imbalance and the primary credit markets have dried up for most of the issuers in the market. Since the SARB relaxed prudential capital buffer ratios for banks, they can now afford to refinance upcoming debt maturities for corporates without forcing them to go to debt capital markets. At the same time, the risk/return characteristics of other asset classes have turned less favourable, making listed credit, with its reduced return volatility, a seemingly attractive opportunity set. Unlike investing in an equity, where one can double or triple one's initial investment, when one invests in a credit, the best one can hope for is to receive one's coupon payments on time and one's capital back at the end. The return profile is therefore discreet; that is, one continues to earn a steady interest rate (coupon) until maturity or default.

Even though underlying fundamentals might be deteriorating, the return of the South African corporate credit market has remained steady, predominantly due to there being large holders of individual issues, hence limiting secondary market activity and price discovery. This reduced volatility hides the underlying risk within the sector currently. In addition, the inclusion of structured products in a portfolio can also be used to reduce the volatility of returns of the underlying credit exposures due to inefficiencies in the mark-to-market process for structured products.

Figure 3 highlights why we believe underlying fundamentals are not being reflected in credit spreads. Bank credit loss ratios have increased dramatically following Covid-19 and are set to remain elevated for at least the next 12 to 18 months as the second-round effects of the crisis make its way through the economy. However, banks pay less for funding now than they did before the crisis or at any point during the last 10 years, despite credit loss ratios (a reflection of the condition of their lending book) being higher now than they were during the Global Financial Crisis, a situation we believe is not sustainable.

The margin of safety in the valuation of listed credit is not very encouraging either. In Figure 4 overleaf we list the yield coming off the SAGB 10-year bond, the yield on a floating credit (spread over three-month Jibar) and the equivalent fixed rate of the 10-year credit to maturity. As is evident, government bonds offer a much more attractive yield versus the underlying credit. The credit's fixed rate to maturity materialises at a much lower yield due to the low level of cash rates and the ability of banks to borrow money at a cheaper rate than government. As an aside, it is cheaper for the average South African to borrow money than the government, given prime is at 7%, highlighting how much risk premium is embedded in SAGB yields. Given current prevailing levels of credit spreads in the listed market and the underlying

Figure 2

INFLATION-LINKED BOND RETURNS AND YIELD

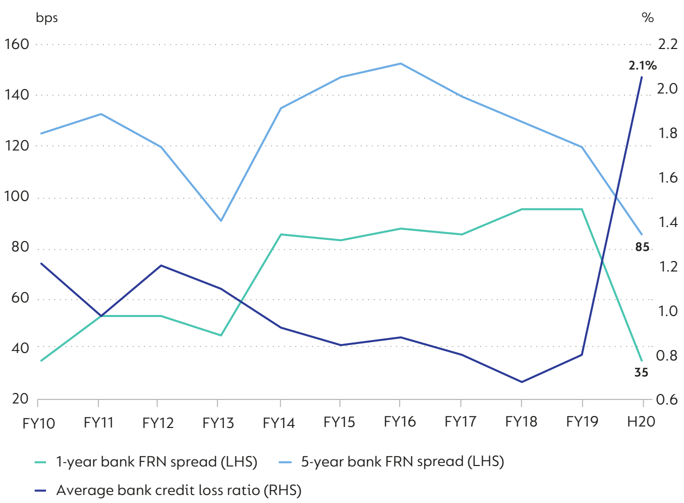
CILI* Index	Total return (last 12 months)	Real yield	Implied nominal yield @ 4.5% inflation	Equivalent nominal yield
1 to 3 years	7.6%	0.9%	5.5%	4.8%
3 to 7 years	7.2%	2.5%	7.2%	7.4%
7 to 12 years	1.7%	4.1%	8.8%	9.8%
Over 12 years	(10.4%)	4.8%	9.5%	11.5%

* Composite Inflation-Linked Index

Source: Coronation

Figure 3

AVERAGE BANK CREDIT LOSS RATIO VS BANK FLOATING-RATE NOTE (FRN) SPREADS



Source: Coronation

Figure 4

10-YEAR SAGB VS 10-YEAR FLOATING RATE NOTE

	Spread	Implied yield	Fixed rate to maturity
10-year government bond	-	9.65%	9.65%
10-year floating credit	3mJ + 1.5%	4.86%	8.58%

Source: Coronation

fundamentals, we believe credit to be an unattractive allocation option within a bond or multi-asset fixed income fund.

BONDS IN YOUR PORTFOLIO

In summary, South Africa is on the brink of a debt trap due to years of poor policy choices that have been exacerbated by the effects of the Covid-19 crisis. At the heart of the country's problems lies a large debt load that is being financed at exceptionally high levels of interest and ailing SOEs, key among them Eskom.

Policy choices are moving in the right direction; however, the political will to implement appears sluggish.

However, the valuation of SAGBs does embed a significant amount of risk premium, commensurate with the underlying risk, if not more. This valuation is specifically attractive in the longer end of the bond curve due to high yields and low cash prices. ILBs in the front end of the curve (greater than seven years) offer an attractive pickup relative to their nominal counterparts with inherent inflation protection, while listed credit is unattractive given expensive valuations.

We believe bond portfolios should have a neutral to overweight position to SAGBs in the longer end of the curve, an allocation to ILBs in the short end of the curve and low (if any) allocation to listed credit. +

SOUTH AFRICAN SECTOR REVIEW

Emergent themes add shine to resources

Transformation through green initiatives and new demand sources

By **NICHOLAS STEIN** *and* **NICHOLAS HOPS**

THE QUICK TAKE

Unprecedented supply restraint meets a strong demand outlook

The move to a green economy is a boon for commodity prices

Management teams are committed to returning cash to shareholders

Nicholas Stein is an equity analyst with 11 years' investment experience.

Nicholas Hops is an equity analyst with seven years' investment experience.

THE FTSE/JSE RESOURCE 10 Index (JSE RESI) has more than doubled off its end-of-2015 lows. The index masks the performance of a number of its constituent shares, where the price rises have been even more spectacular. For example, Glencore, Anglo American plc and Kumba Iron Ore are up 120%, 650% and 1 934%, respectively. With good returns in the bag and healthy commodity prices, it begs the question why we still hold meaningful positions in the resources sector.

We believe that the commodity sector currently has several elements to it that are unprecedented versus historical cycles which, when combined, present a unique investment opportunity. We discuss these themes in more detail below.

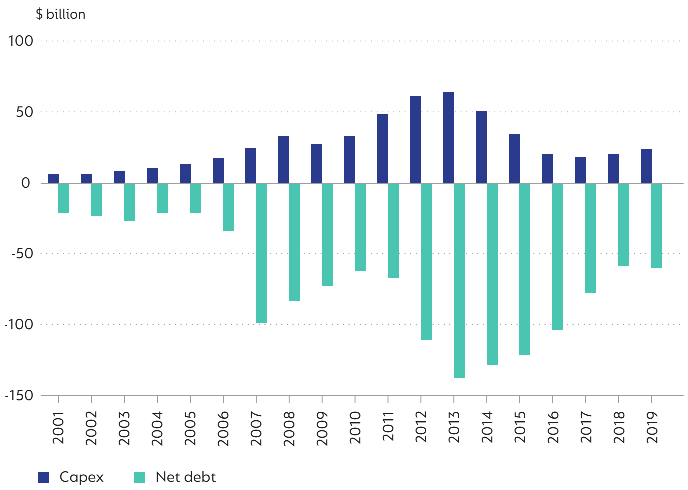
CAPITAL DISCIPLINE

If one considers the previous cycle ending in 2015, it played out broadly as follows: robust demand growth driven by China on which miners capitalised. They then extrapolated it into the future by living beyond their means (increasing debt levels and channelling it into capital expenditure to boost supply) – Figure 1 overleaf. Gearing works in a rising price environment, yet increased gearing is a contributing factor to a deflationary price environment. Over-exuberant investment into volume growth in good or benign times sowed the seeds for oversupply (bad times). This came to a head when there was a wobble in 2015. A deflationary price environment ensued and collided with stretched balance sheets. Low prices and high debt are a toxic combination. The JSE RESI fell 61%, while Anglo American and Glencore lost 80% and 72%, respectively. This led market commentators at the time to question the viability of many of these stocks. Glencore did a rights issue and Anglo American expressed a strong desire to do so.

This 2015 'near-death' experience is firmly entrenched in the minds of mining executives, many of whom have retained their positions in their respective companies. However, they now appear to appreciate the risk of price deflation caused by excess leverage and supply growth, and understand that high gearing and mining companies are not very compatible.

Figure 1

INDUSTRY CAPITAL EXPENDITURE AND NET DEBT



Source: RMB Morgan Stanley

On the back of 2015's wake-up call, companies have started running conservative balance sheets. Rather than anticipating demand growth and bringing forward supply using leverage (basically using balance sheets to balance the market), they're using retained earnings (and allowing commodity prices to balance the market). This places the miners on a firmer financial footing and the sector now lags cycles rather than leading them, resulting in far less slack in the system. Take the 2019 Brumadinho tailings dam disaster that saw Vale's production drop by 34% (c.64 million tonnes). There was simply no alternative supply source able to fill the missing tonnes, which, when combined with stronger-than-expected demand, sent iron ore prices up 68% from January 2019 to today.

While we don't expect this capital expenditure discipline to last forever, we expect it to continue as long as the current cohort of executives remains in place at the companies and/or while share prices remain at levels attractive to valuation-based investors.

CHINA IS GROWING STRONGLY

When it comes to commodities, the trajectory of the Chinese economy is critical, with c.50% of most commodities being consumed in the People's Republic. Of the key commodities, roughly 75% of the seaborne iron ore market goes into China, followed by c.50% of copper and nickel, 32% of platinum group metals (PGMs) and 13% of crude oil. China is heavily dependent on key commodity imports given its lack of an in-country natural resources base. Metallurgical and thermal coal are slightly different, as China has large resources and only relies on imports for higher-quality product and where coastal plants find it easier and cheaper to import product than to transport it from the inland coal-producing regions.

Overall, China still makes up c.20% of the seaborne coal markets, more in line with Chinese GDP as a share of the world's total at 19%. We expect GDP growth in China to continue slowing and the commodity intensity (consumption:GDP) of steel-related commodities to follow suit. Where we expect trend growth to be more resilient and, in some cases, to increase over the next 10 years, is in copper, nickel and PGMs, where moves towards a greener world have very positive implications for these metals.

GREEN CREDENTIALS

Miners are arguably transforming themselves into an ESG[1]-positive industry, spending billions of rands on initiatives such as community programmes, staff training and land rehabilitation, among others. Particularly over the last decade, we have seen a significant decrease in injury and fatality rates in the local mining sector.

The other critical point that perhaps gets overlooked is that you can't make energy-intensive industries greener without the use of certain commodities. Put differently, decarbonising the world requires the use of a number of commodities.

Reducing carbon dioxide (CO_2) emissions requires either a decrease in the population or for the existing population to use less energy. Both scenarios seem unlikely. The alternative is to focus on energy efficiency and reducing the CO_2 intensity per unit of energy generated through low (or no) carbon power generation. Indeed, it is in the latter area where much of the action is taking place today. Two areas of focus are the vehicle drivetrain and electricity production. In both cases, copper is a critical component, given its unrivalled thermal and electrical conductivity.

The vehicle drivetrain is in the process of shifting away from fossil fuel (oil) as a power source to electricity. A typical electric vehicle (EV) requires 150 kilograms of copper. Based on our inhouse assumption of a 25% battery electric vehicle penetration by 2030, combined with mass-hybridisation, this decarbonisation of the drivetrain would require an additional 4.3 megatonnes of copper and 1 150 kilotonnes of nickel. This incremental demand represented 19% and 49% of the 2019 supply base for copper and nickel, respectively, enough to push these markets into material deficits in the years to come.

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[1] Environmental, social and governance factors

Efforts are also under way to transform the electricity mix away from fossil fuels such as coal and towards greener energy sources such as wind and solar. Wind and solar require multiples more copper per unit of power than coal and traditional sources (they require this for increased cabling, as well as generators, inverters and transformers). Investment firm Bernstein estimates that copper demand from wind energy will require an additional megatonne per annum of copper by 2030.

The PGMs also benefit heavily from the shift towards cleaner air and general decarbonisation. In the medium term, PGMs will benefit from increased regulatory pressure on car manufacturers to reduce emissions, with large fines for non-compliance. Adding palladium or rhodium to the catalyst of an emissions treatment system is a natural solution for vehicle and catalyst manufacturers. Longer term, the PGM complex stands to benefit from the arrival of the hydrogen economy, at least a few decades after it was first heralded.

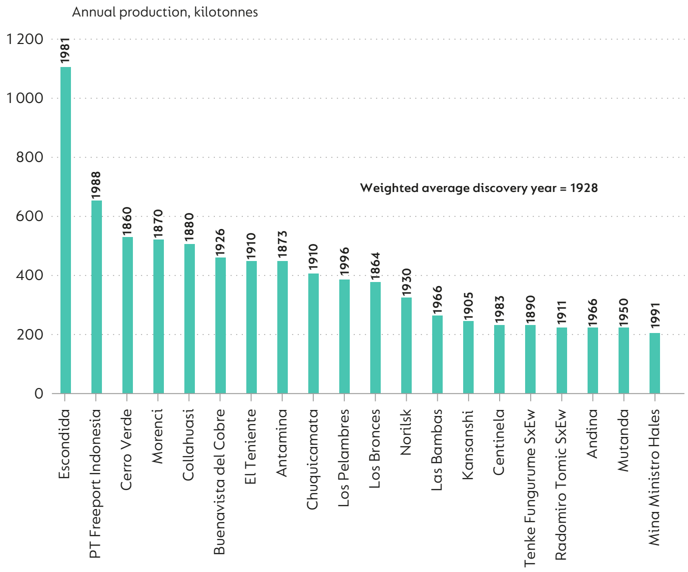
The last 12 months have seen a step change in political will to tackle climate change from most political parties globally as well as large corporates. The most recent stimulus response out of Europe is a clear example, with a continental 'net zero' goal by 2050 and tens of billions of euros committed to the cause. China has also committed to being net zero by 2060.

There is broad consensus that to fully decarbonise, there is a large role for hydrogen to play across a raft of industries. Fuel cells can be used to power ships, heavy- and light-duty vehicles and even buildings, not to mention the burning of hydrogen for heat in heavy industry such as steel and cement manufacturing. Platinum in particular is vital in several elements of a hydrogen-based economy.

We should point out, however, that we aren't thematic investors. We don't see a bullish story for copper simply because it's 'green'. Rather, it's about a new source of incremental demand adding to a constrained supply base. We don't see this as incompatible with a reasonable outlook for thermal coal, which suffers from muted demand growth, virtually no new mine investment and prices that render half the industry unprofitable – a situation that we don't think will persist.

Figure 2

WORLD'S 20 LARGEST COPPER MINES' DISCOVERY DATES



Sources: USGS, Wood Mackenzie, corporate reports, Bernstein analysis

ANGLO AMERICAN

The Anglo American of today is very different from the one of 2015. Aside from the balance sheet (which is now strong), the company has disposed of a number of smaller, higher-cost operations, leaving it with a few large, low-cost, long-lived assets. This has seen return on capital employed improve. We expect further improvement as two key greenfield assets come into production, being Quellaveco (copper) and Woodsmith (crop nutrients). These projects, alongside a number of brownfield expansion opportunities, give Anglo American the most attractive growth profile of its peers over the next few years.

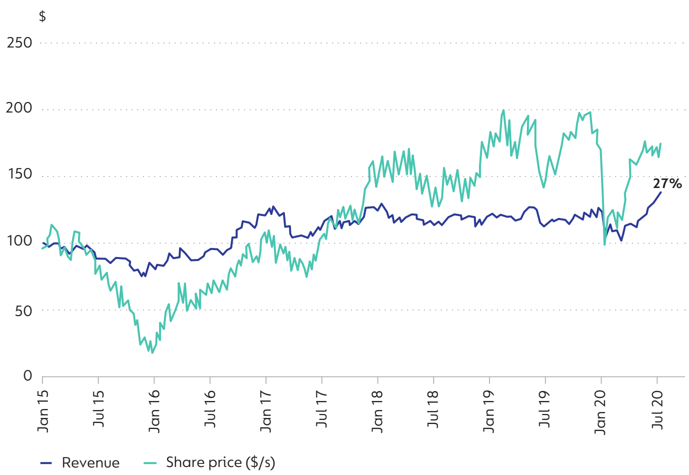
Anglo American's portfolio is well diversified across commodities and geographies. The company has a differentiated portfolio compared to its peers, owing to its exposure to PGMs and diamonds (PGMs are discussed above and overleaf). The outlook for diamonds is the most promising it's been for some time. While 2020 will be exceedingly tough for De Beers, 2021 onwards should see material improvements to the diamond markets owing to current supply discipline, the closure of Argyle (a large Australian diamond mine that has come to the end of its life), and improvement in demand as lockdown restrictions ease globally and on the back of increased diamond marketing by De Beers.

Anglo American has invested meaningfully in technologies to reduce its energy and water use at its assets. These investments are close to bearing fruit. In addition, Anglo American's exposure to copper, nickel and PGMs (over two thirds of normal earnings) positions it well to contribute to the decarbonisation journey we've been discussing.

Anglo American trades on seven times our assessment of normal earnings. This is compelling, given its favourable commodity mix and low-cost, long-lived positions in many of these commodities.

Figure 3

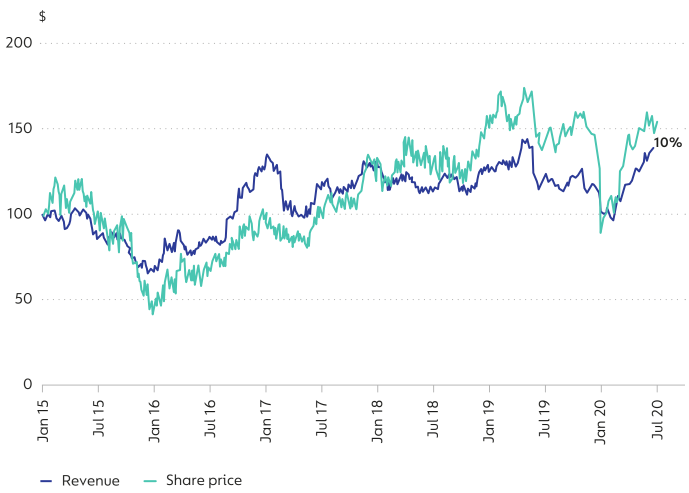
ANGLO AMERICAN SHARE PRICE AND UNDERLYING REVENUE BASKET



Source: RMB Morgan Stanley

Figure 4

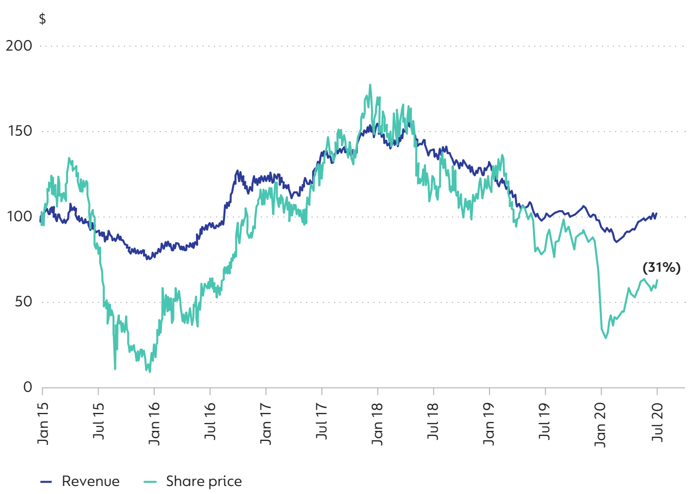
BHP BILLITON SHARE PRICE AND UNDERLYING REVENUE BASKET



Source: RMB Morgan Stanley

Figure 5

GLENCORE SHARE PRICE AND UNDERLYING REVENUE BASKET



Source: RMB Morgan Stanley

PGM STOCKS

We still see meaningful upside in the PGM sector, coupled with the potential for outsized cash returns in the short term. Northam Platinum is a small, growing PGM miner with a highly experienced and entrepreneurial management team. Investments in new, low-cost production at the bottom of the commodity cycle has put Northam in an excellent position to capitalise on this period of high prices. Production growth across three assets over the next few years should drive earnings and cash returns to shareholders, an area where Northam has been exemplary in committing to returning all surplus cash.

Impala Platinum has the potential to return even more cash to shareholders in the medium term, given the steady-state nature of its production and improved operational performance in recent years. Solid delivery by the management team has set the business up to be extremely cash generative in this environment, and we believe they will take further steps in the next 12 months to return shareholder capital. Northam and Impala are the two largest PGM positions within our equity portfolios.

GLENCORE

Glencore is one of the few companies whose free cash flow has been (and will likely continue to be) higher than accounting earnings. As such, a focus solely on accounting earnings misses just how cash generative Glencore is. At spot prices, Glencore trades on a 14% free cash flow yield and we see upside to most of Glencore's key commodities (copper, nickel and coal). Furthermore, Glencore has been good at returning large portions of this free cash flow to shareholders. We think figures 3 to 5 are instructive. First, they highlight the relative weakness that Glencore's commodity price basket has experienced versus Anglo American and BHP Billiton (largely owing to its larger coal exposure and the fact that it does not produce any iron ore).

We are bullish on the prospective outlook for Glencore's commodity basket, and, as mentioned, also on EV metals, which make up almost half of our normal profits.

Another point to note is how weak Glencore's share price has been relative to its commodity price basket. This decoupling started at the time that the US Department of Justice (DoJ) announced it was investigating Glencore. We note that the investigation likely centres on Glencore's holdings in the Democratic Republic of Congo – an issue which predates the company's listing.

We also note that Glencore's compliance department has grown notably since listing (from five members at listing to 150 now). If you make the assumption >

that the underperformance relates to the investigation and that Glencore would have performed in line with its commodity price basket but for this, the market is pricing in a c.$16 billion fine – over eight times higher than the highest fine the DoJ has levied in its history under the Foreign Corrupt Practices Act. We think the market is too penal in its assessment here. We also think the transition away from the old guard of management to new management – a process that has been under way for years and is nearing its conclusion – is not fully appreciated by the market, as highlighted by Figure 6.

Figure 6

CHANGING OF THE GUARD

	At merger	Now
CEO	Ivan Glasenberg	Ivan Glasenberg
Head of mining	n/a	Peter Freyberg
Copper marketing	Telis Mistakidis	Nico Paraskevas
Aluminium marketing	Gary Fegel	Robin Scheiner
Ferroalloy marketing	Stuart Cutler	Jason Kluk & Ruan van Schalkwyk
Iron ore marketing	Christian Wolfensberger	Jyothish George
Zinc marketing	Daniel Mate	Nick Popovic
Nickel marketing	Kenny Ives	Kenny Ives
Coal marketing	Tor Peterson	Tor Peterson
Oil marketing	Alex Beard	Alex Sanna
Copper industrial	Telis Mistakidis	Mike Ciricillo
Zinc industrial	Chris Eskdale	Chris Eskdale
Aluminium industrial	Gary Fegel	n/a
Ferroalloy industrial	Gary Nagle	Japie Fullard
Nickel industrial	Peter Johnston	Marc Boissonneault
Iron ore industrial	Mark Eames	n/a
Coal industrial	Peter Freyberg	Gary Nagle
Oil industrial	Alex Beard	n/a
Agriculture	Chris Mahoney	n/a

Management changes

Source: Glencore company reports

EXXARO

In our view, Exxaro's coal business is mispriced by the market. The bulk of earnings comes from Grootegeluk, one of the lowest-cost, longest-lived coal mines in South Africa. The company's fixed-price contract supplying Eskom (with inflationary escalations) ensures a high degree of margin and cash-flow stability. We are also bullish on thermal coal exports where margins and cash flows are anything but stable. The seaborne thermal coal price trades deep into the cost curve and is unlikely to be sustained at current low levels. Asian demand growth for thermal coal is offsetting European demand declines. A lack of willingness to build and fund new coal mines means supply is under pressure. As such, we expect thermal coal prices to increase.

If you exclude Exxaro's stake in Sishen Iron Ore Company (Kumba Iron Ore's only operating subsidiary), you are not paying anything for the coal business, which generates over R10 per share in annual earnings. While there is a risk around capital allocation errors as Exxaro spends outside of its core competency on clean energy initiatives, we view these as more than priced in. Exxaro's core competence is as a coal miner and returns from green investments are typically lower than those earned from mineral extraction.

TO CONCLUDE

The commodities sector is displaying remarkable supply restraint in the face of healthy margins and incentive prices in several commodities. The decarbonisation of the world that will take place over the next few decades is incredibly positive for metal demand and stands to produce strong price outcomes when combined with supply, which is yet to respond meaningfully. On top of this supportive earnings environment, management teams have committed to delivering material capital returns to shareholders, made more attractive by historically cheap starting valuations. +

EMERGING MARKETS

This is a tale of Davids and Goliaths

Bloated merchant acquirers face disruption in the Brazilian market space

By **LISA HAAKMAN**

THE QUICK TAKE

- Cielo and Rede have dominated the Brazilian merchant acquiring industry for years
- These two Goliaths have exploited their duopoly by overcharging and underserving merchants
- Brazilian merchants have thus generally preferred cash over cards
- Government levelled the playing field by removing card exclusivity rights

Lisa is a portfolio manager with 13 years of investment experience.

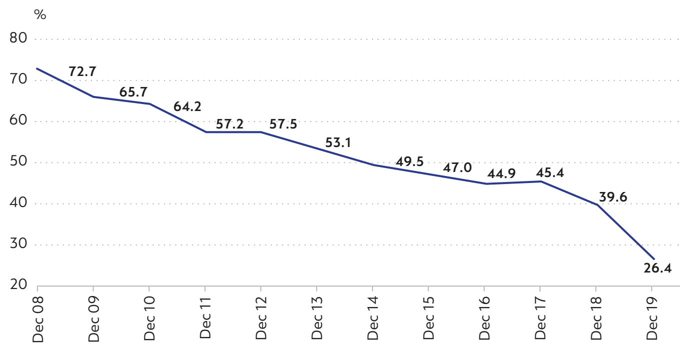
IN THIS STORY, the Goliaths are Cielo and Rede, two companies that have enjoyed and abused a cosy duopoly in the Brazilian merchant acquiring[1] space.

The first giant, Cielo, enjoyed exclusive rights to process Visa cards, while the second giant, Rede, had exclusive rights to process MasterCard.

[1] These enable retailers to accept card payments.

Figure 1

CIELO EBITDA* MARGIN



*Earnings before interest, taxes, depreciation and amortisation

Source: Bloomberg

Cielo is jointly owned by Banco do Brasil and Banco Bradesco (the largest and fourth-largest banks in Brazil, respectively), while Rede is majority owned by Itaú Unibanco (the second largest), which further cemented their position of strength. Together the two companies enjoyed a 90% market share of the merchant acquiring market in Brazil.

Like all bullies, they didn't play fair – both exploited their exclusivity by charging merchants extortionate fees while delivering very little value to their clients. As a listed company, Cielo was a market darling, as its extremely high margins resulted in strong returns for shareholders (Figure 1).

Cash has always been the preferred means of payment in Brazil, and under the reign of Cielo and Rede, there was little incentive for merchants to encourage the use of cards instead. All-in fees for accepting card payment were extremely high, and merchants had to lease or purchase the point-of-sale device from the merchant acquirer at a further cost. In fact, they had to lease or purchase two point-of-sale devices – one from Cielo and one from Rede – if they wanted to accept both Visa and MasterCard.

>

OTHER HEADWINDS

The structure of the Brazilian card market is a further prohibiting factor to card acceptance. In most countries, the merchant acquirer settles the transaction within 48 hours, while in Brazil, card transactions are only settled after 30 days. Furthermore, due to consumer affordability constraints, the Brazilian market has evolved to allow payments in interest-free instalments for everything from clothing to fuel to white goods. The merchant may tier its pricing to compensate for the implied financing it is offering the client, but this places a substantial working capital burden on the merchant who sells a product today and may only receive full payment in 12 months.

Together, these anomalies have caused a general reluctance to accept cards and, as a result, card usage has remained extremely low in Brazil, with credit card usage particularly low (Figure 2).

TOPPLING THE GIANTS

To foster competition in the merchant acquiring sector, the Brazilian government put an end to these exclusive rights in July 2010.

This paved the way for the emergence of new competitors and enabled a rapid disruption of the status quo. New entrants have succeeded by solving many of the pain points of accepting cards – high fees, poor service and a large working capital outlay.

We own two of these new competitors, the Davids in this story, Stone and PagSeguro.

Stone was founded in 2012, and primarily targets the small, medium and micro enterprise (SMME) market in Brazil. The company's key selling point at launch was a better quality (and cheaper) point-of-sale device (that accepted both Visa and MasterCard), lower merchant discount rates and superior service levels. Merchants are serviced via hubs located around the country, staffed by Stone agents. Besides better service, Stone's key differentiator is the software add-ons that merchants can use for order and sales management, invoicing, inventory management, cash and payments management, customer relationship management, logistics and e-commerce integration. Instead of merely facilitating payments, Stone's offering empowers businesses to perform better and enables all-important e-commerce integration.

Stone also prepays the yet-to-be-received instalments to the merchants at affordable funding rates, and merchants can elect to have transactions settled immediately rather than only after 30 days, allowing businesses to manage their cash flow and grow faster. At the same time, this provides a valuable and risk-free revenue stream for Stone, which has the balance sheet to fund this prepayment.

PagSeguro entered the micro-merchant space in 2013 with a similarly differentiated approach. Its proposition is a very simple and affordable point-of-sale device, with transparent and standardised pricing for all clients. PagSeguro's offering is entirely digital, and all processes are standardised, allowing the company to keep costs low and hence offer compelling pricing to clients. This has allowed micro-merchants to accept card payments at a reasonable cost. PagSeguro also prepays the instalment sales and offers merchants immediate settlement to assist them with cash flow.

There is some risk that the structure of the market changes to a shorter settlement period, removing an important revenue source for both companies; however, we believe that merchant discount rates would increase to compensate, converging with the rate they currently charge for immediate settlement.

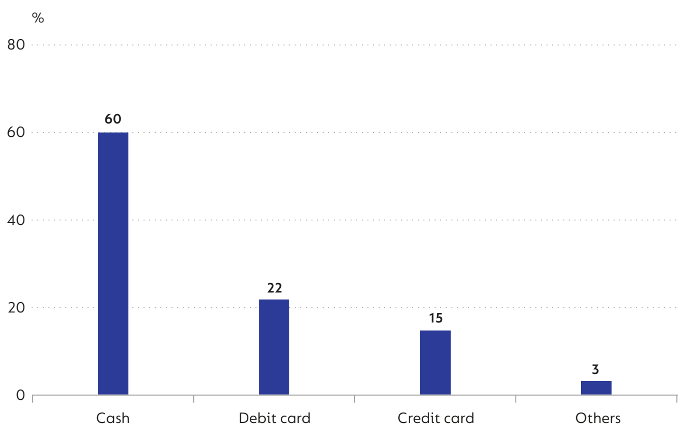
INNOVATION AND AGILITY

Both Stone and PagSeguro were able to gain market share quickly as a result of their differentiated propositions and their lower pricing, which has resulted in a reduction of the merchant discount rate for the country as a whole (Figure 3 overleaf).

As they've grown, they've also evolved to offer more services to enhance customer stickiness. Stone recently launched a basic banking product enabling electronic transactions, bill payments, and cash in and out, as well as working capital loans. As of 30 June 2020, 48% of Stone's merchants had

Figure 2

PAYMENT METHOD MOST USED FOR IN-PERSON TRANSACTIONS IN BRAZIL IN 2018



Sources: Atlantico Study, Banco Central do Brasil 2018 Study subscribed for a bank account and 9% for credit. Stone continues to add software capabilities it believes will help clients, and the company is the preferred bidder for Linx, Brazil's largest software company, specialising in omnichannel retail.

PagSeguro launched PagBank, a full-spectrum digital bank, to enhance its ecosystem. The bank has proved immensely popular, and the take-up by both merchants and external consumers has been impressive. PagBank has already amassed 4.9 million customers since launch a year ago.

TOO LITTLE, TOO LATE

The primary incumbents (Cielo and Rede) are now left with a conundrum. They previously each enjoyed a monopoly over their card network and hence had no need to invest in product or innovation or service. Their cost bases became as bloated as their revenue bases. As a result, they are now in a position where they cannot afford to cut pricing. They are also owned by their respective banks and hence do not offer the entire ecosystem of acquiring, banking and credit, as this would result in them competing with their parents. These companies have realised too late that it's better to disrupt yourself than be disrupted by others. Cielo, in particular, has been slow to improve its offering and has lost substantial market share (Figure 4).

Stone and PagSeguro's runway for growth is extremely long. They are well positioned to continue taking market share from the two incumbents. More importantly, the pie is also growing quickly. Card usage remains low in Brazil, but accelerated due to Covid-19 when a large proportion of personal consumption expenditure moved online – a habit we believe will continue even after the pandemic. We believe that the cash-to-card conversion is set to accelerate further, providing a structural tailwind for both these companies.

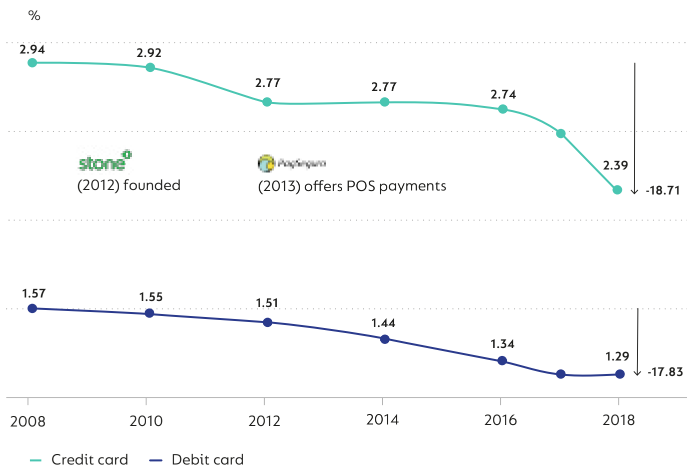
Our estimates assume that card penetration will increase from 33% to 56% over the next 10 years (Figure 5).

Consequently, we are excited about the prospects for these two companies, which are managed by smart and innovative teams. Both shares have performed well over recent months; however, we believe that they remain attractively valued over a longer-term horizon.

We feel that the market is overlooking the strength of their ecosystems and the length of their runways for growth. As such, we are confident that these Davids will topple the two Goliaths of Brazil's merchant acquiring industry. ✚

Figure 3

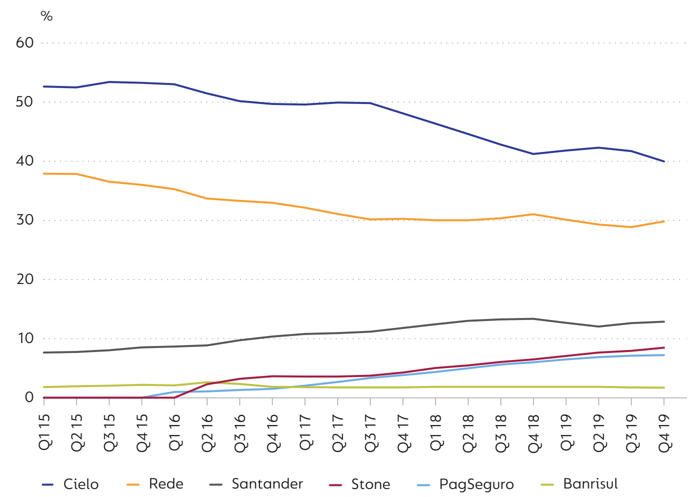
MERCHANT DISCOUNT RATE OVER TIME



Sources: Banco Central do Brasil, ABECS

Figure 4

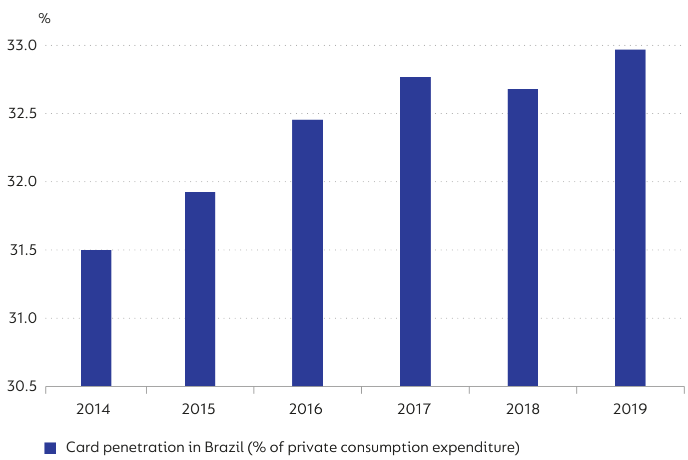
MARKET SHARE OF MAIN PLAYERS



Source: UBS

Figure 5

CARD PENETRATION IN BRAZIL



Source: Bradesco

MARKET REVIEW

Local opportunity amidst global uncertainty

NOTWITHSTANDING THE LINGERING Covid-19 uncertainty and distressed economic conditions around the world, equity markets continued to grind higher in anticipation of the post Covid-19 economic recovery, aided by unprecedented fiscal stimulus and record-low interest rates.

During the third quarter of 2020 (Q3-20), the MSCI All Country World Index (+8% in US dollars) rallied to recover all of its losses for the year. US equity markets in particular were strong, with the S&P 500 (+8.9%) and Nasdaq (+12.6%) both reaching new all-time highs. Emerging markets, underpinned by China, also produced strong returns of 9.6%, while European equity markets lagged at 4.5%. The Bloomberg Barclays Global Aggregate Bond Index gained 2.7% during Q3-20. Low yields, record levels of government indebtedness and continued monetary policy expansion by central banks around the world leave us very negative on the long-term return prospects for global bonds. Gold continued its rally, increasing nearly 7%.

The rand remained volatile but ended the quarter more than 3% stronger against the US dollar on broad-based dollar weakness. Local sentiment also improved, informed by a relaxation in lockdown restrictions and some long-anticipated arrests by our law enforcement authorities. More arrests, and successful prosecutions, are crucial to restore investor confidence in our governance structures and our economy.

While the All Bond Index ended Q3-20 up 1.5%, its 3.6% return over the past 12 months is still behind the 5.6% cash yield over the same period. The FTSE/JSE Capped Shareholder Weighted All Share Index appreciated 1.0% for the quarter, but the outcome over the past 12 months remains a decline of 5%. The resources sector had another very strong quarter and was up 6%. Platinum stocks especially were up strongly (+21.6%) on the back of a rising platinum group metals basket price and after reporting good annual results. The industrial and financial sectors (both down around 2%) continued their recent underperformance, while the property sector had another challenging quarter and ended down 15%.

All global returns mentioned are expressed in US dollar and all South African returns in rand.

Key performance indicators and fund performance

AS AT 30 SEPTEMBER 2020

		QTD	YTD	1 YEAR	3 YEARS	5 YEARS	10 YEARS	15 YEARS	20 YEARS
INTERNATIONAL INDICES [USD]									
Global Equity	MSCI ACWI	8.1%	1.4%	10.4%	7.1%	10.3%	8.5%	6.5%	-
	MSCI WORLD	7.9%	1.7%	10.4%	7.7%	10.5%	9.4%	6.6%	5.0%
	MSCI GEM	9.6%	(1.2%)	10.5%	2.4%	9.0%	2.5%	5.8%	7.8%
	S&P 500	8.9%	5.6%	15.1%	12.3%	14.1%	13.7%	9.2%	6.4%
Global Property	Global Property (FTSE EPRA/NAREIT Developed Index)	2.3%	(19.1%)	(17.5%)	(0.5%)	3.0%	5.6%	4.6%	-
Global Bonds	Barclays Global Bond Aggregate	2.7%	5.7%	6.2%	4.1%	3.9%	2.4%	3.8%	4.8%
US Cash	3 Month Libor	0.1%	0.6%	1.1%	1.9%	1.5%	0.9%	1.7%	1.9%
SPOT RATES AND COMMODITY PRICES									
Exchange Rates	Rand Dollar exchange rate	17.4	14.0	15.1	13.5	13.8	7.0	6.3	7.2
	Rand Dollar % change	3.6%	(16.4%)	(9.7%)	(6.8%)	(3.8%)	(8.4%)	(6.3%)	(4.1%)
	Rand Euro exchange rate	19.5	15.7	16.5	16.0	15.5	9.5	7.7	6.4
	Rand Pound exchange rate	21.5	18.6	18.6	18.0	20.9	10.9	11.2	10.7
Select Commodities	Gold price (USD)	1768.1	1523.0	1485.3	1283.1	1114.0	1307.0	473.3	273.7
	Oil price (USD barrel)	41.3	66.2	60.8	56.8	48.4	82.3	63.5	29.8
SOUTH AFRICAN INDICES [ZAR]									
SA Equity	ALSI (J203T)	0.7%	(2.5%)	2.0%	2.4%	4.8%	9.6%	11.3%	13.3%
	CAPI (J303T)	1.5%	(3.7%)	0.9%	1.5%	4.2%	9.3%	11.3%	-
	Capped SWIX (J433)	1.0%	(9.8%)	(5.0%)	2.0%	(2.4%)	1.1%	-	-
	Resources Index (J258)	6.0%	11.9%	27.3%	20.3%	16.3%	4.9%	7.6%	12.1%
	Industrial Index (J257)	(2.3%)	4.3%	4.3%	(0.7%)	2.7%	12.4%	14.3%	14.0%
	Financials Index ex property	1.3%	(29.0%)	(26.7%)	(5.8%)	(2.1%)	8.0%	-	-
SA Property	Africa All Property Index (J803T)	(15.4%)	(47.8%)	(47.2%)	(25.2%)	(15.2%)	0.8%	-	-
SA Bonds	BEASSA (TR) All Bond Index	1.5%	1.8%	3.6%	7.3%	7.6%	7.6%	8.0%	10.0%
SA Cash	Short Term Fixed Interest 3 Month Cash Rate	0.9%	3.9%	5.6%	6.5%	6.7%	6.1%	7.0%	7.7%
SA Inflation	Inflation	1.8%	2.8%	3.1%	4.1%	4.7%	5.1%	5.6%	5.7%

	QTD	YTD	1 YEAR	3 YEARS	5 YEARS	10 YEARS	15 YEARS	20 YEARS	SINCE LAUNCH
DOMESTIC FUNDS (PERFORMANCE IN ZAR)									
Coronation Top 20 Fund	1.3%	(3.4%)	3.9%	0.8%	5.2%	9.3%	12.4%	16.2%	16.2%
ASISA Mean of South African Equity General	1.1%	(7.0%)	(3.0%)	(1.1%)	1.7%	6.9%	9.0%	12.5%	12.5%
Coronation Market Plus Fund**	2.9%	(0.7%)	2.8%	1.5%	5.0%	9.6%	11.1%	-	14.3%
ASISA Mean of South African Multi-Asset Flexible	1.2%	(3.0%)	(0.3%)	0.8%	2.9%	8.1%	8.8%	-	10.1%
Coronation Balanced Plus Fund	2.7%	(0.2%)	3.7%	2.6%	4.5%	9.2%	10.9%	13.1%	13.6%
ASISA Mean of South African Multi-Asset High Equity	1.3%	(0.7%)	1.8%	2.3%	4.0%	7.7%	8.9%	11.7%	11.8%
Coronation Capital Plus Fund	1.7%	(0.1%)	1.1%	2.2%	4.0%	7.3%	9.0%	-	11.0%
ASISA Mean of South African Multi-Asset Medium Equity	1.1%	0.6%	2.5%	3.1%	4.4%	7.4%	8.0%	-	10.3%
Coronation Balanced Defensive Fund	1.8%	1.6%	2.9%	4.4%	5.7%	8.5%	-	-	8.9%
ASISA Mean of South African Multi-Asset Low Equity	1.0%	1.3%	2.8%	4.1%	5.1%	7.3%	-	-	7.3%
Coronation Strategic Income Fund	1.0%	2.1%	3.5%	6.6%	7.5%	8.1%	8.7%	-	9.9%
ASISA Mean of South African Multi-Asset Income	1.5%	3.5%	5.3%	6.9%	7.3%	6.9%	7.4%	-	8.9%
INTERNATIONAL FUNDS (PERFORMANCE IN USD)									
Coronation Global Equity Select Fund	6.6%	(2.3%)	10.1%	4.0%	9.8%	-	-	-	5.5%
Coronation Optimum Growth Fund	6.9%	2.4%	12.6%	5.2%	11.0%	7.0%	6.0%	9.4%	9.6%
Coronation Global Managed Fund	4.7%	(1.6%)	6.5%	2.4%	6.6%	5.7%	-	-	5.9%
Coronation Global Capital Plus Fund	1.8%	(2.1%)	2.1%	2.3%	4.1%	3.3%	-	-	3.8%
Coronation Global Strategic Income Fund	0.6%	(0.2%)	0.9%	1.8%	1.7%	-	-	-	2.3%

* All ASISA averages exclude Coronation funds in that category

** Highest annual return (Coronation Market Plus): 50.0% (Aug 2004 - Jul 2005); lowest annual return: -20.1% (Mar 2008 - Feb 2009); fund launch date 2 July 2001

Meaningful periods

Figures as at 30 September 2020; for detailed fund performance, refer to pages 48 and 50

FUND UPDATE

Coronation Balanced Plus and Coronation Equity funds

By **KARL LEINBERGER, SARAH-JANE ALEXANDER** *and* **ADRIAN ZETLER**

Karl is Chief Investment Officer (CIO) and manager of Coronation's Houseview strategies.

Sarah-Jane is a portfolio manager with 16 years of industry experience.

Adrian is a portfolio manager with 11 years of investment industry experience.

BOTH THE EQUITY Fund (our diversified general equity fund) and the Balanced Plus Fund (our flagship multi-asset fund for pre-retirement investors) had a satisfactory Q3-20, returning 3.0% and 2.7%, respectively. Both funds continue to perform well against their peer groups over all meaningful, longer-term periods, which aligns to our long-term investment horizon.

Our large global equity weighting added to performance in both funds during the quarter. Although global equity markets have recovered strongly off their lows, we continue to believe that valuations look reasonable – especially relative to other asset classes. Balanced Plus also benefited in Q3-20 from no international government bond exposure and a meaningful position in gold. Although we reduced the gold position during the quarter, we believe that in a world characterised by ongoing pressure on policymakers across the globe to print and spend, zero interest rates and heightened geopolitical risks, gold has a unique role to play in protecting the Portfolio.

STREAMING OFFERS ATTRACTIVE FLOWS

One of the new additions to the Equity Fund is Tencent Music Entertainment Group (TME). TME is a subsidiary of Tencent and owns the leading music streaming platform in China, with a staggering 650 million monthly active users. TME also owns a suite of cash-generative social entertainment businesses, including the dominant online karaoke app and various live-streaming apps on which users interact with performers online. There are significant synergies between these platforms.

TME is well positioned to play a leading role in the multi-year development of the Chinese audio industry. The nascent music market is growing off a low base, with consumers increasingly willing to pay for digital content. While TME's proportion of paying users is growing rapidly, it remains low (7%) when compared to global peers, such as Spotify (c.50%). Average revenues per user are also very low, with significant scope to increase. The group has also moved into adjacent areas such as record label activities, thus offering artists the full spectrum of services, from music creation to distribution. More recent initiatives such as live concerts and a broader push into audio, including podcasts, provide additional future revenue streams.

TME has an excellent management team and a fortress-like balance sheet, with over $3 billion of net cash (13% of market cap), which positions the company well to execute its strategy. We expect healthy revenue growth of around 20% p.a. over the medium term, with even faster earnings growth as the music platforms and new initiatives turn profitable. TME trades on 22 times free >

cash flow adjusting for its cash balance and stake in Spotify (worth over $1 billion), a level we view as attractive given the earnings growth profile of the business.

DOMESTIC EQUITY ATTRACTIVE

Although we are cognisant of the risks around South Africa's worsening fiscal position and the risk of a debt trap, we believe that South African government bonds remain a reasonably attractive investment opportunity, given their high yields and the absence of near-term inflation pressures in the local economy.

Good stock selection in the funds added to local equity market returns. Given the compelling value on offer, we increased our domestic equity exposure during the quarter. While the domestic equity holdings remain skewed to rand-hedge stocks, which are attractive for stock-specific reasons, we have also been increasing our exposure to domestic-facing stocks, many of which we believe are very attractively priced.

One example is the local life insurance sector. Life companies have appealing attributes, including 'sticky' product (retirement savings and life insurance); extensive and hard-to-replicate distribution networks; c.30% to 40% earnings exposure to equity markets, which we think offer good value; the ability to generate fees during lockdowns; diversified earnings streams; and strong capital positions.

Embedded value is a reasonable proxy for life insurance valuations. Life company share prices have derated meaningfully relative to embedded value, with, for example, the Momentum Metropolitan share price moving from a premium to embedded value in 2015 to a 40% discount today. New management has impressed us through its implementation of a turnaround and has placed the business on a firmer footing, as evidenced in Metropolitan Life's recent results. We don't think the market gives enough credit to the turnaround that is under way. Meaningful earnings pain was taken now in the form of Covid-19 provisions. We believe these will support robust earnings growth in future periods.

Sanlam is another recent addition to the funds. We have long admired the business for its strong growth profile, high-calibre management team and high levels of accounting prudence. Historically, we haven't owned Sanlam, given a stretched valuation and the lack of a margin of safety. The recent selloff has allowed us to buy this quality compounder at an attractive valuation.

The funds also benefited from exposure to Shoprite, Anglo American, Northam Platinum and Impala Platinum, as described more fully in Neville Chester and Nicholas Stein's commentary on page 36. We have also added to our Glencore position on share price weakness. Other material activity during Q3-20 was the switching of our remaining Prosus holding into Naspers because we believe the additional discount to intrinsic value is highly attractive. We also trimmed our Anheuser-Busch InBev position on share price strength and opportunistically added to our FirstRand position, along with some other domestic stocks.

TO CONCLUDE

In this uncertain world, our objective remains building diversified portfolios that can absorb unanticipated shocks. We will remain focused on valuation and will seek to take advantage of attractive opportunities that the market may present to us. We are excited by the current portfolios and, given compelling valuations, also about future return prospects. +

FUND UPDATE

Coronation Capital Plus and Coronation Balanced Defensive funds

By **CHARLES DE KOCK** *and* **PALLAVI AMBEKAR**

Charles co-manages the Absolute Return funds with Pallavi Ambekar and has 34 years of investment experience.

Pallavi co-manages the Absolute Return funds with Charles De Kock and has 16 years of investment experience.

THE FUNDS ARE managed to meet the needs of more conservative investors drawing an income from their portfolio over an extended period, and to provide a well-considered balance between risk and return. Both funds had a reasonable third quarter in 2020 (Q3-20), returning 1.7% and 1.8% respectively. All asset classes, bar South African property, contributed positively.

On the domestic front, the South African economy contracted severely in the second and third quarters of the year as the brunt of Covid-19 lockdowns impacted activity. We expect a tepid recovery as the year progresses and only see the country returning to 2019 levels of GDP by early 2023. Globally, the virus seems to be staging a second wave and there are many large uncertainties, including the outcome of the US elections, the Brexit negotiations, and geopolitical tensions between China and various countries. In general, however, the US, UK and Chinese economies seem better positioned to recover from Covid-19 due to quicker access to vaccine treatments, better support from government programmes and more coordinated economic policies.

EQUITY EXPOSURE INCREASED

Effective global exposure in the funds has increased steadily from the beginning of the year to 28% (Capital Plus) and 27% (Balanced Defensive). We have mainly increased our holding of global equities, as the other asset classes look expensive (global bonds) or face structural headwinds (global property). While certain equity indices such as the US S&P 500 look expensive and have rallied hard from the bottom, it has been a narrow market, with only a few shares delivering the bulk of the performance. There remain many compelling valuation opportunities in the broader market.

We have also increased our local equity allocation. The majority of our exposure is to attractively valued rand-hedge shares, such as British American Tobacco and Anheuser-Busch InBev. Despite South Africa's ban on the sale of alcohol and tobacco during the hard lockdown period, these businesses have generally managed to trade their products in many other countries. We think these businesses are defensive and can show real revenue and earnings growth in hard currencies over the medium term. Most importantly, they are strong free cash flow converters, and will use their cash to de-lever their balance sheets and return cash to shareholders. This combination of decent earnings growth and dividend returns is attractive for our portfolios. We have also been adding to domestic businesses that we think have resilient franchises and healthy balance sheets, and can >

deliver earnings growth in a constrained economy. Low expectations are baked into market prices and if we see a better-than-anticipated recovery in earnings bases, we think there will be a robust real performance from our selected basket of equities.

DEBT A CONCERN

The increase in global and local equity allocations has been funded from our South African fixed income allocation. South African bonds still offer very attractive real yields, especially in the long end of the curve, and the funds still have healthy allocations to a mix of government bonds, inflation-linked bonds and corporate credit. But we also recognise that a rising government debt burden and widening fiscal deficit will require some serious intervention by the Finance Ministry. While government acknowledges the seriousness of the economic situation, we think that there is a non-negligible risk that we do not see the decisive policy changes and expenditure reform plans the economy needs to avoid a debt trap.

We remain very cautious on South African property and have not increased our exposure here. Most real estate companies entered the Covid-19 crisis with stretched balance sheets. Pressure on net rental income is likely to intensify and we think a capital restructuring will be necessary for many counters. We had a small allocation to South African property, and we have seen a significant derating of this sector. Despite this, we don't think valuations are compelling enough to increase our allocation.

TO CONCLUDE

The funds have found it difficult to beat their inflation-plus benchmarks, as very few asset classes have delivered the required level of real returns in the last five years. Risk assets, in particular domestic equity and domestic property, have shown sub-inflation to negative returns over this period. Safer assets, such as South African cash and South African fixed income, have outperformed domestic risk assets on a relative basis. However, rising risks for domestic bonds and cash returning less than 4% mean that these assets have become less appealing.

Where we are now, the outlook for risk assets is certainly not rosy, but valuations more than reflect this. We have thus increased our risk asset exposure. We remain mindful of the funds' dual mandate and use asset class diversification as well as appropriate put protection to preserve capital. While the outlook remains uncertain, we believe this creates attractive investment opportunities and that a considered increase in risk exposure is justified at this point to enable the funds to deliver on its mandated inflation-plus return hurdles in the future. +

Note: For more detail on appropriate investment strategies for retired investors, download the *Corolab: The Income and Growth Challenge* investment guide from the publications section on *www.coronation.com.*

FUND UPDATE

Coronation Market Plus and Top 20 funds

By NEVILLE CHESTER and NICHOLAS STEIN

Neville is a senior portfolio manager with 23 years of investment experience.

Nicholas is an equity analyst with 11 years of investment experience.

THE MARKET PLUS Fund, a multi-asset fund aimed at long-term investors growing wealth outside the retirement system, delivered a return of 2.9% in the third quarter of 2020 (Q3-20), which is 1.1% ahead of benchmark. Over the past decade, the Fund returned 9.6% p.a. net of A-class fees. Top 20, our concentrated South African equity fund, returned 1.3% in Q3-20 and is ahead of the benchmark year to date. Top 20 celebrates its 20th anniversary this month and has delivered compelling alpha of 3.6% p.a., net of A-class fees, since inception.

Given the extreme moves in many asset classes and currencies earlier this year, there have been significant opportunities for adding value as markets recovered from the lockdown-driven collapses around the world. The flooding of developed markets by central bank monetary easing and enormous fiscal stimulus programmes is still having an enormous impact on capital markets. In this environment, one must be wary of getting caught up in short-term price moves when the underlying economic conditions remain treacherous.

JSE-LISTED EQUITY COMPELLING

In Market Plus, we increased overall equity exposure to 67%, mainly focused on South African equities, which now make up 45% of the portfolio. We trimmed the global position and re-established some put protection ahead of the US election period, given the high levels of markets and uncertainty around the potential outcome.

In contrast to global markets, the South African equity market looks extremely cheap. While we have successfully avoided owning a lot of South Africa-specific shares that have performed really poorly, their valuations are now such that we cannot ignore the compelling investment opportunities. In addition, recent results indicate that operating performance has not been as poor as we initially expected, although we are cautious about reading too much into this, as the economic damage from the harsh government lockdown will be felt for many years to come. Emerging market economies like South Africa have limited financial resources and institutional capacity to withstand the tough economic outlook we expect to prevail.

The global shares listed on the JSE, both industrial and mining, are also generally still cheap, making the decision to own more JSE-listed shares an easy one. Of course, the path to achieving the expected returns will be bumpy, and any global selloff will still impact the local bourse, even if our shares are not as richly rated as those on developed market exchanges. However, as long-term investors, the ability to own businesses >

on earnings yields in excess of 10% when short-term interest rates are below 4% makes compelling sense in the long term. Our two largest locally listed global holdings remain Naspers and British American Tobacco. We wrote about Naspers and Prosus last quarter. We used Prosus as a funding source during Q3-20, including switching some of our Prosus shares into Naspers. The Naspers discount to Prosus continued to widen, reaching 30%. While we expect some discount to persist, we think the quantum is too wide and that management will take action to deal with the discount in due course.

In a world starved of yield, we find British American Tobacco's 8% dividend yield to be very compelling. In addition, unlike a government bond, we would expect this yield to grow over time. The market remains concerned about a possible menthol ban in the US (US menthol is responsible for c.25% of group profits). However, tobacco legislation tends to play itself out over periods of many years in the US. A menthol ban in Canada saw a limited reduction in smoker numbers and 99% remained with their current cigarette brand. British American Tobacco is also well placed to be one of the winning companies in next-generation products, such as e-vapour and heated tobacco.

We remain constructive on the miners. We believe the commodity sector has several elements to it that are unprecedented versus historical cycles, which, when combined, present a unique investment opportunity, as we report on page 22. We continued adding to our Glencore position during the quarter.

A TILT TO DEFENSIVE STOCKS

Our exposure to local companies remains largely tilted towards defensive businesses with strong economics. A tough economic climate will see strong companies getting stronger and companies with pricing power outperforming weaker ones.

This was well highlighted by the results reported by Shoprite. Shoprite grew earnings strongly, increasing its market share from an already impressive position. The retailer also announced its intention to exit its loss-making Nigerian operations. Cash flow improved meaningfully as inventory levels were optimised after implementing better IT systems. We trimmed our holding given the strong share price performance and reduced margin of safety. Sanlam is another new position in Top 20, as explained in the commentary by Karl Leinberger, Sarah-Jane Alexander and Adrian Zetler on page 32.

COMMODITIES ATTRACTIVE

In the Market Plus Fund's global equity allocation, we have trimmed the developed market exposure but still maintain a large exposure to emerging markets. The rampant printing of US dollars, a disruptive and divisive election, and general mismanagement of the Covid-19 crisis does not bode well for the strength of the US dollar. After a decade of dollar strength, we expect a significant period of dollar weakness, as the US Federal Reserve Board follows a policy of maintaining negative real interest rates and relaxing its inflation-targeting policy. This bodes well for emerging markets and for commodities. We have therefore increased the weighting to commodities within Market Plus, and own gold, platinum and copper exchange-traded funds.

Gold should continue to benefit from flows related to dollar weakness, whereas platinum and copper stand to benefit from looming deficits as supply has been impacted by better supply discipline and growing industrial demand.

FIXED INCOME EXPOSURE

Fixed income exposure in Market Plus continues to be focused on South African government bonds where yields have remained stubbornly high, despite virtually no yield elsewhere in global markets. Such is the lack of demand for domestic government bonds, even corporate credits are now trading at yields below those of the sovereigns. There is a greater expectation that a South African corporate will repay its debt than the State will.

While disappointment is always a possibility, most South African debt is denominated in rands and not dollars, which means, in our view, a very low probability of an actual default under the current government. Finance Minister Tito Mboweni has made himself very unpopular by pushing back hard against the fiscal profligacy that marked the prior decade under then-President Jacob Zuma and is certainly proposing cost-cutting never before spoken about by an ANC Finance Minister.

With real yields in excess of 6% for longer-dated government bonds, any potential negatives are mostly accounted for and any positive news could create opportunities for meaningful capital gains. Global bonds continue to look incredibly expensive and guarantee the holders negative real returns for the foreseeable future.

Property is a difficult asset class in the current environment. Virtually all properties outside of logistics have been negatively impacted by lockdowns, with retail properties the worst, followed closely by office properties. It is difficult to see exactly how the world returns to normal and what this means for rentals in a market where, undoubtedly, demand for space will have reduced. While prices optically show great value, balance sheet strength is the only game in town, and we are being cautious to ensure that any exposure we have is to those companies with robust balance sheets able to resist significant declines in property values.

TO CONCLUDE

Looking ahead, we are still very excited about the potential return opportunities from the various asset class building blocks. Yields from just holding the existing assets in Market Plus should enable double-digit returns for the foreseeable future, with capital gains potential on top of that. While there is always risk in markets, the return potential is such that we have significantly increased the risk asset exposures in the Fund to take advantage of this mispricing.

The world remains an uncertain and volatile place. This does unearth good opportunities for stock-pickers with long time horizons. We track the upside of the Top 20 portfolio over time. Current upside levels remain high relative to history and suggest that future returns from the Portfolio should be good. ✚

FUND UPDATE

Coronation Strategic Income Fund

By **NISHAN MAHARAJ** and **MAURO LONGANO**

Nishan is head of Fixed Interest and has 17 years of investment experience.

Mauro is Head of Fixed Interest Research and a portfolio manager and has nine years of investment industry experience.

THE CORONATION STRATEGIC Income Fund, our managed income fund aimed at investors with a time horizon between one and three years, returned 1% during the third quarter of the year (Q3-20) and 5.8% over the past six months. Over one year, the Fund returned 3.5%, which is 1.9% behind cash (measured using the STeFI 3-month Index) and over three years it returned 6.6% p.a., which is 0.4% p.a. ahead of cash.

September was filled with central bank meetings, and most policymakers voted to keep policy interest rates unchanged. Asset purchasing programmes were maintained, and the focus at the meetings was on providing market guidance with medium-term policy statements. Inflation pressures should remain subdued until the end of the year, and monetary policy interventions are expected to remain in place for a considerable period.

In the US, the Federal Reserve Board (the Fed) left the target interest rate range unchanged at 0.00% to -0.25%. The Fed forecasts suggest policy rates will remain on hold until at least 2023 while it implements an average inflation strategy, which suggests some tolerance for inflation to overshoot the 2% target. US headline inflation increased to 1.3% year on year (y/y) in August from 1.0% y/y in July. Rising vehicle prices contributed to the inflation uptick. Food prices remained stable and the cost of medical care services declined slightly.

In emerging markets, China's headline inflation slowed to 2.4% y/y in August from 2.7% y/y in July, with food prices driving the decline. Elsewhere, the impact of Covid-19 on growth continues to evolve, with many countries still battling rising infection rates and relatively stringent lockdown restrictions.

The Fund maintains exposure to offshore assets and, when valuations are stretched, will hedge/unhedge portions of its exposure back into rands/dollars by selling/buying JSE-traded currency futures (US dollars, UK pounds and euros). These instruments are used to adjust the Fund's exposure synthetically, allowing it to maintain its core holdings in offshore assets.

GROWTH OUTLOOK

The South African Reserve Bank (SARB) met in September and kept the repo rate unchanged at 3.5%. The vote was split, with three members calling for a hold and two members opting for a 25 basis point cut. The SARB also revised its growth assumptions for the year because of weaker-than-expected second-quarter GDP growth. The central bank is expecting the economy to contract by 8.2% in 2020 from a previous forecast of 7.3%.

The SARB sees inflation risks as 'balanced' and average headline inflation is expected to be 3.3% for 2020. Headline inflation for August was 3.1% y/y versus July's 3.2% y/y. Food inflation, rentals (both actual and owners' equivalent rent) and goods price inflation remain contained in the current weak demand environment. However, administered and regulated prices, as well as pressure from imported goods – notably vehicles – are increasingly an upside risk to future inflation.

GDP contracted by an annualised -51.0% quarter on quarter (q/q) seasonally adjusted average (saa) in Q2-20, following a revised -1.8% q/q saa in the first quarter of 2020 (-2.0% q/q saa previously). The biggest detractor was the contraction in activity in the primary and secondary sectors of the economy, which faced the hardest shutdowns, while trade sectors fared a little better. Mining, manufacturing and construction output fell by more than 70% q/q saa. The services sector saw output fall by 40% q/q saa, with the trade sector down by 67.6% q/q saa and transport down by 67.9% q/q saa.

Financial and business services fell less than other services, down by 28.9% q/q saa. On the expenditure side, household spending was down 49.8% q/q saa. The collapse in personal consumption expenditure far outweighed the decline in compensation, in part owing to mobility restrictions, which should improve in Q3-20.

Gross fixed capital formation contracted by 59.9% q/q saa. Net exports contributed negatively to growth as exports fell by 72.9% q/q saa, while imports fell by 54.2% q/q saa. The Q2-20 shock was, on balance, worse than expected, and it extends the recession to three consecutive quarters. Despite the weak growth outlook, we expect the repo rate of 3.5% to remain unchanged for a sustained period, as the SARB monitors the impact of a cumulative 300bps in easing year to date and while fiscal risk remains elevated.

At the end of August, shorter-dated fixed-rate negotiable certificates of deposit (NCDs) traded at 4.58% (three-year) and 5.76% (five-year), much lower than the previous month. Shorter-dated NCDs have pulled lower due to the significant interest rate cuts, recovery in bond yields and tightening of credit spreads. Short-dated fixed-rate NCDs continue to hold appeal due to the inherent protection offered by their yields. NCDs have the added benefit of being liquid, thus aligning the liquidity profile of the Fund with the needs of its investors. The Fund continues to hold decent exposure to these instruments (less floating than fixed) and we will remain cautious and selective when increasing exposure.

Inflation-linked bonds (ILBs) have performed poorly at index level as the ILB bond curve is weighted heavily towards longer-dated bonds. However, ILBs out to seven years have produced decent returns relative to cash over the past year, offer an attractive pick-up to their nominal bond counterparts, and still provide inherent protection against higher inflation.

Furthermore, the one-year forward real policy rate (the difference between the repo rate and one-year forward inflation) sits at -1%, which acts as a very strong anchor for short-dated real yields. The risk, which we believe to be negligible at this point, is that the SARB moves the real policy rate into a marginally positive area.

CONSERVATIVE ON LISTED CREDIT

The listed credit market was not spared during the Covid-19 selloff. However, the subsequent recovery in listed credit spreads has far exceeded the improvement in the quality of the underlying fundamentals. This market is suffering from a supply/demand imbalance, as primary supply has dried up from most of the bond issuers.

Since the SARB relaxed prudential capital buffers for banks, they can now afford to refinance upcoming debt maturities for corporates without relying on the capital markets. At the same time, the risk/return characteristics of other yielding asset classes have turned less favourable, making listed credit, with its optically lower return volatility, a seemingly attractive opportunity.

Unlike investing in an equity, where one can double or triple one's initial investment, when one invests in a credit, the best one can hope for is to receive one's coupon payments on time and one's capital back at the end. The return profile is therefore discrete; that is, one continues to earn a steady interest rate (coupon) until maturity or default.

Even though underlying fundamentals might be deteriorating, the return of the South African corporate credit market has remained steady, predominantly because individual issues are tightly held by a small number of institutions, hence limiting secondary market activity and price discovery.

This reduced observed volatility hides the underlying risk within the sector, in our view. In addition, structured products can also be used to reduce the observed volatility of returns of the underlying credit exposures due to inefficiencies in the mark-to-market process for these products. We remain conservative in our credit allocations.

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PROPERTY UNDER PRESSURE

The local listed property sector remains under pressure and was the largest detractor from Fund performance over the past year. Share prices are weak as a result of a general rise in balance-sheet risk across the sector. The current crisis reduced rental income, put pressure on asset values, increased the cost of borrowing for lower-quality businesses and tested inexperienced management teams. It is entirely possible that many property companies will require additional capital and that dividends are suspended to preserve capital. While historical yields are attractive, we remain cautious not to take these at face value and understand how the key issues mentioned above may affect prospective yields. We believe there are a few select large-cap counters that satisfy our stringent conditionality.

We remain vigilant of the risks emanating from the dislocations between stretched valuations and the underlying fundamentals of the local economy. However, we believe that the Fund's current positioning correctly reflects appropriate levels of caution. The Fund's yield of 5.3% (net of fees) remains attractive relative to its duration risk. We continue to believe that this yield is an adequate proxy for expected fund performance over the next 12 months.

TO CONCLUDE

As is evident, we remain cautious in our management of the Fund. We continue to invest only in assets and instruments that we believe have the correct risk and term premium to limit investor downside and enhance yield. +

FUND UPDATE

Coronation Global Capital Plus, Global Managed and Global Equity Select funds

By **NEIL PADOA, HUMAIRA SURVE** *and* **LOUIS STASSEN**

Neil is Head of Global Developed Markets and has 12 years of investment experience.

Humaira is a portfolio manager with eight years of investment industry experience.

Louis is a founding member of Coronation and a former CIO.

OUR FUND RANGE with a developed market bias includes Global Equity Select and two multi-asset funds – the long-term, growth-oriented Global Managed Fund and the more conservative Global Capital Plus Fund. As you would expect during a period when markets recovered strongly, the funds performed in line with their risk budgets over the quarter in review, with Global Equity Select, Global Managed and Global Capital Plus producing US dollar returns of 5.7%, 4.6% and 1.7% respectively.

In Global Managed and Global Capital Plus, return contributions were broad-based:

- Equity holdings returned 7.9% in the case of Global Managed and 6.2% in the case of Global Capital Plus, compared to the benchmark's 8.1%.
- Property holdings had strong returns of 10.0% and 11.0%, respectively.
- Fixed interest continued a solid rebound, returning 3.7% and 3.1%, respectively, compared to the bond benchmark of 2.7%.
- Gold holdings returned 6.4%.
- Other commodity holdings returned 6.9% and 7.2%, respectively.

QUARTERLY DETRACTORS

Portfolio hedges were the most significant detractor from performance, which is not surprising, as these positions will clearly be a headwind in strong markets. However, it is not unusual for some form of protection to be in place in our multi-asset funds. If purchased when the cost is low, and scaled appropriately, we feel this is an important tool to manage risk and volatility.

Multinational pharmaceutical Bayer detracted over the quarter. We think the stock is materially undervalued at a seven times price-to-earnings ratio. This is due to continued uncertainty regarding the resolution of the Roundup litigation and regulatory uncertainty around its Xtend platform at a time when end-markets (principally corn due to lower bioethanol demand) are temporarily depressed. Longer term, Bayer remains the leading crop science franchise, with significant opportunity to improve profitability from merger synergies, new products in the pipeline (e.g. short-stature corn) and scaling its digital agriculture initiative. While recent results have been disappointing, the range of potential outcomes remain tilted to the upside.

COVID-19 UNDERSCORES NEED FOR SERVICE EXCELLENCE

US cloud-based company Salesforce was a strong contributor to performance, with the share price climbing 26% in one day following the release of better-than-expected results. Organic revenue >

growth of 19% on a year-over-year basis in a quarter heavily impacted by Covid-19 is an excellent result and highlights the company's strong positioning and demand for its software solutions.

Salesforce is the global leader in customer relationship management software and has also moved into adjacent areas, including the broader digitisation of customer-facing activities, such as marketing, e-commerce, data management and business intelligence. While these trends were strong before Covid-19, social distancing has reinforced the need for businesses to invest in revenue-generating activities, to know their customers better and to be able to reach them online. Salesforce offers the tools to do this.

The company sees a large opportunity ahead and continues to invest aggressively in adding staff during a time where many companies are laying people off. Salesforce is a well-managed, high-quality and fast-growing compounder with strong environmental, social and governance credentials, and we remain bullish on its outlook.

PORTFOLIO POSITIONS

At quarter-end, Global Managed was positioned in 68% growth assets and 32% more stable, diversifying assets with limited correlation to equities. The growth-asset allocation consists of 54% effective equity exposure and smaller positions in listed property, infrastructure, convertible bonds and high-yield corporate bonds. The more stable part of the portfolio consists of Treasury bills, hedged equity, inflation-protected securities, commodities and investment-grade corporate bonds.

The more conservative Global Capital Plus owned 43% in growth assets, including 25% effective equity exposure and 57% more stable and diversifying assets, including 19% in investment-grade corporate bonds, 12% in Treasury bills, 8% each in commodities and hedged equity, and 6% in inflation-protected securities.

TO CONCLUDE

Earlier this year, we felt that there were attractive opportunities for those investors with a long time horizon and the ability to filter companies whose prices had been dislocated with little impact to their sustainable earnings power. After a sharp rally over the past six months, these opportunities are now harder to find. In addition, the need to reassess the prospects of many businesses continues as investors parse fundamental virus-induced behavioural changes from short-term noise. Fundamental changes, however, play to the strengths of fundamental investors, and we continue to find a select number of stocks with solid, long-term prospects that are reasonably priced. +

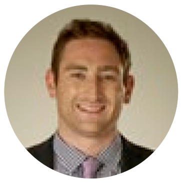
FUND UPDATE

Coronation Optimum Growth and Global Emerging Markets Flexible funds

By GAVIN JOUBERT, SUHAIL SULEMAN, MARC TALPERT and LISA HAAKMAN

Head of Global Emerging Markets, Gavin has 21 years' experience as an investment analyst and portfolio manager.

Suhail is a global emerging markets portfolio manager with 18 years of investment experience.



Marc is a global emerging markets portfolio manager with six years of investment experience.

Lisa is a global emerging markets portfolio manager with 14 years of investment experience.

OPTIMUM GROWTH IS an unconstrained worldwide flexible fund, aiming to meaningfully grow wealth for long-term investors. The Fund appreciated by 3.3% in the third quarter of 2020 (Q3-20), bringing the year-to-date return to 22.5%, which is more than 11% ahead of benchmark. Over the past decade, the Fund returned 16.8% p.a. The Global Emerging Markets (GEM) Flexible Fund aims to give investors access to the best equity opportunities in emerging markets. The Fund returned 5.4% during Q3-20, which is in line with the benchmark. Since inception 13 years ago, it has outperformed the benchmark by 1.9% p.a.

This quarter was less eventful compared to the first six months of the year, which exhibited extreme volatility. The markets remain volatile as the Covid-19 pandemic continues to cause disruption around the world, with various governments responding in different ways, which continues to create a disruptive operating environment for many businesses.

OPTIMUM GROWTH PORTFOLIO POSITION

Optimum Growth is positioned without taking a strong view as to when normalisation will occur across the world, as the last nine months have indicated once again that trying to predict the future is inherently difficult. The Fund holds a collection of businesses that we feel are attractively priced and can operate in what we deem to be a highly complex and fast changing environment. Optimum Growth ended the quarter with 69% net equity exposure, slightly lower than at the end of June. Our negative view on global bonds remained unchanged as a large portion of >

developed market sovereign bonds offer negative yields to maturity, with the follow-on effect that most corporate bonds also offer yields that do not compensate for the risk undertaken. Only 1.4% of the Fund is invested in bonds. The Fund also has c.2.8% invested in global property – largely Vonovia (German residential) and Unibail (European and US retail property). Lastly, the Fund has a physical gold position of 3.9%, along with a 0.7% holding in Barrick Gold Corp, the largest gold miner globally. The physical gold position was added to during the quarter for its diversifying properties. The balance of the Fund is invested in cash, largely offshore. As has been the case for many years, the bulk of the Fund (over 90%) is invested offshore with very little exposure to South Africa.

CONTRIBUTORS TO OUTPERFORMANCE

Optimum Growth's largest positive contributors in the quarter were Alibaba (+30%; 0.7% positive impact), Salesforce (+31%; 0.6% positive impact) and JD.com (+25%; 0.5% positive impact). The Fund incurred unrealised losses on a collection of put-option and short-index positions, which provided valuable protection in the first quarter of this year but detracted from performance this quarter. Collectively, these put options and short-index positions had a 0.9% negative impact during the quarter, but owning them continues to provide the Fund with protection should there be a market selloff. The one other notable negative detractor was Unibail-Rodamco-Westfield (-37%; 0.3% negative impact), which came under renewed pressure post the announcement of a proposed rights issue to deleverage the balance sheet.

NEW BUYS IN THE PERIOD

Notable buys or increases in position sizes during the quarter were NetEase, RELX Plc and Visa.

NetEase is the second-largest gaming company in China, with a long history of successful execution over its more than 20-year history. Netease benefited from the social distancing tailwind and has been very successful in incubating new businesses. NetEase own the second-largest music streaming service in China, which operates in a duopoly with Tencent Music Entertainment. It also owns a rapidly growing online education business (Youdao), which was separately listed late last year, with NetEase still holding c.58%. Both the online music business and the online education business are lossmaking, but should start to contribute both profits and cash flow to the combined group in the next 18 to 24 months. NetEase also has just under 20% of its market capitalisation in cash and trades on a c.6.5% 2021 free cash flow (to enterprise value yield), which we feel is attractive.

RELX is a global provider of information-based analytics and decision tools for professionals and business customers. Its revenue is largely recurring in nature and the company's tools are deeply embedded into its customers' workflows. The company has recognised brands within the scientific, legal and risk analytic markets, and has done a good job over the years to transition its products to the digital realm. Its risk analytic business is made up of a significant proprietary dataset, which is hard to replicate and creates real value for its clients (insurers) who access it to make critical business decisions. Growth should be driven by continued penetration into existing clients and expanding the company's service offerings. The business is highly cash generative as most of its revenue is received in advance, and the bulk of its free cash flow has been returned to shareholders in the past. We estimate the business should be able to grow earnings in the high single digits which, coupled with a c.2.5% dividend yield, should generate double-digit total returns in hard currency.

Visa is a business the Fund has owned for many years due to our positive view on the structural growth driver (the transition from cash to electronic payments) supporting the business fundamentals. Covid-19 has potentially accelerated this transition due to rapid increases in e-commerce penetration and a behavioural shift away from handling cash. There are some headwinds brought about by a curtailment in travel, but we believe this is transitory as opposed to permanent and, ultimately, the move away from cash has been accelerated due to the pandemic. Cashless penetration (as a percentage of personal consumption) globally was just under 50% last year – up nearly 20% from a decade ago. We expect this trend to continue, with penetration approaching 70% over the next decade. This is supportive of growth for Visa, with the business generating very high incremental margins due to low incremental costs in supporting these additional volumes. Against this backdrop, we expect high single-digit revenue growth, which should translate to low double-digit earnings growth.

GEM FLEXIBLE FUND: CONTRIBUTORS TO OUTPERFORMANCE

The largest contributors to the return of the GEM Flexible Fund in Q3-20 were Wuliangye Yibin, JD.com and Yandex.

Having clamped down hard and early – we have heard interesting first-hand accounts of the restrictions placed on daily life in China during their lockdown – China's economy has stabilised and returned toward normality faster than anticipated, and many Chinese shares have benefited from this. This includes Wuliangye Yibin, a Baijiu (local Chinese spirits) producer, which returned 34%, providing 0.9% of alpha and JD.com, up 29% to add 0.7% to alpha.

JD.com can be thought of as the 'Amazon' of China; a large part of what it sells is its own inventory and deliveries use its own fulfilment infrastructure. China was already the country with the highest e-commerce penetration in the world prior to 2020 due to the presence of highly innovative e-commerce retailers that the mediocre pre-existing physical retailers struggled to compete with. The high level of adoption of digital payment methods further enables e-commerce. Despite being already well established in the minds of the consumer, JD.com has benefited tremendously from the demand uplift that accompanied lockdowns.

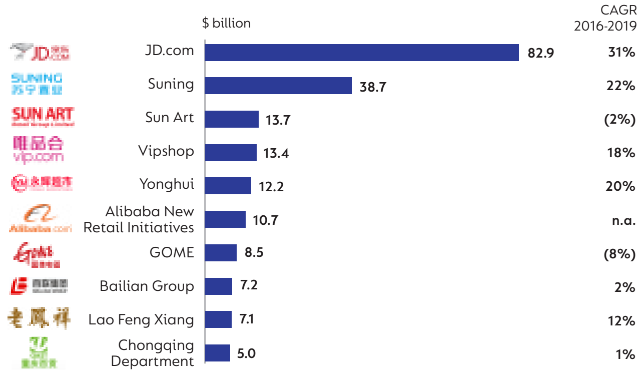
We spoke about the 21% revenue growth in Q1-20 in our last commentary, but Q2-20 results (reported mid-August) were even better, with revenues up 34%, well above consensus of 27%. Even more impressive was the rise in operating profit, up 75% year on year, with margins rising to 2.8% from 2.1% in the same period last year. This led to a 50% increase in earnings per share. All this was driven by a 30% rise in active customers. Most importantly, this operating performance was accompanied by strong free cash flow generation. Unsurprisingly, the share reacted very positively after the results announcement, moving from around $64 to as high as $83.

Like several other US-listed Chinese companies, JD.com did a secondary listing in Hong Kong, raising $4bn and ended the quarter with $18 billion in cash, around 15% of market cap. The secondary listing was part of a wider move by prominent Chinese companies to reduce their exposure to US capital markets over fears the US might unilaterally impose onerous requirements on Chinese companies that they might not be able to meet, as the Chinese government are not fond of foreigners exercising regulatory oversight of Chinese-domiciled businesses. The list of companies that have done this now includes other Fund holdings like Alibaba, NetEase and Yum China. This transfer of trading volume toward Hong Kong is part of the investment case for the Hong Kong Stock Exchange, which is a small position in the Fund (0.5%).

Russian holding, Yandex, increased 30% in Q3-20 and added 0.5% to alpha. Yandex has more than doubled from the low it reached in March and we have trimmed the position to 2.1% of Fund as it has appreciated. The current position size reflects the reasonable valuation and positive long-term outlook for Yandex, which has evolved beyond search to be a meaningful player in many other sectors, such as ridesharing and e-commerce. More recently, Yandex has bid to acquire TCS, Russia's largest digital bank.

Figure 1

NET REVENUE OF MAJOR RETAILERS IN CHINA, 2019



Sources: Goldman Sachs, company reports

QUARTERLY DETRACTORS

The largest detractors from performance during Q3-20 were underweight positions in Taiwan Semiconductor Manufacturing Company (TMSC), the third-largest stock in the index, and Alibaba, as well as holdings in Mexican holding company FEMSA and Naspers/Prosus (the latter was partially offset by not owning Tencent directly).

TSMC was up 43% in the quarter and the underweight cost the Fund 0.7%. We are very positive on the company but feel that a 3% position is more appropriate, given its risk-adjusted expected return and internal rate of return relative to the rest of the investment universe. TSMC reported excellent results for the first half of 2020 (net income up close to 90% versus last year). There have also been continued stumbles by one of its main competitors, Intel, which announced that it is at least a year behind schedule in manufacturing the next generation of 7nm chips. This means that TSMC's competitive positioning is arguably the strongest it has ever been.

FEMSA (2.6% of Fund), fell 8% in the quarter and cost 0.5% of alpha. Mexico continues to struggle in dealing with the coronavirus and most of FEMSA's main assets were negatively affected. The largest contributor to FEMSA, the convenience store chain Oxxo, saw its operations hampered by lockdowns and bans on the sale of alcohol (a large contributor to sales). >

FEMSA's 15% stake in global brewer Heineken was also hurt by the 8% decline in the share price of Heineken. Heineken has been under pressure as they index disproportionately toward premium beers, which tend to be sold on-premise (where margins are higher) rather than in supermarkets (lower margin). With global curbs on socialising, Heineken has seen volumes fall 12% in the first half of 2020.

NEW BUYS IN THE PERIOD

We bought Samsung Electronics, BGF Retail and PagSeguro in our emerging markets funds during Q3-20. Samsung needs no introduction. Developments in the chip and memory industries, which are increasingly consolidated and with returns accruing to the top players disproportionately over time, led us to repurchase it into the Fund. Unlike TSMC, Samsung's share price remains below where it was before the Covid-19-induced market selloff that started in February. Despite a 40% recovery from the lows reached in March, Samsung still trades on less than 12 times forecasted earnings for the 2021 fiscal year with a 3% dividend yield and close to a third of its market cap in cash.

BGF retail is a South Korean convenience retailer and was bought into the Fund for the first time. BGF operate in the convenience value service segment, which is attractive in a country like South Korea where there is very high degree of urbanisation, high population density and small household size. The segment has doubled market share over the last decade to 7%, but this is still below regional peers Taiwan and Japan, with similar demographics. With challenged formats like department stores, hypermarkets and specialty stores still making up over 50% of retail sales in the country, there is reasonable market share up for grabs. BGF trades on 14 times forward earnings, has a net cash balance and consistently generates returns on equity in excess of 20%.

PagSeguro is a Brazilian financial services company catering primarily to small merchants in that country. Small merchants make up the long tail of customers in Brazil and have traditionally been averse to accepting card payments due to the high fees charged by the other acquirers and banks for this facility. PagSeguro already has 5.5 million active merchants using its payment functionality and 3.7 million using its fully digital bank accounts. Like StoneCo, a Fund holding we wrote about in the March quarter, PagSeguro is looking to take market share away from the incumbent acquirers and banks in Brazil as they earn outsized returns for the value they provide to customers. It is estimated that only 30% of micro-merchants currently accept cards. Together with the 1.2% position in StoneCo, which benefits from similar market share gain potential, the Fund now has +/-2% invested in the Brazilian payment providers covering the small- and medium-sized merchant segments.

STOCK POSITIONS EXITED

The GEM Flexible Fund sold South African food retailers Shoprite and Spar during the quarter. These were small positions (combined 0.8%) and we felt the opportunities were better elsewhere, such as the new buys above. The most notable sale was that of 58.com, which we have held in the funds since late 2016 and has been a top 10 stock in the Fund for some time. 58.com was bought out by a private equity firm, which added the founder to the buyout consortium after their initial bid, in order to secure the support of his high voting shares.

We believed the buyout price significantly undervalued the business and was very opportunistic – the share had traded 25% higher than the proposed price as recently as January this year – and we lobbied the board to prevent the founder from exercising his voting rights due to the inherent conflict this represented (as he was both buyer and seller). These actions were not successful and only a nominal increase in the offer price was requested by the board; as a result, we sold the remaining exposure as the share price converged to the new buyout price.

TO CONCLUDE

We are now just over nine months into the Covid-19 pandemic, yet there still remain many unknowns as to the ultimate length, how governments will respond and what permanent consumer behaviours will manifest post the pandemic. However, against this backdrop we feel the portfolios have been built bottom up, while ensuring adequate diversification with limited exposure to potential hard-to-predict future trends. +

Domestic flagship fund range

Coronation offers a range of domestic and international funds to cater for the majority of investor needs. These funds share the common Coronation DNA of a disciplined, long-term focused and valuation-based investment philosophy and our commitment to provide investment excellence.

INVESTOR NEED

	INCOME ONLY	INCOME AND GROWTH		LONG-TERM CAPITAL GROWTH	
FUND	**STRATEGIC INCOME** Cash†	**BALANCED DEFENSIVE** Inflation†	**CAPITAL PLUS** Inflation†	**BALANCED PLUS** Composite benchmark† (equities, bonds and cash)	**TOP 20** FTSE/JSE CAPI†
FUND DESCRIPTION	Conservative asset allocation across the yielding asset classes. Ideal for investors looking for an intelligent alternative to cash or bank deposits over periods from 12 to 36 months.	A lower risk alternative to Capital Plus for investors requiring a growing regular income. The fund holds fewer growth assets and more income assets than Capital Plus and has a risk budget that is in line with the typical income-and-growth portfolio.	Focused on providing a growing regular income. The fund has a higher risk budget than the typical income-and-growth fund, making it ideal for investors in retirement seeking to draw an income from their capital over an extended period of time.	Best investment view across all asset classes. Ideal for pre-retirement savers as it is managed in line with the investment restrictions that apply to pension funds. If you are not saving within a retirement vehicle, consider Market Plus, the unconstrained version of this mandate.	A concentrated portfolio of 15-20 shares selected from the entire JSE, compared to the average equity fund holding 40-60 shares. The fund requires a longer investment time horizon and is an ideal building block for investors who wish to blend their equity exposure across a number of funds. Investors who prefer to own just one equity fund may consider the more broadly diversified Coronation Equity Fund.
INCOME VS GROWTH ASSETS[1] ● INCOME ● GROWTH	96.8% 3.2%	55.6% 44.4%	43.9% 56.1%	24.1% 75.9%	0.1% 99.9%
LAUNCH DATE	Jul 2001	Feb 2007	Jul 2001	Apr 1996	Oct 2000
ANNUAL RETURN[2] (Since launch)	9.9% 7.6%†	8.9% 5.8%†	11.0% 5.7%†	13.6% 12.7%†	16.2% 12.6%†
QUARTILE RANK (Since launch)	1st	1st	1st	1st	1st
ANNUAL RETURN (Last 10 years)	8.1% 6.1%†	8.5% 5.1%†	7.3% 5.1%†	9.2% 10.5%†	9.3% 9.3%†
STANDARD DEVIATION (Last 10 years)	2.1% 0.2%†	5.4% 1.3%†	6.8% 1.3%†	9.1% 8.4%†	13.5% 13.3%†
FUND HIGHLIGHTS	The fund remains the top performing fund in its category since launch in 2001 and outperformed cash by 2.3% over this period.	Outperformed inflation by 3.2% p.a. (after fees) since launch, while producing positive returns over 12 months more than 99% of the time.	The fund remains the top performing fund in its category since launch in 2001 and outperformed inflation by 5.4% p.a. (after fees) over this period.	No. 1 balanced fund in South Africa since launch in 1996, outperforming its average competitor by 1.8% p.a. Outperformed inflation by on average 7.5% p.a. since launch and outperformed the ALSI on average by 1.2% p.a. (since launch).	The fund added 3.6% p.a. to the return of the market. This means that R100 000 invested in Top 20 at launch in October 2000 grew to more than R2.0 million by end-September 2020. The fund is a top quartile performer since launch.

1 *Income versus growth assets as at 30 September 2020. Growth assets defined as equities, listed property and commodities (excluding gold).*

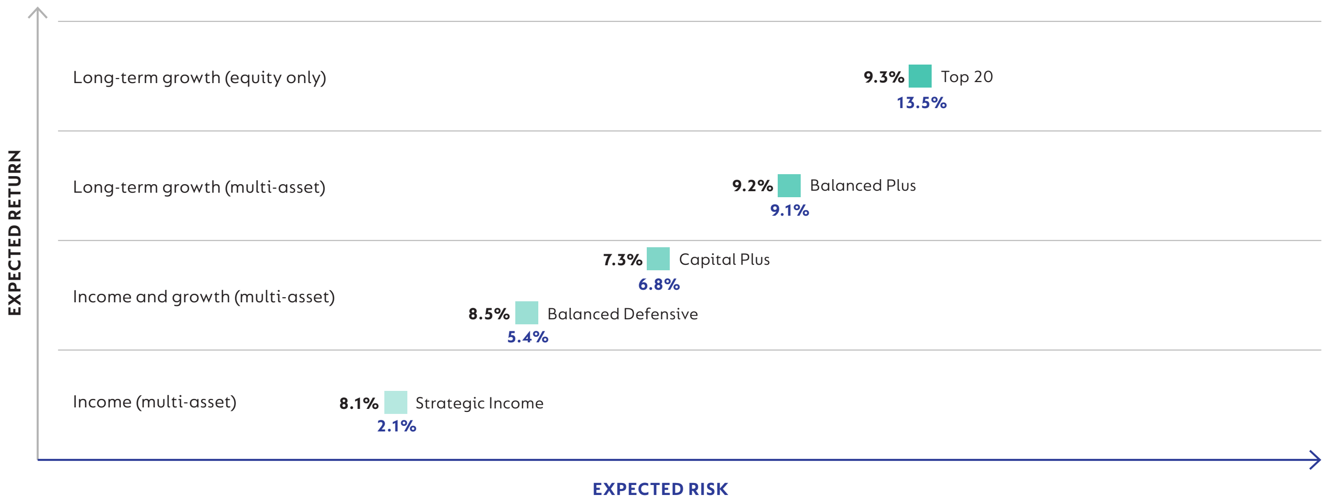
2 *Highest annual return*
Balanced Defensive: 21.2% (Jun 2012 - May 2013); Balanced Plus: 49.3% (Aug 2004 - Jul 2005); Capital Plus: 33.8% (Aug 2004 - Jul 2005); Strategic Income: 18.7% (Nov 2002 - Oct 2003); Top 20: 68.9% (May 2005 - Apr 2006)

Lowest annual return
Balanced Defensive: -5.8% (Apr 2019 - Mar 2020) ; Balanced Plus: -17.4% (Sep 1997 - Aug 1998); Capital Plus: - 9.3% (Apr 2019 - Mar 2020); Strategic Income: 2% (Apr 2019 - Mar 2020); Top 20: -31.7% (May 2002 - Apr 2003)

Figures are quoted from Morningstar as at 30 September 2020 for a lump sum investment and are calculated on a NAV-NAV basis with income distributions reinvested.

RISK VERSUS RETURN

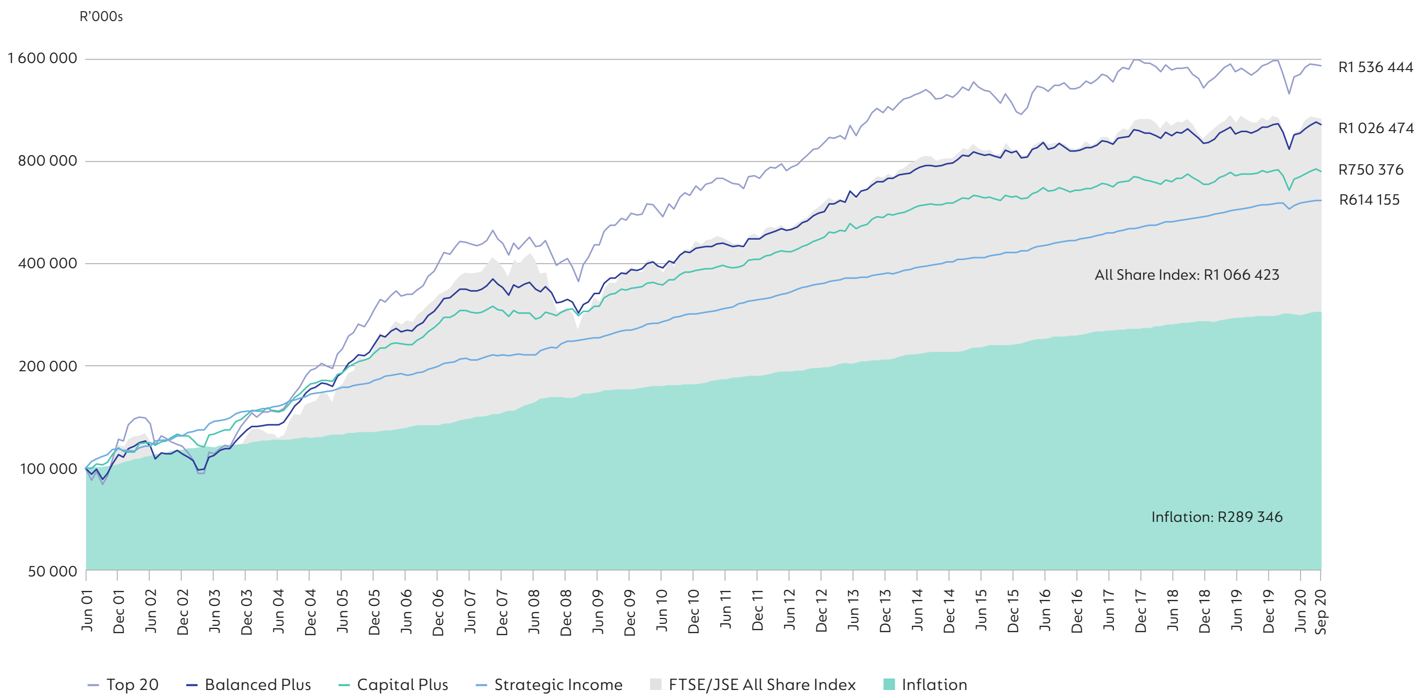
10-year annualised return and risk (standard deviation) quoted as at 30 September 2020.
Figures quoted in ZAR after all income reinvested and all costs deducted.



Source: Morningstar

GROWTH OF R100 000 INVESTED IN OUR DOMESTIC FLAGSHIP FUNDS ON 1 JULY 2001

Value of R100 000 invested in Coronation's domestic flagship funds since inception of Capital Plus on 2 July 2001 as at 30 September 2020. All income reinvested for funds; FTSE/JSE All Share Index is on a total return basis. Balanced Defensive is excluded as it was only launched on 1 February 2007.



Source: Morningstar

International flagship fund range

INVESTOR NEED

	DEPOSIT ALTERNATIVE	CAPITAL PRESERVATION	LONG-TERM CAPITAL GROWTH (MULTI-ASSET)		LONG-TERM CAPITAL GROWTH (EQUITY ONLY)
FUND[1]	**GLOBAL STRATEGIC USD INCOME** US dollar cash (3 Month Libor)†	**GLOBAL CAPITAL PLUS** US dollar cash (3 Month Libor)†	**GLOBAL MANAGED** Composite (equities and bonds)†	**OPTIMUM GROWTH** Composite: 35% JSE CAPI, 15% ALBI, 35% MSCI ACWI, 15% BGBA	**GLOBAL EQUITY SELECT** MSCI All Country World Index
FUND DESCRIPTION	An intelligent alternative to dollar-denominated bank deposits over periods of 12 months or longer.	A low-risk global balanced fund reflecting our best long-term global investment view moderated for investors with smaller risk budgets. We offer both hedged and houseview currency classes of this fund. In the case of the former, the fund aims to preserve capital in the class currency over any 12-month period.	A global balanced fund reflecting our best long-term global investment view for investors seeking to evaluate outcomes in hard currency terms. Will invest in different asset classes and geographies, with a bias towards growth assets in general and equities in particular.	The aim of the fund is to maximise long-term investment growth by investing in a range of opportunities available in public asset markets from both South Africa and around the world. Our intent is to provide competitive after inflation returns measured in rand over all five year periods.	The fund aims to give investors access to the best opportunities in global equity markets. The fund is biased to developed markets and actively seeks out attractively valued shares to maximise long-term growth. Our intent is to outperform the global equity benchmark over all periods of five years and longer.
INCOME VS GROWTH ASSETS[2] ● INCOME ● GROWTH	97.2% 2.8%	65.3% 34.7%	35.1% 64.9%	24.1% 75.9%	0.6% 99.4%
LAUNCH DATE OF OLDEST FUND	Dec 2011	Nov 2008	Oct 2009	Mar 1999	Jan 2015
ANNUAL RETURN[3] (Since launch)	2.3% 1.0%†	4.7% 0.9%†	6.0% 6.9%†	9.6% 6.4%	5.5% 7.9%
QUARTILE RANK (Since launch)	–	1st	1st	1st	1st
ANNUAL RETURN[3] (Last 5 years)	1.7% 1.5%	4.1% 1.5%	6.9% 8.1%	11.0% 5.4%	9.8% 10.3%
ANNUAL RETURN[3] (Last 10 years)	–	2.8% 0.9%	5.5% 6.7%	7.0% 3.6%	- -
QUARTILE RANK (Last 5 years)	–	1st	1st	1st	1st
FUND HIGHLIGHTS	Outperformed US dollar cash by 1.3% p.a. (after fees) since launch in December 2011.	The fund has outperformed US dollar cash by 3.9% p.a. (after fees) since launch in 2008.	No. 1 global multi-asset high equity fund in South Africa since launch in October 2009.	The fund has outperformed the composite benchmark since launch and was a top quartile performer in the Worldwide MA Flexible category since launch in 1999.	The fund outperformed the MSCI All Country World Index by more than 10% during 2019.

1 Funds are available as rand-denominated feeder funds and foreign currency-denominated funds. The Global Capital Plus fund is also available in US dollar Hedged (launched 1 December 2011), GBP Hedged (launched 1 December 2011), EUR Hedged (launched 1 December 2011) or Houseview currency class (launched 1 September 2009).

2 Income versus growth assets as at 30 September 2020 (for US dollar funds). Growth assets defined as equities, listed property and commodities (excluding gold).

3 Returns quoted in US dollar for the oldest fund.

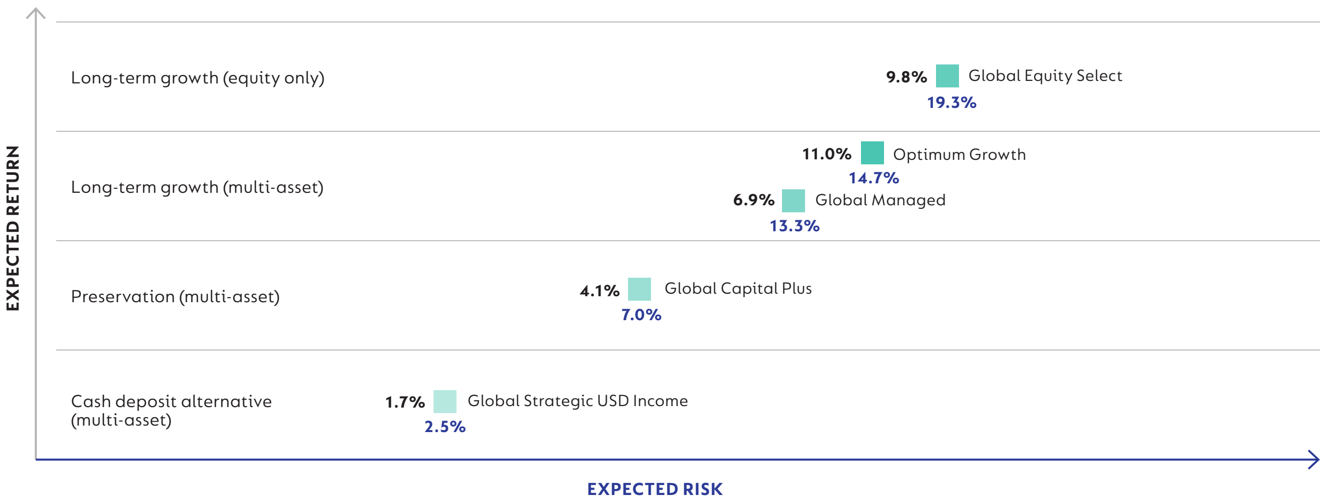
Highest annual return
Global Strategic USD Income: 7.1% (Jan 2012 - Dec 2012); Global Capital Plus [ZAR] Feeder: 31.4% (Mar 2009 - Feb 2010); Global Managed [ZAR] Feeder: 23.1% (Jul 2010 - Jun 2011); Global Equity Select: 37.5% (Jan 2019 - Dec 2019); Optimum Growth [ZAR]: 72.8% (Mar 2009 - Feb 2010)

Lowest annual return
Global Strategic USD Income: -2.0% (Apr 2019 - Mar 2020); Global Capital Plus [ZAR] Feeder: -7.0% (Mar 2015 - Feb 2016); Global Managed [ZAR] Feeder: -14.9% (Mar 2015 - Feb 2016); Global Equity Select: -21.9 % (Mar 2015 - Feb 2016); Optimum Growth [ZAR]: -49.2% (Dec 2007 - Nov 2008)

Figures are quoted from Morningstar as at 30 September 2020 for a lump sum investment and are calculated on a NAV-NAV basis with income distributions reinvested.

RISK VERSUS RETURN

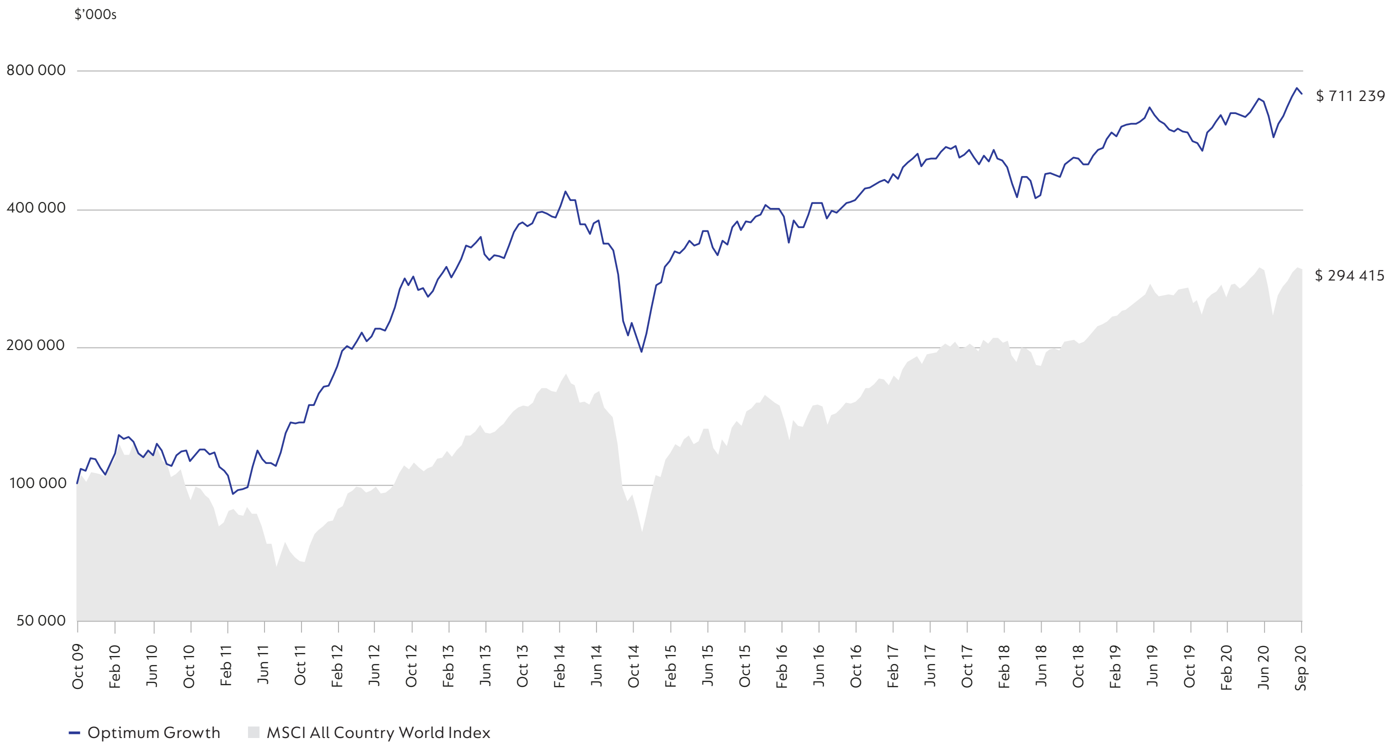
5-year annualised return and risk (standard deviation) quoted as at 30 September 2020. Figures quoted in USD (for the oldest fund) after all income reinvested and all costs deducted.



Source: Morningstar

GROWTH OF $100 000 INVESTED IN OPTIMUM GROWTH FUND SINCE INCEPTION

Value of $100 000 invested in Optimum Growth Fund [ZAR] on 15 March 1999. All income reinvested for funds. MSCI All Country World Index is on a total return basis. All returns converted to USD.



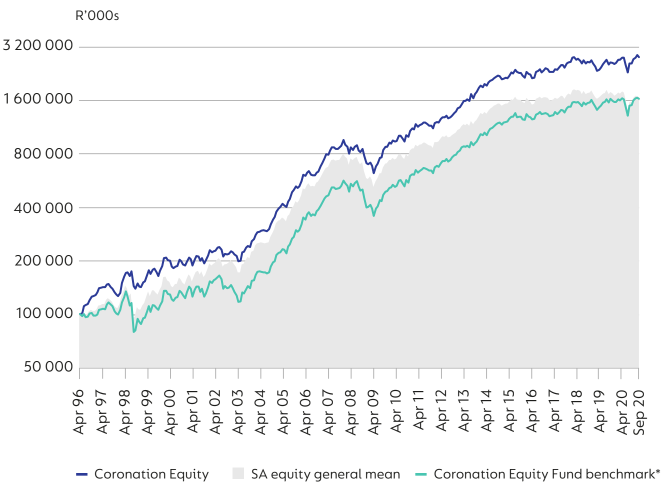
Source: Morningstar

Long-term investment track record

CORONATION EQUITY RETURNS[1] VS AVERAGE COMPETITOR[2]

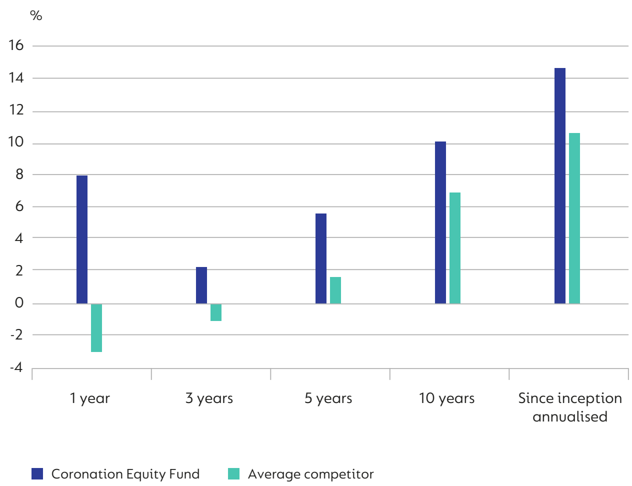
10-YEAR ANNUALISED RETURNS	CORONATION EQUITY	AVERAGE COMPETITOR	OUTPERFORMANCE OF AVERAGE COMPETITOR
2006	19.38%	17.09%	2.30%
2007	21.45%	19.23%	2.22%
2008	17.62%	18.47%	(0.84%)
2009	16.53%	16.68%	(0.15%)
2010	19.59%	19.14%	0.45%
2011	18.03%	16.98%	1.05%
2012	21.12%	18.94%	2.19%
2013	21.60%	18.68%	2.92%
2014	18.44%	16.32%	2.12%
2015	14.86%	12.62%	2.24%
2016	11.95%	9.54%	2.41%
2017	11.99%	8.90%	3.09%
2018	12.77%	10.54%	2.23%
2019	11.35%	8.71%	2.63%
9 Years 9 Months to September 2020	9.38%	6.24%	3.14%
ANNUALISED TO 30 SEPTEMBER 2020	**CORONATION EQUITY**	**AVERAGE COMPETITOR**	**OUTPERFORMANCE**
1 year	7.93%	(3.01%)	10.94%
3 years	2.20%	(1.08%)	3.28%
5 years	5.55%	1.70%	3.86%
10 years	10.08%	6.87%	3.20%
Since inception in April 1996 annualised	14.67%	10.59%	4.08%
Average outperformance per 10-year return			1.87%
Number of 10-year periods outperformed			13.00
Number of 10-year periods underperformed			2.00

CUMULATIVE PERFORMANCE



Source: Morningstar

ANNUALISED RETURNS TO 30 SEPTEMBER 2020



Source: Morningstar

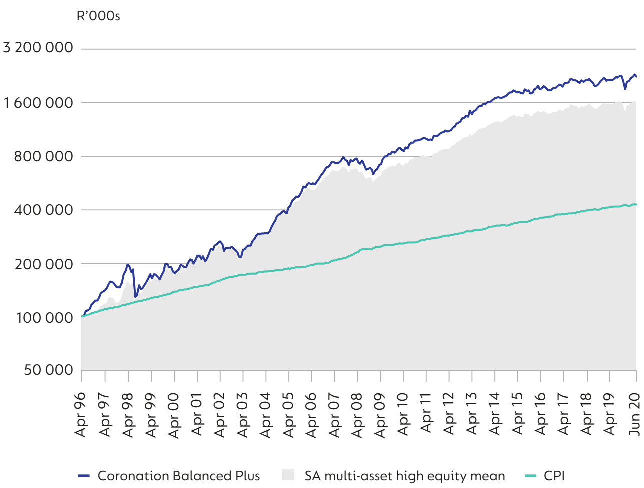
An investment of R100 000 in Coronation Equity on 15 April 1996 would have grown to **R2 827 795** by 30 September 2020. By comparison, the returns generated by the fund's benchmark over the same period would have grown a similar investment to **R1 635 215**, while the South African equity general sector would have grown a similar investment to **R1 675 740**.

[1] Highest annual return 62.5% Aug 2004 - Jul 2005; Lowest annual return (28.7%) Mar 2008 - Feb 2009
[2] Average of performance of the South African - Equity - General category, ex-Coronation Funds

CORONATION BALANCED PLUS FUND VS INFLATION AND AVERAGE COMPETITOR[1]

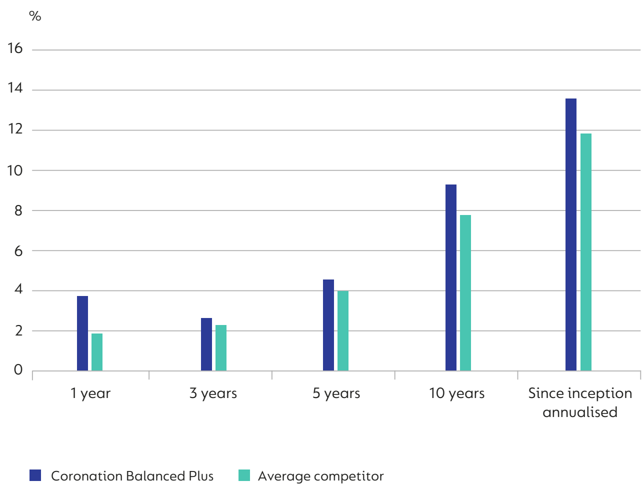
10-YEAR ANNUALISED RETURNS	CORONATION BALANCED PLUS	INFLATION	REAL RETURN
2006	18.33%	6.47%	11.86%
2007	17.81%	6.59%	11.22%
2008	16.96%	6.87%	10.09%
2009	15.69%	6.75%	8.94%
2010	17.20%	6.28%	10.93%
2011	15.78%	6.24%	9.54%
2012	17.85%	5.76%	12.09%
2013	18.63%	5.90%	12.73%
2014	16.58%	6.00%	10.57%
2015	14.01%	6.12%	7.89%
2016	11.08%	6.30%	4.77%
2017	11.04%	5.92%	5.12%
2018	11.26%	5.34%	5.92%
2019	10.30%	5.11%	5.19%
9 Years 9 Months to September 2020	8.94%	5.17%	3.77%
ANNUALISED TO 30 SEPTEMBER 2020	**CORONATION BALANCED PLUS**	**AVERAGE COMPETITOR**	**OUTPERFORMANCE**
1 year	3.72%	1.84%	1.88%
3 years	2.61%	2.26%	0.35%
5 years	4.55%	4.00%	0.55%
10 years	9.22%	7.74%	1.48%
Since inception in April 1996 annualised	13.61%	11.81%	1.80%
Average 10-year real return			8.71%
Number of 10-year periods where the real return is >10%			7.00
Number of 10-year periods where the real return is 5% - 10%			6.00
Number of 10-year periods where the real return is 0% - 5%			2.00

CUMULATIVE PERFORMANCE



Source: Morningstar

ANNUALISED RETURNS TO 30 SEPTEMBER 2020



Source: Morningstar

An investment of R100 000 in Coronation Balanced Plus on 15 April 1996 would have grown to **R2 254 272** by 30 September 2020. By comparison, the South African multi-asset high-equity sector over the same period would have grown a similar investment to **R1 615 877**.

[1] *Median of Peer Group is the median of the fully-discretionary retirement portfolios of the largest managers as published in performance surveys and calculated by Coronation Fund Managers.*