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The Personal Investments Quarterly

Money for nothing?

CORONATION
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IN THIS ISSUE

CORONATION FUND UPDATES AND PERFORMANCE

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Notes from my inbox

"The fact that some choice is good doesn't necessarily mean that more choice is better." – Barry Schwartz in *The Paradox of Choice: Why More is Less*

By **PIETER KOEKEMOER**

Pieter is Head of Personal Investments.

STREAMING SERVICES SUCH as Spotify have been revolutionary for music lovers. For less than R60 a month for the ad-free version, you have access to 70 million songs, or three lifetimes' worth of continuous listening before you need to repeat a song. A further 60 000 tracks are added every day. It offers the pinnacle of instant gratification, personalisation and choice. While you can make your own playlists, most users tend to rely on the curated and personalised playlists available as part of the service. From two weekly mixtapes (one of new releases by artists you like and another with carefully selected songs you have not listened to before) through six daily mixes of old favourites and music new to you, to a wide range of tracks curated by mood, era, genre, artists and other tastemakers, the service is exhaustively comprehensive.

In applying the lessons learnt from the music-streaming revolution to investing, it is easy to draw the wrong conclusions. There are more than 100 million active app-based stockbroking accounts in the US, allowing effortless buying and selling of thousands of securities, including complex leveraged derivatives. The smartphone-based brokerage model optimises the choice and immediacy elements of the streaming experience. Unfortunately, when applied to investment, this approach also incentivises more trading activity and risky short-term performance-chasing. This increases the probability of poorer long-term outcomes through timing-related errors: the likelihood of buying high and selling low is increased when trading is on tap and perceived as free.

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In my view, recent studies have highlighted a more applicable analogy to the world of long-term investment. Faced with overwhelming choice, listeners have become reliant on the playlists built by the recommendation engines. These systems effectively become active agents shaping music tastes and listening habits. Streamers increasingly respond in typical relationship-driven emotional terms to the recommendations received, valuing credibility and trust, and expressing a sense of betrayal if they get the sense that their streaming service's recommendations are optimised for their own commercial interests rather than their customers' personal satisfaction. This is the same expectation that we know you have of your fund manager: that we always remain committed to making decisions that are in your best interests, not ours.

2021 IN REVIEW

Last year was generally a good one for financial markets. As you can see in more detail in the market performance table on page 22, most asset classes did well in absolute terms. The US equity market had another very strong year (S&P500 Index +29% in US dollars, as are all the return data in this paragraph), outperforming the rest of the developed world (MSCI Europe, Australasia and the Far East Index +11%).

The exceptions were global bonds (Bloomberg Barclays Global Aggregate Bond Index -4.7%) and emerging market equities (MSCI Emerging Market Index -2.5%). The South African (SA) market did well too (FTSE/JSE All Share Index +19%) and local government bonds produced the best performance among all major bond markets.

Our multi-asset funds such as Balanced Plus, Capital Plus and Balanced Defensive had a good year, benefiting from good asset allocation and security selection decisions in the domestic equity and bond building blocks. Top 20 had a mediocre year relative to benchmark. While its concentrated nature added significant value over the longer term, it detracted last year as it meant that the Fund was not invested in some of the 'long-tail' holdings that added value in our multi-asset funds.

Our longer-term global funds such as Global Optimum Growth and Global Managed had a poor year, due to positions in China and long-duration growth shares that came under pressure in the second half of the year. We continue to have high conviction in these funds' current holdings and expect relative returns to improve from here. For more detail on specific funds, please refer to the fund commentaries included herein or available on our website.

OUTLOOK

With a rand return of 20% p.a., global equities have performed exceptionally well over the past decade. Over this period, US equity markets have consistently outperformed the rest of the world, increasing the US weight in the MSCI All Country World Index from 45% to 60%. The unfortunate side-effect of this strong performance is elevated starting valuations in the world's biggest equity market, which, coupled with increasing economic and geopolitical headwinds, mean that it is prudent to expect a significant moderation in global equity returns over the next decade.

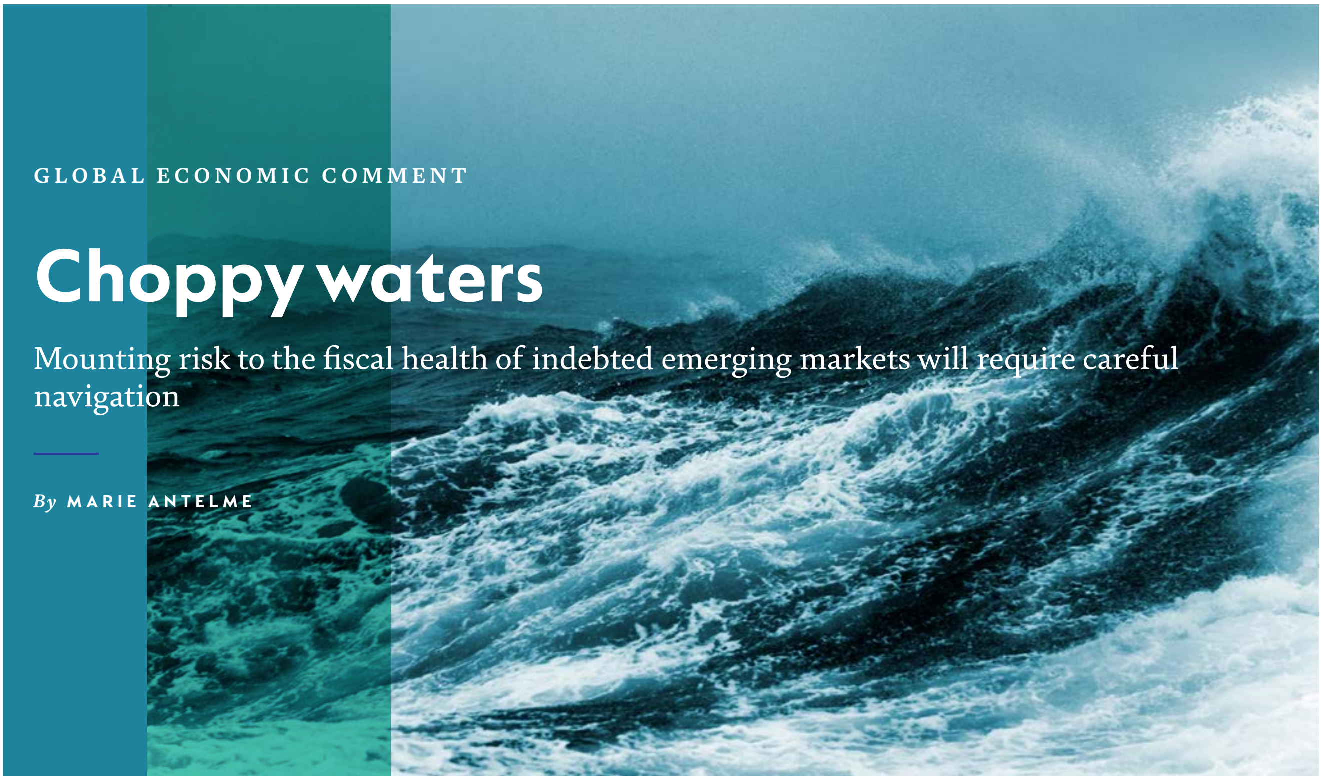
Domestically, we view the situation somewhat differently. While we continue to remain concerned about the structural headwinds facing SA and expect economic growth to remain anaemic for the foreseeable future, a lot of pessimism is reflected in asset prices, even after the strong recovery post the 2020 Covid-19 crisis. Attractive valuation levels mean that it is reasonable to expect returns over the next decade in line with the double-digit rand returns produced over the last 10 years. Local bonds also offer much more attractive starting yields than global bonds.

CHANGES TO *COROSPONDENT*

This will be the last time that our quarterly update will be published in its current magazine form. From next quarter, we will publish content on our website as and when produced. Look out for an updated, more user-friendly publication and investment views section on our website. Our aim is to make it much easier for you to find relevant content when you need it. We will continue to send you the best of each quarter's content in digest form via e-mail, and we remain committed to report back to you in increasingly more comprehensive and useful ways. Thanks to all the regular readers for your ongoing interest – we hope you do not miss the old way of doing things too much.

As always, please do not hesitate to contact us via clientservice@coronation.com if any aspect of our delivery to you failed to meet your expectations.

Pieter



GLOBAL ECONOMIC COMMENT

Choppy waters

Mounting risk to the fiscal health of indebted emerging markets will require careful navigation

By MARIE ANTELME

THE QUICK TAKE

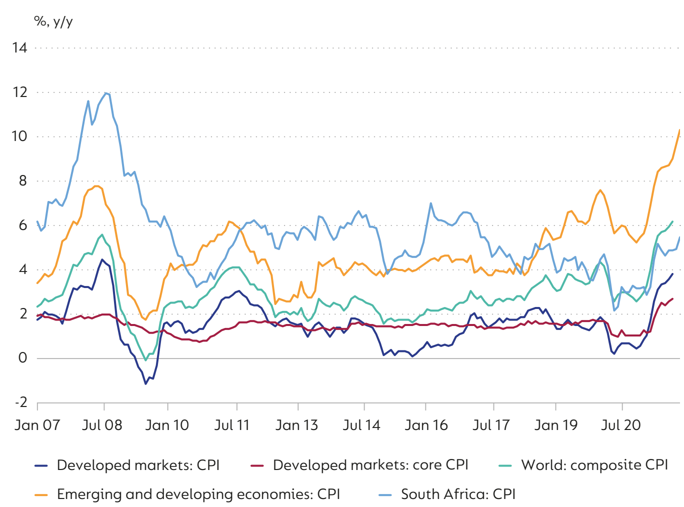
- Policy rate normalisation in a post-pandemic world will require skill to navigate
- Emerging markets in particular are much more indebted than before
- History shows that debt waves and financial crises are empirically linked
- Firm commitments to sustainable fiscal policy are essential to navigating away from the fiscal cliff

Marie is an economist with 21 years' experience as a market economist.

MARKETS AND POLICYMAKERS are – rightly – grappling with the implications of the surge in inflation experienced in 2021. Most recent Federal Reserve Open Market Committee (FOMC) minutes suggest a more hawkish outlook for US interest rates than we have experienced in more than a decade.

Figure 1

GLOBAL CONSUMER INFLATION, % Y/Y



Source: Haver

Globally, central banks are likely to remain reluctant to aggressively tighten policy settings in the short term. This is because they are still unsure of the trajectory of inflation from here and are wary not to derail an equally uncertain recovery, which may mean that persistent price pressures are more likely to see normalisation cycles prolonged and extended in time (Figure 1).

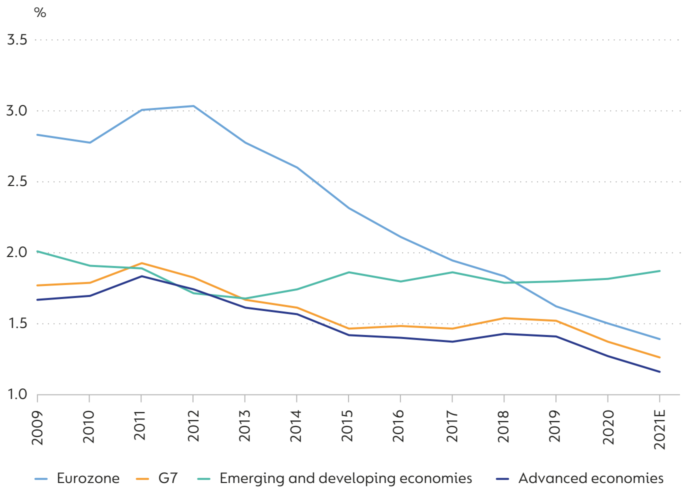
The implications for growth and asset prices are likely to be painful. But the test will be navigating higher interest rates in the significantly more indebted post-pandemic world, especially for emerging markets.

Global debt stock since 2010 has risen at an extraordinary pace, across all economic agents and all regions, to unprecedented peacetime levels. The pandemic-induced recession in 2020 led to the largest single-year surge in global debt since that time. History tells us that more than half of the periods of aggressive debt accumulation since the 1970s have ended in some form of crisis. While the pandemic – and policy responses that were mobilised globally – were exceptional, and worked to mitigate its economic impact, the resulting very high levels of debt materially increase economic fragility. >

For a long time, policymakers have managed to keep the cost of borrowing low, both through very low policy rates and through various unconventional policy tools deployed to meet mandates with policy rates at zero or below. The result has been that governments have been able to fund persistent deficits without debt becoming unsustainable. This is less true for emerging markets where the large accumulation of debt has seen rising debt costs, despite low rates. Nonetheless, we have become comfortable with the idea that advanced (and some emerging) economy governments can continue to spend because central banks will continue to provide costless liquidity. This may no longer be the case (Figure 2).

Figure 2

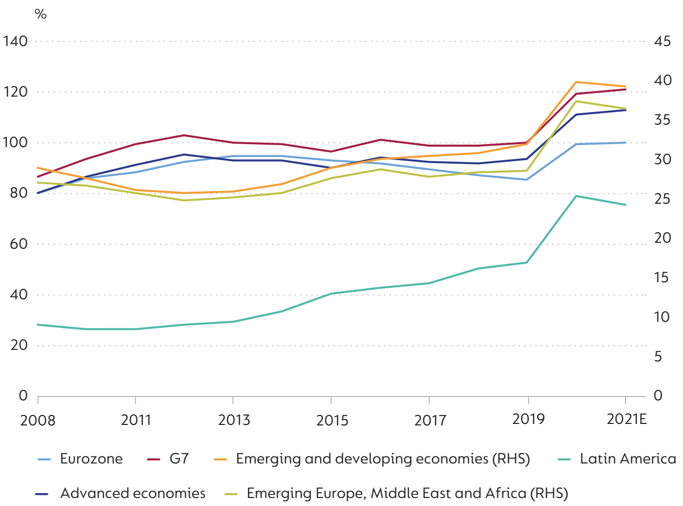
INTEREST PAYMENTS ON GOVERNMENT DEBT, % GDP



Source: UBS

Figure 3

GROSS GOVERNMENT DEBT, % GDP



Source: UBS

DEBT CYCLES ARE COMMON

The World Bank has identified 519 periods of debt accumulation since the 1970s, mostly in emerging markets. The detailed 'Global Waves of Debt' study[1] finds that, within these, there have been four distinct debt cycles in the past 50 years; the fourth and latest has been accumulating since 2010. Previous debt waves have generally been concentrated in specific regions (1970-1989, in Latin America, the Caribbean and parts of sub-Saharan Africa; 1990-2001, in East Asia and the Pacific; 2002-2009, in Europe and Central Asia). In contrast, the latest debt cycle shows rising debt stock – both private and public – across all emerging and developing economies (EMDEs). This is the biggest, fastest and broadest wave of debt accumulation, even before the pandemic (Figure 3).

All waves share several common features. Importantly, they all began during periods of prolonged low interest rates and were facilitated by changes in financial market conditions, whether in practice or prompted by regulatory changes that promoted an acceleration in borrowing. All three previous waves also ended in financial crises of some kind and in all cases the crisis was prompted by a shock that resulted in a sharp increase in borrowing costs.

EMPIRICAL LINKS BETWEEN DEBT ACCUMULATION AND CRISES

High levels of debt carry significant risks. First, debt is much harder to refinance during periods of financial stress, as borrowing costs rise. Secondly, high levels of debt carry broader and far-reaching economic risks. In the case of government debt, rising borrowing costs can crowd out more productive private sector investment, undermining long-term growth. As servicing costs increase, fiscal resources are redirected from other areas of spending, and service delivery and infrastructure investment fail, also undermining growth and adding to longer-term liabilities. As this continues, the cycle becomes unsustainable.

When large amounts of public debt are held by foreigners, a weaker fiscal position may prompt selling, in turn raising the risk of materially higher inflation. Domestically, an increase in government debt held by local financial institutions could see rising systemic risk as asset quality deteriorates.

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[1] The World Bank, Kose, Nagle, Ohnsorge and Sugawara, "Global Waves of Debt, Causes and Consequences", 2019.

WHAT THE GLOBAL FINANCIAL CRISIS DID – LOW RATES AND INFLATION

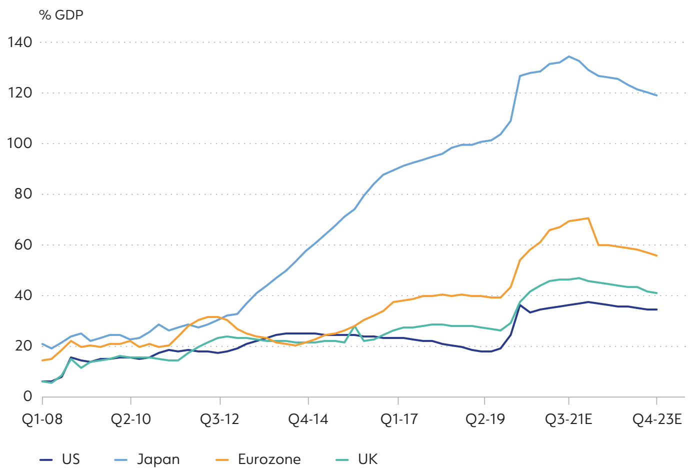
Sharply lower interest rates and low inflation have been dominant features of financial markets over the past decade. These have underpinned low borrowing costs and rising asset prices across classes and maturities. The sustained drop has also raised conjecture that ultra-low rates create room for governments to spend much more than deemed prudent to stimulate growth, while not being overly concerned about taking offsetting steps to lower debt levels.

An important ingredient in this was the utilisation of unconventional policy tools by advanced economy central banks – specifically the Federal Reserve Board (the Fed) and the European Central Bank (ECB) – in a manner that was more effective and less risky than many initially feared. Specifically, the management of long-term interest rates through the expansion of central bank balance sheets to encourage borrowing and help raise inflation towards targeted levels did not lead to runaway inflation or financial instability.

As a knock-on, a global search for yield during periods when risk was perceived to retreat helped lower the borrowing costs for many emerging markets too. Since 2010, EMDE total public and private debt has risen on average almost seven percentage points (ppts) of GDP per annum. While much of this is accounted for by rising debt in China, given its sheer size, as well as aggressive leveraging in 2009-2010 and 2012-2016, debt has risen in 80% of EMDEs over this period, and by at least 20ppts of GDP in more than a third of these.

Figure 4

DEVELOPED MARKET CENTRAL BANK ASSETS, INCLUDING ROLLOVER FORECASTS



Source: UBS

WHAT COVID-19 DID – LOW RATES, RISING INFLATION

The impact of Covid-19 has been to materially accelerate these dynamics. Governments deployed an estimated 4% of global GDP in fiscal support in 2020 and withdrew only about 0.3% in 2021. Significant market disruption provided the space and need for interventions by central banks to support dysfunctional markets. Where possible, they slashed policy rates, and where not, materially extended asset purchase programmes. For the first time, a broader base of emerging markets also utilised unconventional monetary policies, and asset purchases were more common in 2020 and into 2021 in these markets too.

In 2020, global gross government debt registered its fastest-ever single-year increase since 1970, to the highest level since the end of World War II. Total debt was 300% of GDP, while government debt accounted for almost a third, at 97% of GDP. In advanced economies, government debt stood at 120% of GDP, and in emerging markets at 63% – the highest since 1987. The period following the Global Financial Crisis saw fiscal policy take low rates as a baseline and a signal to accumulate debt was amplified by the growth shock.

However, 2021 brought new challenges. The massive supply shock was followed by a low rate, fiscal stimulus-induced demand shock, which has led to a significant surge in inflation. *Ex-ante*, it is very hard for policymakers to know which shocks are transitory and which are permanent, and uncertainty about the drivers of inflation initially saw policymakers dismissive of the risks.

The December minutes of the FOMC meeting clearly articulate a change in sentiment. The Fed will wind down its asset purchase programme by the end of March and will raise interest rates shortly thereafter. A new signal that it plans to start shrinking its balance sheet suggests that the 'costless' stimulus of more than a decade is ending (Figure 4).

EXCEPTIONALISM

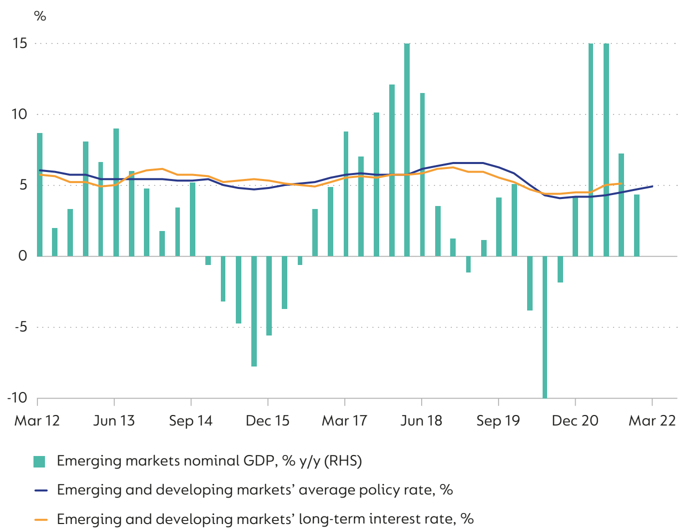
The long period of low interest rates, especially relative to growth, allowed developed economies to sustain high, but relatively stable, levels of debt to GDP, despite the jump in 2020. Importantly, the relatively robust developed market post-pandemic recovery, with strong demand and relatively healthy private balance sheets, has already improved recovery debt ratios. These countries will face their own refinancing challenges as policy >

rates rise, and much will depend on clear communication of policy direction. In some cases, relatively short average term to maturity (US) may see debt reprice fast. In others, unfunded contingent liabilities are a hidden risk, despite a longer-term maturity profile (UK). Importantly, questions of fiscal or financial dominance – about how far and how fast monetary policy will be able to normalise in the face of a growing long-term inflation threat under such a debt overhang – remain unanswered.

The problem is that advanced economy debt calculus does not transfer well to EMDEs. Despite globally low interest rates and relatively strong GDP growth (debt-positive r-g dynamics), rising primary expenditures have led to higher debt in EMDEs over the past decade, with a jump in 2020-2021. Also, while growth was relatively strong in emerging markets, it was slower and disappointing even before the pandemic. We don't really know what the lasting cost of the pandemic will be on emerging market growth, in part because global policy support remains in place. As this is rolled back, the scarring will be clearer, but early indicators are that longer-term growth will be lower, just as interest rates start to rise. So EMDEs face the triple challenge of low growth, rising interest rates and large, persistent deficits against a large existing stock of debt (Figure 5). *In many, this is likely to become quickly unsustainable and global incidence of emerging market debt traps is likely to increase.*

Figure 5

EMERGING AND DEVELOPING MARKETS' INTEREST RATES AND GROWTH INTERACTION INCREASINGLY UNFAVOURABLE FOR DEBT DYNAMICS



Sources: Haver, IMF

WHAT DOES THIS MEAN FOR SOUTH AFRICA?

South Africa (SA) has trod the same debt accumulation path as the rest of its emerging market peers, perhaps even more enthusiastically than some, over the past decade. Government debt has risen from a nadir of 23.1% of GDP in the third quarter of 2008 to an estimated peak of 71.2% in the second quarter of 2020. In the depth of the pandemic, estimates for the debt trajectory varied wildly, but all saw an ongoing sharp increase in the debt stock in coming years as low growth, high borrowing costs and large primary spending continue to accumulate.

Luckily, this has not been the way things turned out. Stronger-than-expected growth and a large revenue windfall – mostly related to commodity-related revenues – materially improved the realised deficit and saw a boost to nominal growth, even as interest costs remain stubbornly high. We expect debt stock at the end of the fiscal year 2021/22 to be 70.1% of GDP, from 70.7% in 2020/21.

While starting positions do count in fiscal arithmetic, the dynamics between interest rates and growth matter too. SA's nominal average funding rate remains high at 6.8%, despite low global yields, and nominal growth has been slowing. Our fiscal baseline sees a moderation in the primary deficit towards a surplus by 2025/26. Assuming this holds, SA will still need to impose a fiscal adjustment of about 2% of GDP to stabilise debt in the short term and a consistent 0.5% to 1% thereafter – a painful adjustment from the current position needed over a long period of time. The alternative is the growing risk of a debt trap, an unsustainable situation where the country is unable to service debt without 'exceptional financing assistance, or default', as broadly defined by the IMF.

SA also has large contingent liabilities, which cannot be ignored. Eskom is the most immediate risk, with government-guaranteed debt of c.5% of GDP. The debt solution needed urgently to ensure that the State-owned electricity provider can legally separate into viable entities will probably add to the sovereign's debt stock. Should government take this debt onto its balance sheet, average financing costs may rise from 6.8% to well above 7%, and debt will accumulate at a faster rate. Perhaps more importantly though, the burden of debt service costs will rise quickly, from 4.4% of GDP to above 5%, with upside risk. This would become SA's structural headline deficit and implies ongoing large funding needs.

GOOD MEDICINE NEVER TASTES GOOD, BUT BAD IS MUCH, MUCH WORSE

A recent paper by the World Bank Group[2] examines methods by which countries have, or may in future, deal with extreme debt distress. Orthodox measures include deficit reduction through consolidation (both spending and taxes) and the privatisation of an array of national assets. Growth should play an important role here, but in practice growth seldom flourishes during times of fiscal austerity.

In SA's case, however, efforts made to consolidate spending have been undermined by weak growth, and, more recently, a larger-than-hoped wage agreement in 2021/22, and by large and ongoing additional, costly, support for State-owned enterprises (SOEs). It is not clear that less spending on operational and investment budgets has undermined growth, although it seems likely that fiscal slippage and institutional decay associated with this strategy have undermined confidence and investment. As yet, any meaningful privatisation is an unlikely strategy, although a shift in thinking in this regard would be welcome.

Heterodox strategies include high inflation, which represents a painful tax on the poor, financial repression, and restructuring or default.

BREATHING ROOM?

The prospect of higher US yields creates a potentially challenging environment for indebted emerging markets. This will be exacerbated as global growth slows, especially from China as it battles to contain Omicron, with knock-on to supply constraints, commodity demand and an uncertain US Fed policy response. In EMDEs where growth has been reasonably good, large primary government spending has kept debt rising relative to GDP. Many EMDEs also have large financing needs in coming years, which amplify this risk. We should expect the incidence of debt distress – especially in emerging markets – to increase from here.

Worryingly, SA also faces many of these challenges. Growth has been weak for a long time, and the lingering effects of the pandemic, especially on employment, incomes and poverty levels will be felt for a long time, especially in the absence of a more aggressive contribution to growth from investment. We are concerned about the ability of the National Treasury to achieve its stated consolidation objective of a primary surplus by 2023/24, as the social cost of the pandemic is likely to remain high, and claims on revenue for transfers to households, wages, for debt service and persistently to SOEs (with more to come) remain politically challenging, even with the best intentions.

More encouragingly, revenue performance has been better than expected, and some capacity renewal at the South African Revenue Service suggests this may continue. It is unclear whether the political revelations of the Zondo Commission can assist in prompting political renewal and improving general levels of confidence; much will depend on the prosecutorial pipeline.

LOOKING AHEAD

Despite what feels like a mountain of risk, we still think that there are several important mitigating factors that should help SA navigate this uncertain territory, for now.

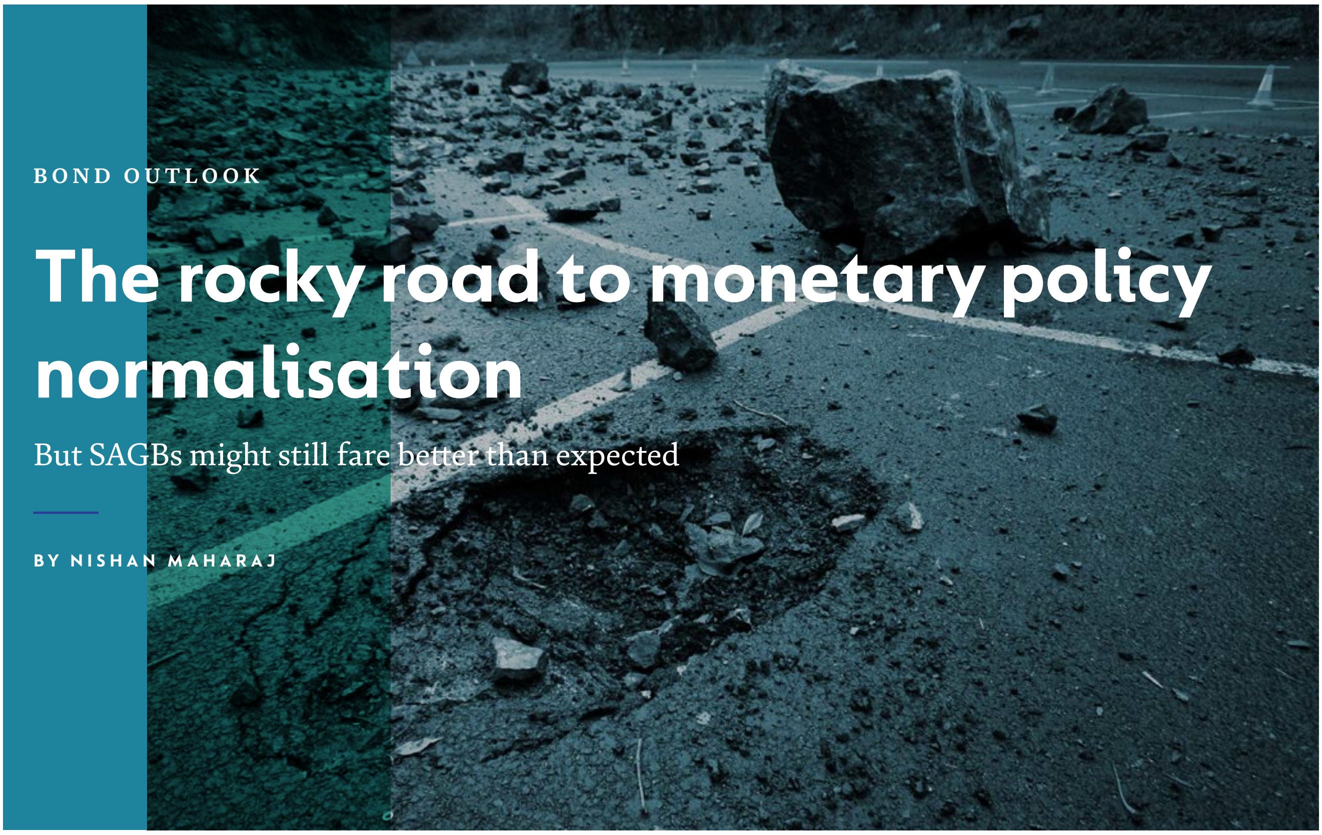
Globally, we think central bank policy normalisation will start in a slow, cautious and well-communicated manner. Both the Fed and the ECB have wider mandates than just the inflation target, and there will probably be some caution about derailing large fiscal packages aimed at supporting a growth recovery. This may change as longer-term inflation outcomes become clearer.

SA should be cushioned by its strong external position on the back of high commodity prices, with a current account surplus of 3.6% in the third quarter of 2021, and positive trade data in the fourth quarter. Further, foreign positioning is considerably lower than in the past, which should limit the risk of aggressive foreign selling – both to the currency and to yields.

Low inflation should underpin both the rate at which policy rates normalise and the risk priced into the longer end of the yield curve. The very steep yield curve, which we believe embeds considerable risk premium, is already a reflection of these risks. A more creative issuance strategy by the Treasury may also alleviate some long-term yield pressures. The IMF has warned that governments in precarious fiscal positions need to maintain a strong commitment to sustainable, well-communicated fiscal strategies in the uncertain wake of the pandemic to avoid crises.

SA will also need to clearly articulate additional spending, critically conclude an affordable wage settlement and actively pursue long-promised growth strategies to successfully weather the storm. ✚

[2] World Bank Group, Policy Research Working Papers, Kose, Ohnsorge, Reinhard and Rogoff, "The Aftermath of Debt Surges", September 2021.



BOND OUTLOOK

The rocky road to monetary policy normalisation

But SAGBs might still fare better than expected

BY NISHAN MAHARAJ

THE QUICK TAKE

- SA is on the brink of a debt trap
- Government needs to do much more, with much less
- SA government bond pricing encapsulates a significant risk premium
- All eyes are on US inflation and how sticky it pans out to be

Nishan is Head of Fixed Interest and has 19 years of investment experience.

IN 2020, THE world was ravaged by the Covid-19 outbreak. The devastation inflicted on people, families and countries was extraordinary, leading to what was the first 'lost year' in the history of modern civilization. 2021 was meant to be the year in which we picked up the pieces and returned to some version of pre-Covid-19 normality. Instead, we were faced with multiple waves of infections and new strains of the virus that seemed set to make this period of abnormality our new way of life. The Omicron variant, which was discovered in November 2021 in Botswana, threatened to put the world into another tailspin, due to the variant's higher transmissibility. However, initial studies suggest that its virulence is much lower, providing some hope that this might finally mark the beginning of the end of the pandemic.

South African assets have had a roller coaster of a year. South African government bonds (SAGBs) traded in a 130-basis point (bp) range and, despite ending the year just above the midpoint of the trading range, still managed to outperform most emerging and developed bond markets. The FTSE/JSE All Bond Index (ALBI) was up 8.4% in local currency, but the depreciation of the rand over the year eroded most of the return. This still puts its return at -0.18% in US dollars, which is better than the FTSE World Government Bond Index at -6.97% and the JPMorgan Emerging Market Bond Index at -1.51%.

The ALBI's return far exceeded cash at 3.55% and was driven by the outperformance of bonds with a maturity of greater than 12 years that produced a return of 12.56%. This flattening of the yield curve was in large part due to the front end of the yield curve (less than seven years' maturity) widening relative to longer maturities. Inflation-linked bonds (ILBs), which carry a significantly higher duration than nominal bonds, saw real yields compress by almost 100bps, which helped them produce a bumper return of 15.45%. However, over three years their return (7.26%) remains below that of nominal bonds (9.11%).

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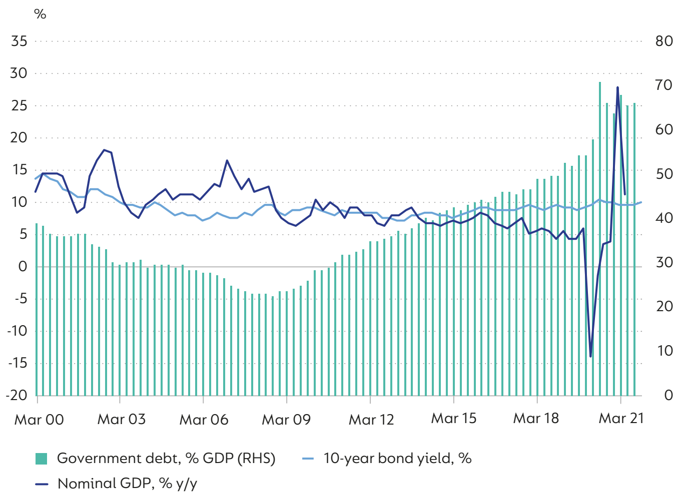
RISKS ABOUND

The local fundamental picture remains relatively unchanged going into 2022, but high levels of unemployment and poverty mean that risks remain elevated. Fiscally, although the country remains on a better footing, deficits are still wide, and the debt load is unsustainable. SA's saving grace is that inflation remains under control and interest rates should remain well below historic norms, providing some support to the economy. The debt trap continues to loom and the math behind it is quite simple: SA needs to fund itself at a nominal rate that is below the nominal growth rate of the economy. Since SA does not lower its funding rate through quantitative easing like many other emerging and developed markets do, the fiscal risk premium embedded in SA bond yields will remain so for some time until investors are confident that government finances have turned around, leaving the onus on nominal growth to save us from financial obscurity. SA's effective funding rate should sit between 7% and 7.5% over the next three to five years and, with expected GDP inflation of 5% to 5.5%, it implies a required minimum real GDP growth rate of 2% to 2.5%, just to stand still. This might not sound demanding but, considering SA has only grown at 1% per annum pre-Covid, reforms and the pace thereof are key to achieving that level of growth, so that the country can avoid a debt trap over the longer term.

Figure 1

SA: NOMINAL INTEREST, GDP AND DEBT



Sources: Bloomberg, Coronation

In Figure 1, one can clearly see how the decline in the nominal growth rate relative to the 10-year SAGB has led to an increase in the debt load. While some of this can be attributed to the growth/funding gap, the last 10 years of the Zuma administration also took their toll, with a significant uptick in unproductive expenditure. The risks to the fiscus for 2022 loom large as government is under pressure to introduce an income grant to offset staggering unemployment levels, while also having to provide support to ailing State-owned enterprises and municipalities. On paper, government seems set to hold the line but, as we have become quite accustomed to in SA, the gap between intention and implementation can be quite stark.

Figure 2

SA SOVEREIGN SPREAD VERSUS BB INDEX SPREAD

Sources: Bloomberg, Coronation

The local fundamental picture and the associated risks are quite well flagged, but for bond portfolios, what matters most is whether the current embedded risk premium in SAGBs contains a sufficient margin of safety. SA bond yields are driven by the global risk-free rate (the US 10-year Treasury Bill [T-Bill] rate), the inflation risk premium (SA inflation versus US inflation) and the sovereign risk premium (the SA sovereign bond spread over that of the US 10-year spread). Currently, we assume a normalised value of 3% for the US 10-year T-Bill and 2.5% inflation for the US economy.

SA inflation is expected to average 5% over the next few years and the current SA sovereign spread is 3.34%. I discuss our assumption about the global risk-free rate and US inflation further on, but for now, I want to discuss the pricing of SA's sovereign risk premium, which is pretty much in line with similar-rated countries in the emerging market universe (Figure 2). However, SA has traded significantly wider over time. In the last two years, the SA risk premium has been around 50bps wider than those of traditionally BB-rated peers.

This might seem conservative given the current fiscal trajectory, but we believe it is appropriate considering the risks on the horizon. Using a >

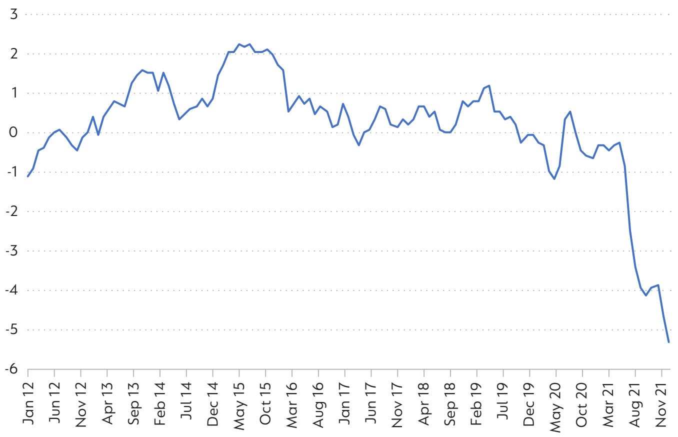
revised sovereign risk premium of 3.84%, the expected fair value for the 10-year SAGB is 9.34%, calculated as follows: (3% [US 10-year T-Bill] + 5% [SA expected inflation] - 2.5% [US expected inflation] + 3.84% [SA sovereign spread]). Even with these more conservative assumptions, the SAGB fair value is considerably lower than the current SAGB 10-year yield of 9.8%. This suggests, from a local perspective at least, that SAGBs still encapsulate a significant risk premium even if fiscal conditions deteriorate further.

INFLATION IS A KEY FACTOR

Global conditions, and more specifically global monetary policy, have been a large driver of the emerging market bond appetite and its bond yields. US inflation is expected to touch 7% at the end of 2021, before starting its gradual retreat towards 2.5% over the next year. The risk is that US inflation remains higher for longer, prompting a more aggressive monetary policy response from the Federal Reserve Board (the Fed) that sends bond yields soaring and sinks risk appetite. Current market pricing puts US inflation expectations at a 3.5% average for 2022 and 3% average for 2023, with the Fed fund rates expected to increase to 1.75% by end-2023. The US 10-year T-Bill currently trades at 1.75%, while the expectations for five-year rates in five years' time sit at 2%. Pre-pandemic, the US 10-year T-Bill generally traded 0.5% to 1% above US inflation (Figure 3), which is in line with US real policy rates of 0.5% to 1%. This would imply that US 10-year rates are too low and need to trade somewhere in the range of 3.5% to 4.5% if the current expectations for inflation are correct.

Figure 3

US 10-YEAR MINUS US CPI



Sources: Bloomberg, Coronation

There are, however, two caveats. First, the US debt load is 50% larger than it was pre-pandemic, which suggests that real rates might now need to be in the region of 0% to 0.5% to keep growth buoyant and debt levels contained. Secondly, current high levels of inflation are being driven by supply chain bottlenecks, which are leading to low supplies and higher prices for consumer electronics, appliances and many other products. In addition, there has been a spike in travel-related expenses after they collapsed in 2020. These bottlenecks are starting to ease and travel expenses will normalise, which suggest these items might prove to be less of a contributor to inflation in 2022. The Fed has acknowledged that current inflation trends are proving sticky, and in the most recent Federal Open Market Committee meeting, it doubled the tapering of asset purchases and alluded to bringing forward the interest rate hiking cycle. Moving rates from 0% to 1.75% might not seem a lot, but it does mean that one's cost of financing goes up substantially, which dampens consumer spending.

Bringing this together, US inflation will indeed be higher than we have experienced, but most likely in the 2.5% to 3% range, and real rates are going to be lower, in the 0% to 0.5% range, which implies a fair US 10-year rate of 2.5% to 3.5%. If this repricing occurs in a very short period, emerging market bond markets will take quite a bit of strain, but if it happens gradually, it might be a supportive environment for risk and emerging markets.

SAGBs will feel the repercussions of the inflation debate through two key areas; first, as the global risk-free rate rises and secondly, through the inflation differential between SA and the rest of the world. Half of the basket in SA is made up of food (17%), rent (12%), transport (15%) and insurance (10%). Food prices are already peaking and bumper crops should help keep food inflation contained. Rental inflation collapsed during 2020 and although it has started its slow climb back up, it is unlikely to progress much past 4% over the next two to three years. Healthy competition and new entrants into the insurance sector should help to keep a lid on premiums, while transport remains the only wild card as SA is a net importer of oil and, hence, at the mercy of global oil prices. SA has a very orthodox and credible central bank that wants to keep inflation at the midpoint of the band, and it is expected that the inflation targeting band will be revised lower at an upcoming macro review. This lends support to an SA inflation outcome that is around 5%.

Higher-than-expected inflation outcomes in the rest of the world would mean that the inflation differential will offset any commensurate rise in the global risk-free rate (SAGB fair value = global risk-free rate + SA inflation – global inflation + SA sovereign spread). That is, if there is an increase in the global risk-free rate because of higher global inflation, the inflation differential will narrow, since SA inflation is not as correlated to the same factors that would be driving global inflation.

The outcome for SAGBs is therefore not as severe as history might suggest and, given the high risk premium already encapsulated in SAGB yields, it is possible that SAGBs fare better than expected over this turbulent period of global and local monetary policy normalisation.

ILBs had quite a recovery in 2021 but started from a much weaker position than nominal bonds. Nonetheless, there remains selective value across the ILB curve. Real yields are elevated across the curve, with implied breakeven inflation significantly lower than current expectations for local inflation in some areas. Despite the 4% real yields at the longer end of the ILB curve, these bonds carry a significantly higher duration (almost 2.5 times their nominal equivalent), with implied breakeven inflation of well above 6%. We continue to believe that there is better value in the nominal bond curve for bonds with a maturity of greater than 12 years, given the steepness of the nominal curve, longer duration and higher implied real yields. However, given the high real yields in the four- to nine-year area and low breakeven inflation, we view this as an attractive investment opportunity and relatively better value than the nominal bond curve in the same area – especially since one is effectively getting the inflation protection for free. This is illustrated in Figure 4.

Figure 4

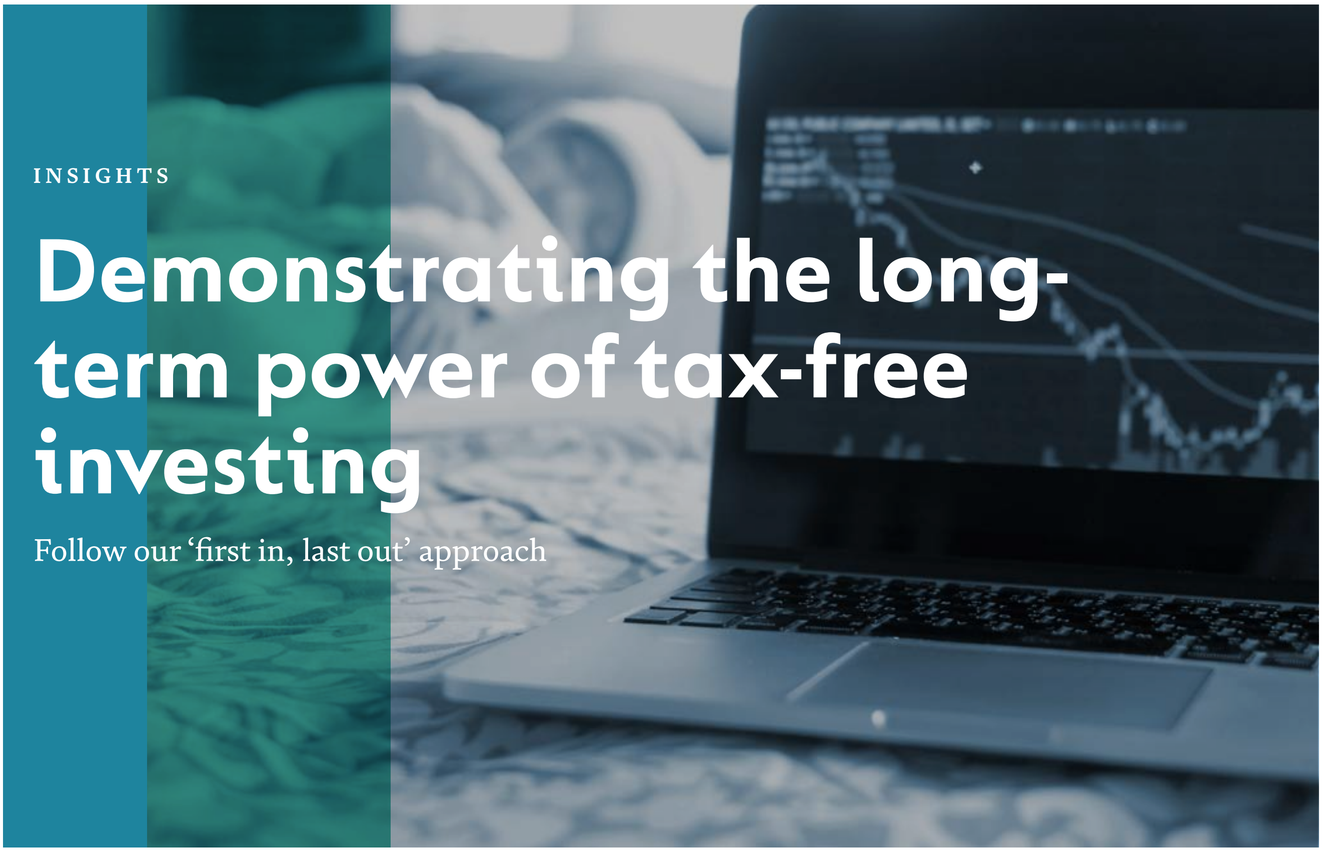
RELATIVELY BETTER VALUE IN ILBS THAN NOMINAL BONDS

Bond	Maturity	Real yield	Equivalent nominal yield @ 5% inflation	Same maturity nominal bond	ILB pick-up over nominal	Required ILB breakeven inflation
R212	31 Jan 22	1.6	6.68	4.3464	2.3336	2.7032
R197	31 Dec 23	1.695	6.77975	5.6751	1.1067	3.9138
I2025	31 Jan 25	2.68	7.814	6.5038	1.3102	3.7240
R210	31 Mar 28	3	8.15	8.4829	(0.3329)	5.3233
I2029	31 Mar 29	3.55	8.7275	8.9709	(0.2434)	5.2351
I2033	28 Feb 33	3.82	9.011	9.9922	(0.9812)	5.9451
R202	07 Dec 33	3.75	8.9375	10.1208	(1.1833)	6.1405
I2038	31 Jan 38	3.91	9.1055	10.6067	(1.5012)	6.4447
I2046	31 Mar 46	3.91	9.1055	10.6908	(1.5853)	6.5257
I2050	31 Dec 50	3.91	9.1055	10.6267	(1.5212)	6.4639

Sources: Bloomberg, Coronation

OUTLOOK

The local economy remains on track to recovery; however, the repercussions of the pandemic continue to reverberate in the form of high unemployment, increased levels of poverty and reduced business confidence. Government finances remain fragile and increased demands on the fiscus threaten to increase the debt load further, pushing the country into a debt trap. Inflation is moving higher but should remain under control despite uneasiness around global inflation. Despite the precarious local backdrop amidst the turbulence caused by local and global monetary policy normalisation, SAGBs still encapsulate a significant risk premium and large margin of safety. We continue to view overweight positions to bonds in the 10- to 15-year area of the curve as attractive. In addition, we believe ILBs in the four- to nine-year area offer good value due to high real yields and embedded inflation protection. +



INSIGHTS

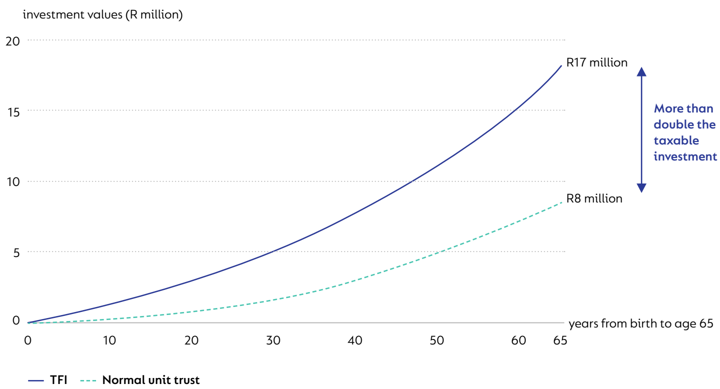
Demonstrating the long-term power of tax-free investing

Follow our 'first in, last out' approach

WITH THE TAX year drawing to a close at the end of February, remember to take advantage of your R36 000 tax-free investment allowance. Our analysis shows that if you start early and invest the maximum allowed every year, you could double the returns from the same taxable investment over the long term. By staying the course, we believe that you can harness the full power of tax-free investing – what we call the 'first in, last out' approach.

Figure 1

THE POWER OF COMPOUNDING TAX FREE



Assumptions:
- R36 000 per year invested in a TFI and a taxable investment (a normal unit trust) at birth until the lifetime limit of a TFI of R500 000 is reached at around the age of 14.
- Investment then grows in both products until age 65.
- End-values assume 6% growth above inflation, 5% inflation and marginal tax of 45%, split between income, dividends and capital growth, based on the historic average of Coronation Market Plus.

Source: Coronation

By 'first in', we mean that you should prioritise taking advantage of your annual tax-free investment allowance as early as possible when you start investing so that you can reap the benefits of compound growth.

We recommend that you be 'last out' of your tax-free investment, because remaining invested for as long as possible further accentuates the compounding of returns not reduced by tax. We also know that leaving your money invested over multiple decades enables it to withstand the effects of short-term market volatility. Over the long term, the ups and downs of markets smooth out, and history has shown that the overall trend in the value of your investment is upwards.

THE REWARDS OF BEING 'FIRST IN, LAST OUT'

The following illustrative example highlights the long-term benefits of adopting a 'first in, last out' tax-free investing strategy.

Imagine that you invest the maximum annual amount (R36 000) in a tax-free investment for your child from birth. If you continue doing so, you will reach the lifetime limit of R500 000 before your child turns 14. The longer you decide to keep the money invested, the more the benefits of compounding and the greater the extent to which your tax-free fund outperforms the same taxable fund.

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Our analysis, based on the assumptions shown in Figure 1, shows that if you keep the money in the fund until your child turns 18, the value of the tax-free investment will be 22% greater than the equivalent taxable investment. By age 30, this difference widens to 42% and, by age 65, the investment would be double the value of the same taxable investment. These results show that by resisting the temptation to disinvest from the fund, the nest egg being built up would keep your child in good stead by either financing tertiary education, buying a first home or ideally investing in their retirement, depending on when your child decides to disinvest.

This theoretical exercise also shows the incredible power of compounding over long periods of time. Investing R500 000 spread out over 14 years and then doing nothing for 41 years result in an investment worth R17 million in today's money by the age of 65. That is enough to fund a retirement income for life of more than R80 000 a month, again in today's money. Our hypothetical (very patient) tax-free investment beneficiary would therefore never have to contribute to retirement while working, effectively freeing up 10% to 15% of annual income that would normally have been required to fund retirement income if you start contributing in your early 20s.

ONCE OUT, ALWAYS OUT WHEN YOU MAKE WITHDRAWALS

While you are free to access your tax-free investment at any time, it's well worth resisting the temptation, because you cannot top-up the fund again. The South African Revenue Service only considers the amounts invested into the fund and disregards any withdrawals when determining your tax-free investment limits.

While the last couple of years have been financially challenging, as always, the best advice is that no matter the external circumstances, start investing now with what you have and reap the rewards in the future. The example above is a keen reminder of the benefits of compounding and how much more your capital grows when not eroded by taxes. So, take the leap before the 2022 tax year ends on 28 February, and remember you have 22 tax-free Coronation funds from which to choose.

NOT YET A CORONATION TAX-FREE INVESTOR?

You can start investing with us via a monthly debit order from as little as R250, or you can make lump-sum investments from R5 000 to R36 000. If you have an existing tax-free savings account with a bank, you can switch it to a tax-free investment at no cost.

To select the funds that suit your needs, speak to your financial adviser if you have one, or visit www.coronation.com and follow our simple online investment process. ✚

STOCK ANALYSIS

Transaction Capital

An attractive new add to our portfolios

BY RUAN KOCH

THE QUICK TAKE

Transaction Capital recently acquired WeBuyCars in a highly value-accretive deal

WeBuyCars is disrupting the traditional used-vehicle dealership business model and presents exciting growth prospects in a low-growth economic environment

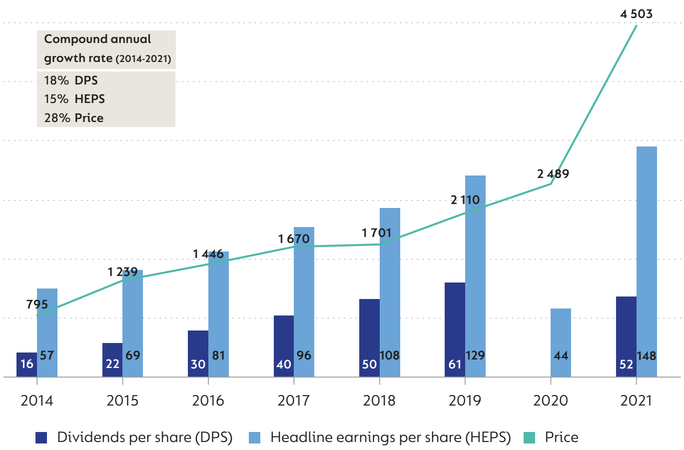
We forecast strong free cash flow per share growth for Transaction Capital

Ruan is an equity analyst with seven years of investment experience.

CORONATION HAS BEEN following Transaction Capital (TCP) for years, but it was its recent acquisition of WeBuyCars that catapulted TCP into our focus and funds. Our analysis suggested that the WeBuyCars deal was done at an extremely compelling valuation and represented an inflection point in the growth prospects of the TCP group. Shareholders have been handsomely rewarded, with TCP delivering a total shareholder return of 83% for 2021 versus 27% from the FTSE/JSE Capped Shareholder Weighted All Share Index (Capped SWIX). A total return rate since inception of 27.7% also compares very favourably to the 10.2% of the Capped SWIX (Figure 1).

Figure 1

TCP PERFORMANCE (ZAR)



Source: Company reports, Bloomberg

TCP is an innovative, entrepreneurial company focused on increasing levels of trust and sophistication in niche industries. It has broad societal relevance in meeting the mobility needs of South Africans, and in the development and empowerment of emerging consumers and businesses, with the majority of South Africans using either personal vehicles or minibus taxis to commute, and 38% of credit-active consumers having impaired records (NCR Credit Bureau).

This article expands on the exciting prospects we see for WeBuyCars. Prior to the WeBuyCars deal, TCP only had two business verticals, SA Taxi and Transaction Capital Risk Services (TCRS).

SA Taxi is a vertically integrated offering to black-owned SME taxi operators that includes financing, insurance, parts and services for new and used minibus taxi vehicles. As the dominant provider >

of finance to the industry and with a strategic relationship with the South African National Taxi Council, we think SA Taxi is well poised for further growth.

TCRS mainly collects on non-performing loans, as an agent on behalf of clients or as a principal on acquired books. We think debt collection, although stigmatised, is a growing industry in South Africa (SA) and internationally. While predominantly an SA business, TCRS has established a growing footprint in Australia and started a disciplined expansion into Europe. We think it can continue this growth while servicing those businesses from the low-cost SA fixed cost infrastructure.

We forecast that SA Taxi and TCRS will generate returns on equity (ROE) exceeding 20%, with double-digit earnings growth over the medium term. After the WeBuyCars deal, we think the growth algorithm for the company has changed to be structurally higher. For the 2021 financial year, WeBuyCars constituted 27% of group earnings, and our analysis suggests it could exceed 60% of group earnings in a few years, growing at more than 30% p.a..

WHAT MAKES WEBUYCARS SO COMPELLING?

There are 12.9 million vehicles in the SA vehicle parc, of which 11 million are registered as passenger or light commercial vehicles (eNaTIS). It is illegal to import used vehicles into SA, so the only stock for the parc can come from new vehicle sales. There are 500 000 to 600 000 annual new vehicle sales in SA (National Association of Automobile Manufacturers of SA [NAAMSA]) and roughly 1.2-1.4 million used-vehicle sales (eNaTIS and Lightstone).

WeBuyCars, founded in 2001 by brothers Faan and Dirk van der Walt, started with the idea that the best used-vehicle stock is currently in the hands of consumers. They decided to build a business around consumer-to-business sourcing and focused on massively improving the experience for vehicle sellers. Acquiring cars directly from consumers is still a critical part of the company's competitive advantage. WeBuyCars spends >R150 million annually on marketing through countless social media, billboard, radio and print campaigns to ensure it remains top of mind for consumers when they consider selling a vehicle.

WeBuyCars creates more utility for vehicle sellers (instant quotes, coming to your house or office, doing the paperwork, paying cash immediately, no haggling), and for buyers (wider and deeper selection of models and colours in one place, better experience, online capabilities). Although it competes with dealers, WeBuyCars also adds utility for these entities. Dealers view WeBuyCars as a low-cost, efficient origination channel for vehicles that the dealer can recondition and sell for profit.

Unlike traditional dealerships, WeBuyCars does not have expensive glass-walled showrooms in prime locations. Instead, they leverage scale benefits by using large warehouses closer to industrial areas, giving its supermarkets the capacity to display between 500 and 1 500 vehicles. Large dealer groups also often have vehicle original equipment manufacturer brand affiliation and limited pricing flexibility. In contrast, WeBuyCars has no brand affiliation and can dynamically adjust pricing to optimise stock turn and drive good cash conversion.

SA has one of the broadest selections of vehicle makes and model derivatives relative to market size in the world (NAAMSA), and being able to price these vehicles accurately and quickly is another competitive advantage. WeBuyCars has built a rich database of older used-vehicle prices and uses artificial intelligence to further fine-tune its pricing algorithms.

ECOMMERCE DISRUPTION

Online marketplaces like cars.co.za and Autotrader are platforms where traditional dealers consolidate their marketing spend to originate leads for their physical dealerships. The marketplaces carry no stock, and once a lead gets converted, the buying experience requires a visit to a physical dealership. WeBuyCars has already done away with the physical visit requirement on the selling side, and it's now doing the same on the buying side too. The company aims to become the leading online used-vehicle ecommerce platform in SA, and already allows dealers and the public to participate in online vehicle auctions, making up 30% of sales. The next step is allowing the public to buy cars online that are then delivered directly to them, with no dealership visit necessary.

Online sales will drive further efficiencies, where faster stock turns could allow more flexibility to optimise returns. Better prices and more convenience should narrow the bid/ask spread, lower the friction to trade a vehicle and lead to an expansion of market demand.

FINANCING

Another source of additional market demand will come from providing bespoke financing solutions for older vehicles. Unlike banks that mostly only finance used vehicles younger than five years, WeBuyCars can underwrite and recover residual

>

values for much older vehicles. This should attract new consumers to the used-vehicle market, while also generating an attractive return for WeBuyCars.

WeBuyCars could also potentially expand internationally, replicating in other markets. Compared to many of the online used-vehicle start-ups that have proliferated recently (Vroom, Shift and Carlotz in the US; Cinch and Cazoo in the UK), WeBuyCars already has a more profitable business model and has reached more scale than most.

Its current sales run rate is 10 000 vehicles per month, with a medium-term target of 15 000. We think the superiority of its business model could easily see WeBuyCars reach 20% market share in SA, implying more than 20 000 vehicles sold per month. We also think that the learnings from finance and insurance in SA Taxi will be a huge benefit to WeBuyCars, so we forecast an improvement in unit economics and overall margins as the business scale increases.

WEBUYCARS NEW INITIATIVES

VEHICLE SUPERMARKET IN DEVELOPMENT

1 400 parking bays

NEWLY LAUNCHED VEHICLE BUYING POD IN GAUTENG

27 buying pods nationwide

NEW DELIVERY TRUCKS INTRODUCED IN GAUTENG

Launched August 2021

Source: Company presentation

CONCLUSION

In all its businesses, TCP has deep specialisation and expertise, and offers attractive customer value propositions. The durability and profitability of all three verticals have been proven over 20-year operating histories and various crises, and TCP is now in the scaling and replication phase.

The proof is in the numbers, and the existence of the moat and quality of the business are shown in the historically high returns and earnings growth. SA Taxi and TCRS have averaged 25% and 20% ROEs, respectively, and WeBuyCars is generating an ROE of more than 50%. The competitive advantage period for TCP will be significantly longer than we think is being priced in, and TCP will continue to generate high returns. TCP is a leader in all its industries and shows promise of organic growth, either by participating in the growth of the overall market or by growing its market shares.

Although the mispricing gap we identified has somewhat narrowed, we think there is ample room for upside surprise from a management team that has true skin in the game (the founding partners and current management own 17% of the shares in issue) and has proven themselves to be excellent capital allocators over time. SA Taxi and TCRS provide stable and defensive business prospects, while WeBuyCars offers a big growth opportunity with scale benefits and offshore expansion opportunities. The company's unique positioning will continue to deliver growth in free cash flow per share far exceeding that of the general market for some time to come. ✚

EMERGING MARKETS

European value retail

An attractive, growing sector in both Eastern and Western Europe

By NICOLE MADURAY

THE QUICK TAKE

- Value retail thrives in Central and Eastern Europe (CEE) where consumers are extremely price conscious
- High minimum wage increases across CEE is positive for the value retail sector
- Dino Polska is a fast-growing value food retailer in Poland, the most populated country in CEE
- Pepco Group is expanding across CEE and Western Europe, and is on track to become Europe's largest value variety retailer

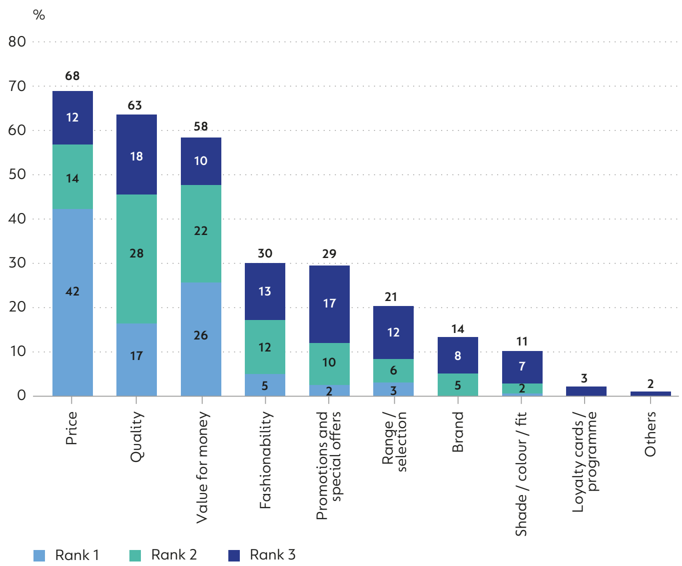
Nicole is an equity analyst in the Global Emerging Markets team.

VALUE RETAILERS, ALSO called discount stores, are shopping outlets that sell branded and private label merchandise at significantly lower prices than conventional retailers. In order to offer low prices, value retailers negotiate low wholesale prices with suppliers, maintain high sales volumes through regular promotions, and furnish stores with basic fixtures, displays and decorations. The low-cost, low-price business model has proven to be a winning retail format globally as cash-strapped, value-seeking customers search for quality products at bargain prices.

In Europe, value retail is relatively underpenetrated compared to the US, but the sector is rapidly growing. It is estimated that the number of value retail stores in Europe could double by 2029, taking even greater share of the overall retail market.

Figure 1

WHEN BUYING CLOTHING, WHAT IS THE KEY REASON FOR YOUR CHOICE OF RETAILER? (RANK 1-3)



Sources: HSBC, Toluna; number of respondents: 1 205

CENTRAL AND EASTERN EUROPEAN VALUE DEMAND

Value retail penetration varies across Europe, with some of the greatest demand for value coming from countries in CEE, such as Poland, Romania, Hungary and the Czech Republic (Czechia). CEE consumers are estimated to have the highest level of price sensitivity globally and are extremely value conscious. In Poland, the most populated CEE country, consumers rank 'price' as the most important factor in deciding where they shop, followed by 'quality' and 'value for money' (see Figure 1).

Across CEE, the disposable incomes of value consumers are rising due to high minimum wage growth. In Poland, Romania and Czechia, minimum wages outpaced nominal wage growth between 2012 and 2019. In 2020, minimum wages increased by high single digits in Romania, Hungary and Czechia, and surged by a sizeable 15.6% in Poland. The Polish government plans >

a continuation of steep increases in minimum wages through to 2024, increasing the minimum wage to 40% higher than 2021 levels. While the proposed hikes should have some negative impact on value retailers due to higher employee costs, the increase should lead to sustainable growth in the disposable incomes of value retailers' core customers and support increased value retail spending.

In the value retail segment, online sales have not yet been widely adopted in CEE countries. Ecommerce penetration is low, ranging from 12% to 24% compared to >30% in the UK.

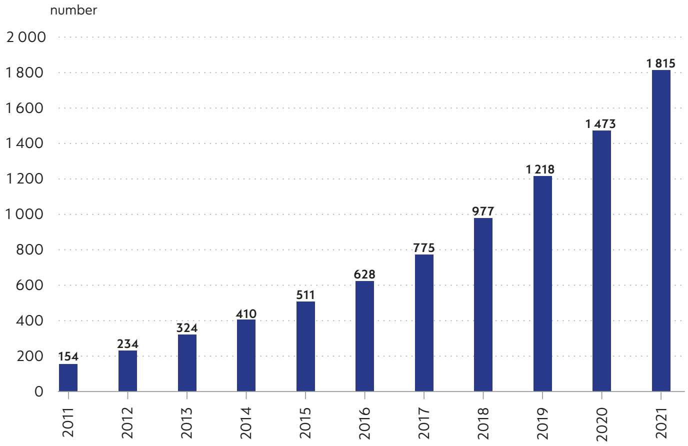
Highly dispersed populations in CEE countries make ecommerce operations less attractive than in many Western European markets, as the proportion of CEE consumers living outside major cities is high, making last-mile logistics more expensive. In addition, credit card penetration across CEE is low, which poses somewhat of a barrier to ecommerce.

Globally, many discount retailers have not integrated ecommerce, as the low average transaction sizes make it difficult to absorb order delivery and fulfilment costs, and be profitable online.

However, value retailers are not behind the times; they embrace digital tools to connect with their customers by offering online product search functionality, and using social media and digital advertising to promote their products. Demand for value retail continues to grow despite the lack of ecommerce, as price remains king.

Figure 2

DINO STORE EXPANSION TO DATE



Source: Company reports

POLISH FOOD RETAIL – DINO POLSKA

With its population of 38 million, Poland is CEE's largest food retail market. The market is largely formalised, with high penetration of modern food retail, but it is still very fragmented, offering opportunities for value food retailers to consolidate the market. While price competitiveness remains most important for Polish consumers, the need for convenient grocery shopping has increased. This trend accelerated in 2020 as the pandemic resulted in more consumers shopping in smaller stores, closer to home. Leading Polish food retailer Dino Polska offers both convenience and low prices, and has rapidly expanded from 154 stores in 2011 to approximately 1 800 stores across Poland today (see Figure 2).

Dino's strategy is built on low levels of urbanisation and the lack of convenient modern food retail alternatives in smaller towns and rural areas. Its stores are mid-sized supermarkets primarily located outside major cities, as 60% of the Polish population lives in small towns and rural areas.

The company has an effective 'cheap-enough' pricing strategy where it matches the pricing of household staples and basic food items to lowest price discounters. The low pricing of basic items attracts footfall, while pricing of the overall product portfolio remains broadly in line with the market, to remain competitive.

While discounters and hypermarkets generally offer similar prices to Dino, their large store footprints present a hurdle to their expansion to outlying areas. Dino's store base continues to expand in small towns and rural areas, and the company sees significant white space for further store expansion. We expect food discounters and value supermarkets like Dino to continue gaining share of the overall food retail market in CEE, as its expansion results in greater economies of scale and leads to better value for consumers.

VALUE VARIETY RETAIL – PEPCO GROUP

Alongside the shift in value food retailing, discount apparel, homeware and fast-moving consumer goods (FMCG) retailers are rapidly expanding across Europe, particularly in CEE countries. Penetration of discount retailing in CEE is relatively low at 19% compared to 23% in Western Europe, indicating significant potential for further value variety retail expansion.

Pepco Group is one of the fastest-growing value retailers in CEE, with the potential to become Europe's largest value variety retailer.

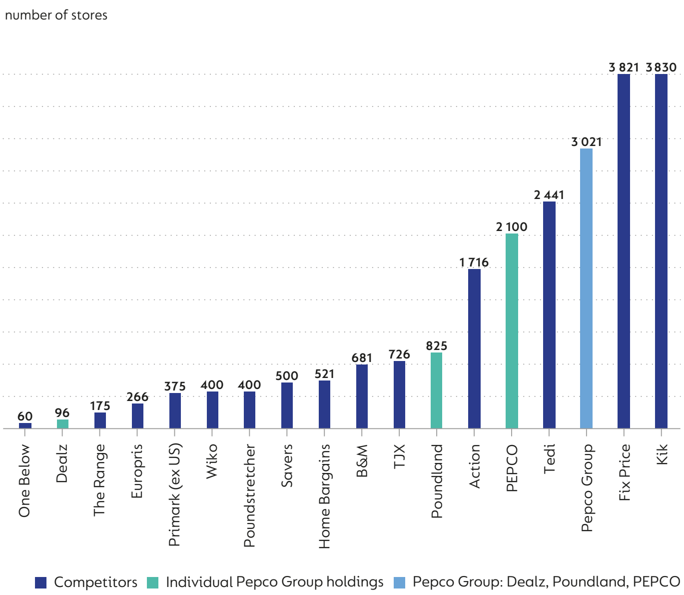
The company aims to be the price leader in its markets and operates an 'everyday low price' strategy instead of a heavy reliance on promotions. Pepco Group's offering is perceived as good value for money, with low prices for good quality items, which appeals to core value customers.

Pepco Group is a multi-format value retailer, with over 3 000 stores across Europe (Figure 3). The Group comprises three brands:

1. PEPCO*, a clothing and general merchandise retailer in Poland and other CEE countries (the European equivalent of Pep in South Africa).
2. Poundland, a FMCG, general merchandise and clothing retailer in the UK.
3. Dealz, the Poundland equivalent outside the UK, currently in Poland and Spain.

Figure 3

STORE COUNT OF LEADING EUROPEAN VALUE RETAILERS, 2020



Source: JPMorgan estimates based on companies' public sources

PEPCO is the biggest brand within the Group, accounting for almost 80% of profits. About half of the Group's PEPCO stores are located in Poland, followed by numerous stores in other CEE countries, such as Romania, Hungary and Czechia. Poland has become a battleground for value variety retail, with value retailers rapidly expanding their store bases in the region and Western European retailers starting to enter the Polish market.

The most recent example of this is leading UK value retailer Primark, which opened its first store in Poland in August 2020.

While competition in Poland is intensifying, PEPCO's large scale and everyday low prices should provide some degree of protection from increased competition.

Pepco Group management sees significant opportunities to expand across Europe and has set a target of opening 300 PEPCO stores and >100 Dealz stores per annum over the next three years. The Group uses a centralised management and sourcing approach, combined with standardised product assortment and a consistent store layout across each brand. These key practices enable fast store rollouts as they simplify the process of setting up in new markets and support longer-term operating efficiencies.

In addition to CEE, Pepco Group sees Western Europe as an exciting opportunity for further expansion, with the market opportunity in Italy and Spain roughly equal to the size of the entire CEE market. The Group plans to expand in Western European markets with its attractive offering, selling at Eastern European prices. In 2020, Pepco Group opened its first stores in Italy and delivered well above target, with profits approximately 40% higher than in its CEE stores. The company plans to expand across Italy, Spain, Austria, Greece, Germany and Portugal, and remains on track to become Europe's largest value variety retailer.

Overall, we view European value retail as an attractive, growing sector. Our outlook on both Dino Polska and Pepco Group is positive; however, we believe that Dino is currently overvalued. Pepco Group is our top pick in the European value retail sector.

The company has delivered a solid operational performance since the stock listed on the Warsaw Stock Exchange in May 2021. We feel that the market is overlooking Pepco Group's ability to successfully expand its footprint across both Eastern and Western Europe, and grow its share of the total retail market. In our view, Pepco Group remains attractively valued over a long-term horizon and we therefore own Pepco Group shares in our portfolios.✚

* PEPCO in uppercase denotes the brand and Pepco Group is the holding company that owns PEPCO, Poundland and Dealz.

Key performance indicators and fund performance

AS AT 31 DECEMBER 2021

		QTD	YTD	1 YEAR	3 YEARS	5 YEARS	10 YEARS	15 YEARS	20 YEARS
INTERNATIONAL INDICES [USD]									
Global Equity	**MSCI ACWI**	6.7%	18.5%	18.5%	20.4%	14.4%	11.9%	7.1%	8.0%
	MSCI WORLD	7.8%	21.8%	21.8%	21.7%	15.0%	12.7%	7.4%	8.1%
	MSCI GEM	(1.3%)	(2.5%)	(2.5%)	10.9%	9.9%	5.5%	4.5%	9.6%
	S&P 500	11.0%	28.7%	28.7%	26.1%	18.5%	16.6%	10.7%	9.5%
Global Property	**Global Property (FTSE EPRA/NAREIT Developed Index)**	10.4%	27.2%	27.2%	12.9%	8.8%	9.6%	4.4%	9.6%
Global Bonds	**Barclays Global Bond Aggregate**	(0.7%)	(4.7%)	(4.7%)	3.6%	3.4%	1.8%	3.3%	4.4%
US Cash	**3 Month Libor**	0.0%	0.2%	0.2%	1.1%	1.4%	0.9%	1.2%	1.6%
SPOT RATES AND COMMODITY PRICES									
Exchange Rates	**Rand Dollar exchange rate**	15.1	14.7	14.7	14.4	13.7	8.1	7.0	12.0
	Rand Dollar % change	(5.5%)	(7.8%)	(7.8%)	(3.4%)	(3.0%)	(6.6%)	(5.4%)	(1.4%)
	Rand Euro exchange rate	17.4	18.0	18.0	16.5	14.4	10.5	9.2	10.6
	Rand Pound exchange rate	20.3	20.1	20.1	18.3	16.7	12.5	13.7	17.4
Select Commodities	**Gold price (USD)**	1 742.8	1 891.1	1 891.1	1 281.7	1 159.1	1 531.0	632.0	276.5
	Oil price (USD barrel)	78.3	51.8	51.8	54.4	56.8	107.4	60.9	19.9
SOUTH AFRICAN INDICES [ZAR]									
SA Equity	**ALSI (J203T)**	15.1%	29.2%	29.2%	15.7%	11.4%	12.2%	10.8%	13.6%
	CAPI (J303T)	14.4%	31.7%	31.7%	15.7%	11.1%	12.2%	11.0%	-
	Capped SWIX (J433)	8.7%	27.1%	27.1%	10.9%	7.2%	10.7%	-	-
	Resources Index (J258)	21.6%	32.3%	32.3%	27.3%	22.9%	7.8%	7.1%	9.8%
	Industrial Index (J257)	16.1%	26.5%	26.5%	15.5%	9.3%	14.0%	13.5%	16.5%
	Financials Index ex property	2.5%	29.6%	29.6%	1.6%	2.9%	10.2%	8.1%	12.1%
SA Property	**Africa All Property Index (J803T)**	8.4%	38.6%	38.6%	(3.8%)	(5.2%)	5.3%	-	-
SA Bonds	**BEASSA (TR) All Bond Index**	2.9%	8.4%	8.4%	9.1%	9.1%	8.2%	8.3%	9.5%
SA Cash	**Short Term Fixed Interest 3 Month Cash Rate**	0.9%	3.6%	3.6%	5.1%	5.8%	5.8%	6.7%	7.3%
SA Inflation	**Inflation**	1.2%	5.8%	5.8%	4.3%	4.4%	5.0%	5.7%	5.6%

	QTD	YTD	1 YEAR	3 YEARS	5 YEAR S	10 YEARS	15 YEARS	20 YEARS	SINCE LAUNCH
DOMESTIC FUNDS (PERFORMANCE IN ZAR)									
Coronation Top 20 Fund	7.1%	24.1%	24.1%	16.2%	10.2%	11.6%	11.8%	15.4%	17.1%
ASISA Mean of South African Equity General	9.3%	27.6%	27.6%	12.2%	7.8%	9.8%	8.9%	13.2%	13.7%
Coronation Market Plus Fund	7.5%	22.1%	22.1%	14.6%	9.1%	11.4%	10.9%	14.6%	15.0%
ASISA Mean of South African Multi-Asset Flexible	6.9%	22.8%	22.8%	11.7%	8.2%	10.6%	9.4%	11.6%	11.4%
Coronation Balanced Plus Fund	7.3%	21.5%	21.5%	14.3%	9.5%	11.1%	10.5%	13.4%	14.1%
ASISA Mean of South African Multi-Asset High Equity	7.3%	20.4%	20.4%	11.5%	8.0%	9.2%	8.3%	11.8%	12.2%
Coronation Capital Plus Fund	5.9%	16.0%	16.0%	10.6%	7.1%	8.5%	8.7%	11.0%	11.5%
ASISA Mean of South African Multi-Asset High Equity	7.3%	20.4%	20.4%	11.5%	8.0%	9.2%	8.3%	11.8%	12.2%
Coronation Balanced Defensive Fund	4.7%	12.7%	12.7%	9.5%	7.6%	9.0%	-	-	9.3%
ASISA Mean of South African Multi-Asset Low Equity	5.0%	13.7%	13.7%	9.0%	7.3%	8.1%	-	-	7.7%
Coronation Strategic Income Fund	1.9%	6.7%	6.7%	6.5%	7.2%	7.9%	8.4%	9.3%	9.7%
ASISA Mean of South African Multi-Asset Income	1.9%	6.7%	6.7%	6.9%	7.3%	7.0%	7.6%	9.0%	8.8%
INTERNATIONAL FUNDS (PERFORMANCE IN USD)									
Coronation Global Equity Select Fund	1.0%	4.9%	4.9%	18.1%	10.4%	-	-	-	7.6%
Coronation Optimum Growth Fund	0.0%	(5.2%)	(5.2%)	12.6%	8.9%	7.7%	5.0%	11.0%	9.3%
Coronation Global Managed Fund	0.5%	2.1%	2.1%	11.3%	6.6%	7.1%	-	-	6.4%
Coronation Global Capital Plus Fund	1.2%	3.0%	3.0%	6.7%	4.2%	4.3%	-	-	4.1%
Coronation Global Strategic Income Fund	0.0%	1.1%	1.1%	2.3%	1.8%	2.3%	-	-	2.3%

All ASISA averages exclude Coronation funds in that category.
For detailed information on our range of unit trust funds, including highest and lowest annual return ranges, please visit our fund centre on www.coronation.com.

Meaningful periods

Figures as at 31 December 2021.

FUND UPDATE

Coronation Top 20 Fund

By **NEVILLE CHESTER** *and* **NICHOLAS STEIN**

Neville is a senior portfolio manager with 25 years of investment experience.

Nicholas is an equity analyst with 13 years of investment experience.

THE FUND RETURNED 7.1% for the quarter and 24.1% for the last 12 months. The Fund's long-term performance remains pleasing against both the peer group and the benchmark.

Our commodity positions (including gold) contributed to performance for the fourth quarter of 2021 (Q4-21), while underweights in MTN and Richemont detracted.

The major commodity-related news of the last quarter was the ongoing potential takeout of Royal Bafokeng Platinum (RB Plat), with both Northam and Impala vying for control. Initially, Impala announced that it was in talks to acquire RB Plat. Subsequently, Northam surprised the market by buying RB Plat's parent company's 34.9% stake in RB Plat for R180 per share. Impala subsequently bought stakes from other shareholders and now sits with c.35% of RB Plat's shares.

We are somewhat uncomfortable with Northam paying R180 per RB Plat share, with Impala paying closer to the R150 level for its stake. Impala has contiguous operations to RB Plat and can extract meaningful synergies. Northam's operations are far from RB Plat, and it has no such opportunities. As a result, Impala should be able to offer a higher price than Northam, and our concern is that Northam overpays for the remaining stake, should the company pursue this avenue. We reduced the size of our Northam holding and increased Impala during the quarter.

The gold price and gold equities performed well over the quarter. Investors grew increasingly concerned that the high levels of inflation we have seen will prove to be persistent and not transitory. This, coupled with concerns that the Federal Reserve Board is behind the curve in hiking rates to curb inflation, provided a buoyant environment for gold. AngloGold advanced by c.40% over the quarter.

The diversified miners performed strongly over December, as Chinese demand for commodities stabilised and the Chinese government eased monetary policy. We reduced the size of our Glencore holding.

Along with most other emerging market currencies, the rand weakened meaningfully over the quarter (8%). This was supportive of our overweight positions in the so-called 'global shares that happen to be listed here'. This includes Anheuser-Busch, Naspers and British American Tobacco.

One global share we don't own is Richemont. The Richemont share price was very strong this quarter, rising 55% on the back of very good operating results. Goods consumption has outperformed services in the post-pandemic recovery, which has been felt particularly acutely in the luxury sector. Hard luxury goods have been resilient in the recovery from the pandemic as wealthy

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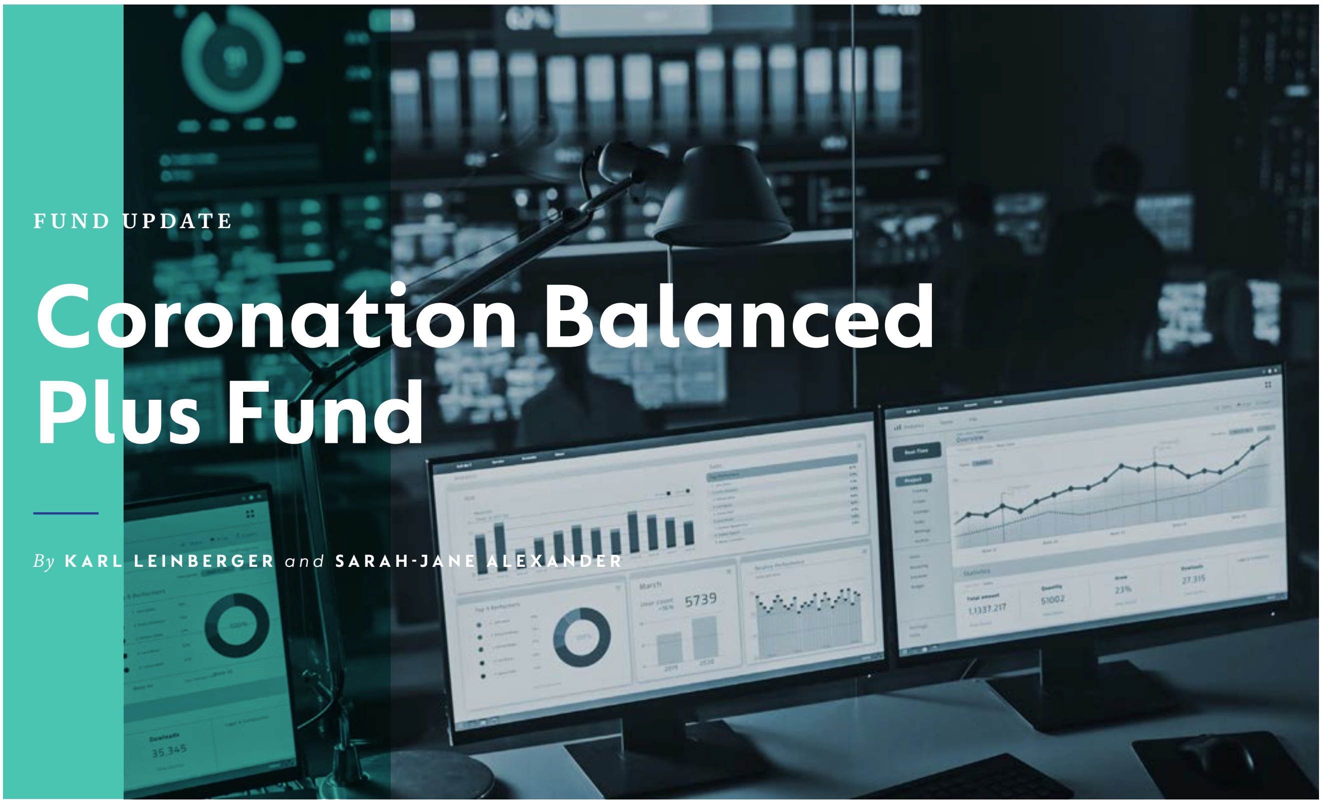
buyers, unable to spend on international holidays, have repurposed their spending towards this category. While the runway for Richemont to keep growing the jewellery business is clear, as branded jewellery grows from low levels, we believe this is more than discounted in the current share price and that there is no room for error in the Richemont valuation. We see better risk-adjusted returns in our current global holdings.

There was little to cheer about on the domestic news front. The emergence of the Omicron variant came at a terrible time for South Africa's (SA) hospitality industry. Despite the government's sanguine approach and level-headed lockdown measures, governments around the world blocked key travel into and out of SA. Fortunately, despite record Covid-19 case counts, Omicron's mortality rate appears to be far lower. This should benefit our local life insurers. Our insurers raised provisions that assumed the Omicron wave would experience worse mortality than appears to be playing out. We added slightly to our life insurers during the quarter.

While far less exposed to the direct impact of Covid-19, a number of misgivings around the Spar investment case came to the fore during the quarter, including a weak sales update that implies an uncharacteristic loss of market share, an impending SAP system implementation (these rarely go smoothly), Spar lacking a credible omnichannel offering (no online and on-demand offering) and a deteriorating balance sheet. Spar's business model conveys excellent economics (high return on equity, free cash flow conversion and a strong moat). We hold the management team in high regard and believe it will overcome all these challenges. However, there are a number of balls in the air at the same time, and the business is up against strong competition. While we still see Spar as attractive, we no longer view it as a Top 20 idea. We sold our Spar holding during Q4-21.

In its place, we added Woolworths, a stock that has featured in the Fund before. The share has derated meaningfully versus the market over the last quarter. Woolworths has an incredibly strong SA food business that has taken consistent market share over the last decade – a trend we expect to continue. The SA and Australian clothing businesses have been a disappointment. The upshot of this is that margins here are low, with good scope for margin expansion in the future. We are encouraged by the steps new management is taking, such as reducing management layers, simplifying the clothing range, etc. Australia should also be a beneficiary of the reopening trade as the country emerges from acute lockdowns. Woolworths trades on less than nine times our assessment of normal earnings. ✚



FUND UPDATE

Coronation Balanced Plus Fund

By **KARL LEINBERGER** *and* **SARAH-JANE ALEXANDER**

Karl is CIO and manager of Coronation's Houseview strategies.

Sarah-Jane is a portfolio manager with 18 years of investment experience.

THE FUND RETURNED 7.3% for the quarter, resulting in a return of 21.5% over the last year. Performance benefited from strong markets, accretive asset allocation decisions and good alpha in the domestic building blocks. The Fund has performed well against its peer group over all meaningful time periods.

It was another strong year for global markets, as the MSCI All Country World Index ended the year up 19% in US dollars. Markets shrugged off the rise in infections caused by the Omicron variant to deliver a 7% rise in the fourth quarter of 2021 (Q4-21) – including 4% in December. Having aggressively increased global equity exposure during the Covid-19 collapse, the Fund is currently underweight, given full valuations and the concerns we have over multiple signs of speculative froth in global markets.

Emerging markets performed poorly, with the MSCI Emerging Markets Index declining -3% in US dollars over the course of 2021. This was materially impacted by China, where government regulation of the economy has become increasingly intrusive and capricious. While the risks are high, Chinese technology stocks trade at extremely attractive valuations. The Fund is exposed to China through both its global equity allocation and its domestic equity allocation where the Fund holds Naspers/Prosus and commodity stocks.

Expectations for inflation are shifting from transitory to structural. The easing of lockdown restrictions and huge monetary stimulus have created strong demand. Combined with Covid-19-constrained supply, this has resulted in near-term price pressure. The oil price (Brent crude) rose 71% during the year. Longer-term wage pressures are emerging in developed economies with record-low levels of unemployment. High levels of sovereign indebtedness impair the ability of central banks to respond aggressively to inflation. US CPI rose from below 2% to north of 6% during the year. The high levels of sovereign indebtedness, rising inflation and low yields keep us cautious on developed nation sovereign bonds. For the year, the Bloomberg Barclays Global Aggregate Bond Index declined -5% in US dollars.

The South African (SA) economy is recovering after the deep recession of 2020. The economy is forecast to return to its pre-Covid levels in 2022, a year earlier than previously expected. This better economic performance, combined with improved governance and a commitment to fiscal sustainability, should be sufficient for SA to navigate its fiscal challenges for the next few years. The improved fiscal situation was reflected in the upgrade by Fitch Ratings of SA's credit rating outlook from negative to stable. Longer term, economic growth remains critical to avoid a debt trap. Challenges include unstable power

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supply, structurally high unemployment, a poor education system, declining productivity and slow policy reform. High levels of social inequality and unemployment came to the fore in Q3-21 with the outbreak of looting across KwaZulu-Natal. The rand declined -8.5% against the US dollar for the year (-5.8% for Q4-21).

The FTSE/JSE All Bond Index delivered a return of 8% for the year (3% for Q4-21). The Fund has meaningful exposure to SA bonds, with the long end of the curve offering attractive yields in both absolute terms and relative to other emerging markets and alternatives such as cash. We continuously assess the risks and appropriate positioning. The ANC's elective conference in late-2022 will be another critical milestone. Our base case is the re-election of President Cyril Ramaphosa, which would be positive for ongoing fiscal discipline.

Like global markets, local markets ended the year strongly, with the FTSE/JSE Capped SWIX Index delivering 9% in rands in Q4-21 to end the year up 27%. The Fund's sell-down in global equities earlier in the year funded an overweight exposure to SA equities. This position sits at a decade-high and is a consequence of the breadth of value that we find across resources, global stocks that are locally listed and domestic shares. There was broad strength, with the resource sector delivering 32% for the year (22% for the quarter), financials 30% (3% for the quarter) and industrials 26% (16% for the quarter) despite the pressure on major constituent Naspers (-18% for the year and -1% for the quarter).

Within the resources sector, holdings in the diversified miners (Glencore +80% for the year and Anglo American +46% for the year) have contributed strongly to performance over the past few years. Strong demand, driven by recovering economies and decarbonisation, along with disciplined capital expenditure, have supported tight markets. The diversified miners continue to offer good value with low multiples and solid free cash flow generation. During the year, proceeds from the platinum group metal shares were recycled into gold equities (AngloGold and Gold Fields), which offer upside and reasonably priced protection against stretched sovereign balance sheets and the risk of structurally higher inflation. Both have improved their production profiles and geographic diversification. We anticipate a period of increased returns to shareholders under their new leadership teams.

The Fund has meaningful exposure to several global businesses that are listed in SA. These include Naspers (-18% for the year, -1% for the quarter)/ Prosus (-18% for the year, +9% for the quarter), British American Tobacco (+16% for the year, +13% for the quarter), Bidcorp (+26% for the year, +2% for the quarter), Quilter (+6% for the year, +9% for the quarter), Textainer (+103% for the year, +8% for the quarter) and Aspen (+81% for the year, -17% for the quarter). Aspen is negotiating a potentially accretive disposal of its active pharmaceutical ingredients business and a vaccine licensing deal from Johnson & Johnson to supply the African Union. The weaker Q4-21 return from Aspen reflects high expectations at the onset.

The Fund has a considerable holding in Naspers/ Prosus that we believe to be materially undervalued. This is because of the low value being attributed directly to Tencent and the discounts that exist at the holding company level. The investment risk has increased, with China's regulatory interventions and the threat to foreign capital. Thus far, regulations affecting technology companies are broadly consistent with what we see elsewhere, covering fintech, antitrust law, data security and 'Gig employee' labour protection. Tencent is a formidable company that generates good free cash flows, has a very engaged user base and is growing businesses across multiple verticals. None of the restrictions thus far are expected to meaningfully change Tencent's prospects. An investment in Naspers/Prosus offers a cheap entry point to Tencent and provides access to an attractive investment portfolio.

Disappointingly, the Fund sold down its investment in MTN (+184% for the year, +21% for the quarter) too early. While we were believers in the operational turnaround, we were very concerned about the outlook for the Nigerian economy and the regulatory risk within Nigerian Telecoms. Improved stakeholder relations and the likely conclusion of a mobile money licence in Nigeria support future earnings growth and we have re-established a holding in the company.

Domestic companies continued to report results ahead of our expectations throughout 2021 due to more resilient economic activity and stringent cost control. We believe attractive stock picking opportunities exist, either from businesses with specific opportunities like Dis-Chem (+71% for the year, +20% for the quarter), Rand Merchant Investment Holdings Ltd (RMI [+43% for the year, +21% for the quarter]) or Transaction Capital (+83% for the year), or even in more mature industries like banking or food retail where those with strong franchises that have continued to invest should benefit from share gain. Shoprite (+54% for the year, +17% for the quarter) demonstrated this during Q4-21 by surprising the market with the strength of its sales growth. The management team has invested behind the business, building

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distribution centre capacity, updating systems and embracing digitisation. The team's progress in building out a data-driven business built around the consumer is impressive.

RMI has been restructuring to create a focused property and casualty insurance company. The restructuring initially announced should unlock shareholder value as the unbundling of holdings in Momentum Metropolitan Holdings and Discovery reduces the conglomerate discount and improves investor focus on the underlying assets (specifically OUTsurance). OUTsurance is a quality business that we expect to deliver double-digit earnings growth while generating high returns. The attractiveness of the restructuring proposal was increased during the quarter when RMI received a generous offer for its stake in Hastings. The resultant cash inflow and associated degearing will enable RMI to avoid the rights issue required to achieve the initial unbundling and improve the dividend flowthrough from the very cash-generative OUTsurance business.

Despite the share price moves during the quarter, this remains an attractive investment, with the core OUTsurance asset trading at a low look-through multiple relative to its high-quality nature and strong growth prospects, particularly in Australia. The portfolio has moderate property exposure, preferring to use its risk budget in equities and bonds. While the sector performed strongly during 2021 (+37%), it is still negative (-3% p.a.) over three years. Holdings are predominantly in the A shares, with some exposure to logistics assets. The medium-term outlook for property remains subdued as a weak economy and a structural shift in demand from increasing digital engagement and work-from-home trends undermine rental tension.

While headwinds exist in both global markets and the domestic economy, we believe that cheap domestic assets are well priced for the risks and should offer attractive returns. +

FUND UPDATE

Coronation Balanced Defensive and Capital Plus funds

By **CHARLES DE KOCK, PALLAVI AMBEKAR** *and* **NEILL YOUNG**

Charles is a senior portfolio manager with 35 years of investment experience.

Pallavi is a portfolio manager with 19 years of investment experience.

Neill is a portfolio manager with 24 years of investment experience.

COVID-19 CONTINUES TO delay a much-desired 'return to normal' in the global economy. The highly transmissible Omicron variant has resulted in another pause in a year marked by economies lurching between stop-and-start phases. While the virus is disruptive, we are learning that vaccines and boosters are at least successful in mitigating severe illness. As the percentage of the vaccinated population increases, we think that 2022 will continue the path of emergence from the pandemic.

Despite this unsettled environment, we have seen a robust economic recovery, with much less scarring than anticipated when the pandemic began. As said before though, things are still far from normal and new risks are emerging. Surging consumer demand, coupled with supply chain bottlenecks, high energy prices and employee shortages are leading to increasing global inflation. Central banks previously indicated a willingness to tolerate higher inflation, but are also realising that allowing things to run too hot may lead to increased recessionary risks. As such, we have seen Chairman Jerome Powell indicate that the US Federal Reserve Board will start tapering asset purchases and raising interest rates in the course of 2022. Global bonds which were, in our view, already expensive to start with, will provide poor returns in this environment. Global equity indices also look full after another year of high returns. However, the concentration of returns to a few large stocks in global equity markets means there is still a broad opportunity set for active managers focused on long-term valuations. The Capital Plus Fund's offshore allocation sits at 25% and Balanced Defensive's is 24%, with the majority of this exposure in global and emerging market equities. A portion of this equity exposure is protected by put options, which provide some portfolio insurance in the event of a general market selloff.

On the local front, the economic growth we saw in the first half of last year has rapidly unwound in the second half. The rioting and looting in the third quarter were further compounded by loadshedding and the inopportune 'red list' travel restrictions imposed on South Africa (SA) at the start of our tourist season. We expect slower domestic growth this year, supported by rising household consumption expenditure and some improvement in investment spend. Longer term, our outlook for GDP growth remains very muted, as we are not seeing evidence of the bold policy reform needed to structurally uplift the economy. Inflation, though, remains well contained at around the 5% level and the projected interest rate trajectory remains benign.

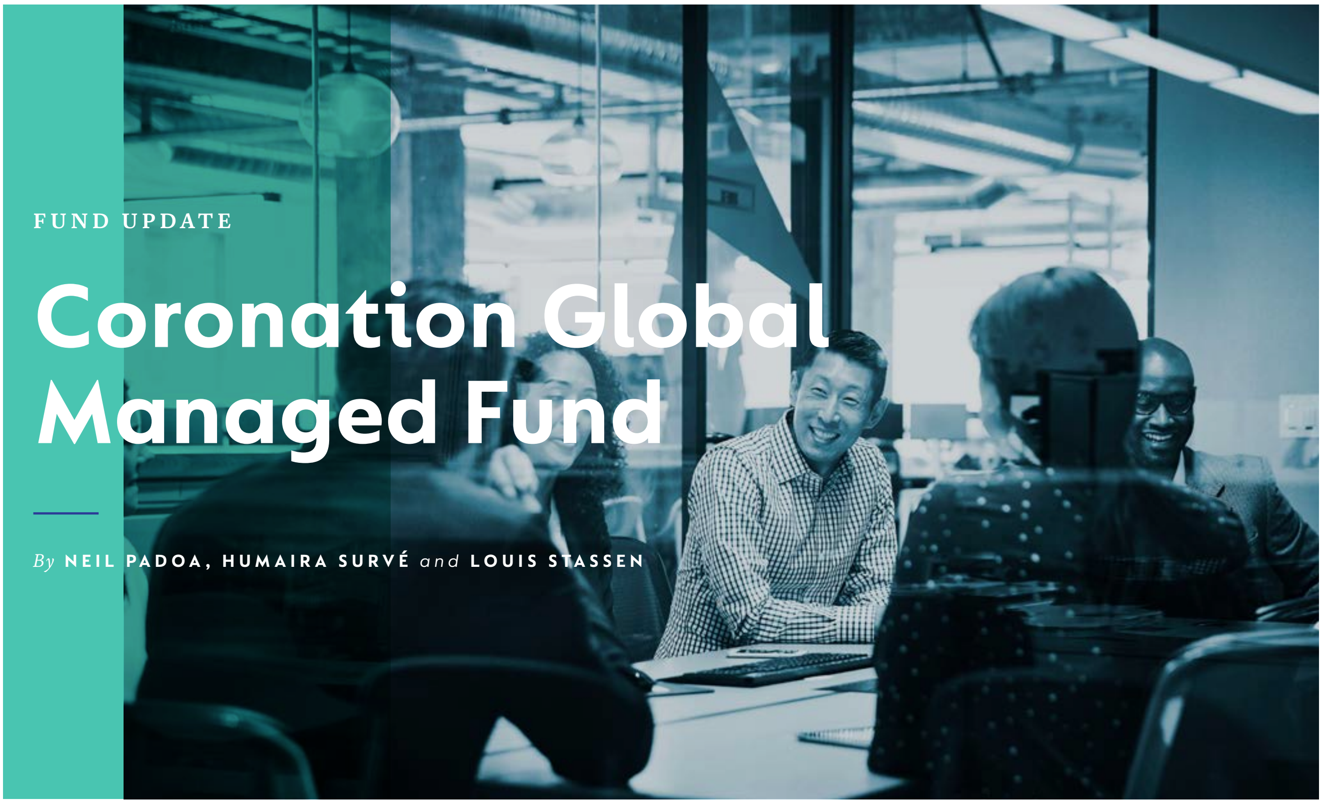
Amidst the enormous uncertainty of the year outlined above, Balanced Defensive has provided returns of 12.7% for the 12 months, well ahead of its target of inflation +3%. Pleasingly, it has also >

exceeded its target over all meaningful long-term time periods. Capital Plus has provided returns of 16.0% over the same period, well ahead of its target of inflation +4%. While it is still behind its target return over longer time horizons (five years plus), this year's performance has helped to close that gap. Both funds have benefited from their high exposure to risk assets, in particular SA equities, where both allocation and selection have contributed. We continue to think SA equities are attractively valued, with many investment opportunities, particularly in good quality global businesses and select defensive domestic companies.

Anglo American has been the top equity contributor to the funds' performance over the last year and is a top five equity holding. The share price has re-rated over the last five years on the back of rising commodity prices and good delivery by management on production growth, cost control and increasing shareholder returns in the form of dividends and buybacks. We are mindful that Anglo American is a cyclical commodity share and that current share prices reflect a positive outlook. We still think valuations are supportive, but will adjust the position sizing as the margin of safety decreases.

Balanced Defensive and Capital Plus have allocations of 44% and 28.1% to domestic fixed income instruments, respectively, with the largest exposure being domestic bonds. Domestic government bonds continue to offer very high real yields, but one needs to be mindful of longer-term fiscal pressures that could impact returns. With the funds' full exposure to risk assets via equities, we have purposely tried to limit duration risk on our fixed income selection. We have managed to do this and still have fixed income exposure that provides a healthy yield ahead of our target.

Both Balanced Defensive and Capital Plus have delivered commendable performance over the last year, comfortably meeting their mandates. This has been achieved by having a considered mix of income and growth assets and a judicious approach to instrument selection. We are confident that the consistent application of this approach will allow us to deliver on their respective CPI +3% and CPI +4% mandates over the medium term. +



FUND UPDATE

Coronation Global Managed Fund

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

Neil is Head of Global Developed Markets and has 14 years of investment experience.

Humaira is a portfolio manager with 10 years of investment experience.

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

GLOBAL EQUITY MARKETS ended the year on a high note, advancing 6.7% and bringing the gain for 2021 to 18.5%. Within equity markets, the S&P 500 Index bested the rest of the world by the largest margin in two decades. A specific sub-set highlights the gap: the S&P500 Index returned 28.7% in 2021 compared to the MSCI Emerging Markets Index, which declined 2.5%. As a result of sustained outperformance, the US now represents over 60% of the MSCI All Country World Index, up from 45% in the early 2010s. Global bond markets fared less well than equities as inflation fears picked up and investors began to price in a series of rate hikes. The Bloomberg Barclays Global Aggregate Bond Index was negative for the quarter, bringing the full-year decline to -4.7%. According to LPL Research, 2021 ranked the third-worst year for US bonds in four-and-a-half decades.

For the Fund, 2021 was a story of two halves: a solid first six months followed by a weak second half. Despite being well positioned from an asset allocation point of view, with an overweight position in equities, no exposure to longer-duration developed market government bonds and a healthy allocation to commodities, stock selection disappointed. The Fund returned 0.5% for the quarter and 2.1% for the year. This is the second-worst relative performance versus the benchmark since the Fund's inception over 10 years ago. We're disappointed with these returns, and would like to apologise to investors for this underperformance. We do, however, remain confident about the current Fund positioning and are encouraged by the potential future upside from the assets that we own in the portfolio.

With regards to stock selection, four areas are worth highlighting:

1. Chinese equities;
2. US cable stocks;
3. Businesses impacted by Covid-19, which should benefit from economies normalising (the so-called re-opening stocks); and
4. Not owning certain mega-caps like Apple (current market cap $2.8 trillion) and Nvidia (current market cap $675 billion), which returned 35% and 125%, respectively, for the year.

So how have we responded? To jump to the answer first, all three of the main detracting 'themes' remain meaningful holdings for the portfolio today. However, the weights, and in some cases the composition, of each theme have changed as specific stocks were either bought or sold based on a reassessment of their relative risk-reward. For example, in Chinese equities, we added to JD.com while reducing Alibaba. We discussed China in depth in this Corospondent article and in the third quarter of 2021's (Q3-21) commentary, while US cable stocks were covered in the Q1-21 commentary (both of which are available on our website). >

This quarter, we will focus on Airbus – the comments below are specific to Airbus, but the market seems to be focused on near-term disruptions as opposed to long-term earnings power, which is a common theme across many businesses that Covid-19 is impacting. We think this dynamic is creating an interesting opportunity in select businesses.

The fourth quarter of 2021 was eventful for Airbus, as tends to be the case seasonally. The stock underperformed this quarter due to the emergence of the Omicron variant and the ensuing increased travel restrictions across different regions. Some airlines revised near-term plans in an already weak late-autumn flying schedule, although the pace of new customer bookings was relatively resilient.

The market was also somewhat captivated by whether Airbus would make its annual delivery target of 600 aircraft in 2021. At the time of writing, the company has not yet released official figures, but it has reached the desired number for the year, according to the press. The late drive to achieve delivery targets is an annual fascination for some market participants, but we view it as noise and observe it with indifference, other than for the potential buying opportunities it could present. The company has aimed to make its delivery plan less seasonal, but Covid-19 disruptions have set back that intention. Either way, demand for new aircraft is determined by long-term fundamentals; while supply is affected by minor production issues that frequently occur due to the aerospace supply chain's complexity, but tend to be resolved in a matter of weeks or a few months. The lumpiness of monthly deliveries is, therefore, largely irrelevant to the intrinsic value of Airbus, despite the occasional severity of share price moves.

The most important long-term debate among investors and industry participants is about whether Airbus can or should increase its very successful narrow-body aircraft (the A320neo family) production rate from the current level of mid-40 units per month to a record more than 70 by around mid-decade. A320s are the company's most important models, contributing almost the entirety of the commercial division's earnings before interest and taxes, and even when other programmes' profitability ramps up, will be making up at least three-quarters of the total. Unnerved by naturally pessimistic views on the production ramp-up issue by lessors and aircraft engine original equipment manufacturers, the market seems to be pricing a figure in the mid-50s. However, our analysis on demand and market share trends suggests that a rate close to 70 is feasible, and there is further upside towards the end of the 2020s.

Various pieces of anecdotal evidence support this (e.g. Allegiant Air's CEO in the US recently noted that there were no free A320 production slots until 2026-2028). We continue to be bullish on Airbus' bolstered strategic position in the global duopoly coming out of the Covid-19 crisis, which, combined with a strong balance sheet sets it up well for the next decade. We expect this to translate into strong earnings and free cash flow growth over several years and believe the shares remain attractively valued.

Liberty Media Corporation, which owns Formula 1 (F1), was a positive contributor. F1 is the third or fourth most-watched event on earth. So, no doubt, many readers would have witnessed the dramatic season finale where the two leading drivers (Lewis Hamilton and Max Verstappen) began the final race of 2021 tied on points. It was a high-stakes race of winner-takes-all, and in a turn of events resembling a Hollywood-scripted drama, it all came down to the final lap. Excitement, drama, emotion, history and fierce rivalry such as this draw the crowds both track-side and on TV (and increasingly, direct to the consumer on any device too), and are exactly what makes live sports valuable.

We think F1 is a unique asset, and in the hands of Liberty (with John Malone as Chairman), the company has been undergoing a transformation over the last few years. While Covid-19 heavily impacted the last two seasons, if economies and societies start to normalise (as we expect), combined with the changes Liberty has been making, the value of this franchise should become evident. F1 has high barriers to entry; is currently under-monetised yet still exhibits fantastic economics, with high margins and limited capex requirements resulting in strong cash conversion; has a dynamic new CEO Stefano Domenicali (with a background as CEO of Lamborghini and at F1 with Ferrari); optionality from mergers and acquisitions; and higher broadcast fees.

Looking at asset classes for the quarter, commodity holdings, infrastructure positions and gold were the primary contributors to returns. At quarter-end, the Fund was positioned as follows:

- 62% effective equity;
- 6% in listed infrastructure assets;
- 8% in commodity-related assets split roughly equally between gold (the metal) and diversified miners;
- 7% in high-yield fixed income; and
- 8% in investment-grade fixed income.

The remaining 9% is invested across a range of other assets.

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Our assessment of what most businesses in the portfolio are worth is largely unchanged and, with many of their prices now lower, the Fund's price-to-value gap has widened and expected returns are now higher. In contrast, the market has increased at a rate in excess of the underlying earnings growth, and such a re-rating would usually be a headwind to future returns. We are, therefore, cautiously optimistic about the returns embedded within the portfolio.

Thank you for your continued support and interest in the Fund. ✚

FUND UPDATE

Coronation Global Optimum Growth Fund

By **GAVIN JOUBERT** *and* **MARC TALPERT**

Gavin is Head of Global Emerging Markets and has 23 years of investment experience.

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

THE FUND ROSE 5.8% in the fourth quarter of 2021 (Q4-21). It was encouraging to see a quarter of strong absolute returns, but the 12-month return of 2.9% was disappointing against a backdrop of buoyant markets. However, we do believe that the collection of assets held by the Fund can deliver compelling long-term risk-adjusted returns to achieve its goal of compounding capital well ahead of inflation. Over the past five years, the Fund has generated a positive return of 12.3% p.a., 15.3% p.a. over 10 years and 14% p.a. since its inception over 20 years ago.

Even though 2021 was a year during which the headline performance of markets was strong, it doesn't tell the full story, as a small number of large stocks drove overall market returns. This is best illustrated by the performance of the Nasdaq, which delivered a very strong total return of 27.5% in 2021, but 40% of all companies in the Index are trading at 50%, or more, below their 52-week highs. In fact, the Nasdaq's returns have been driven largely by five large-cap technology stocks (Apple, Alphabet, Microsoft, Nvidia and Tesla). There has thus been a material market correction in certain pockets of the market, which is being overshadowed primarily by the strong performance of large technology companies.

This market correction has played out mainly in stocks of the companies that are loss-making, had high starting valuations and are characterised as long-duration businesses owing to their terminal value making up the bulk of the business value, as opposed to current free cash flow and earnings. We retain a cautious approach to these types of businesses. But at the same time, we are looking for opportunities to emerge in this category due to what can be described as synchronised and indiscriminate selling of all assets that fall into this category.

We continue to focus significant time on China, with the Fund having approximately 15.5% exposure to Chinese assets. We continue to feel these assets are very attractively priced, but acknowledge the risks, with consistent work being done to keep abreast of the regulatory environment and its long-term impact on the companies owned by the Fund. Prosus (indirect exposure to Tencent) and JD.com continue to make up more than 50% of the Fund's Chinese exposure and 9% of the portfolio in total.

During the quarter, the largest positive contributors were Capri Holdings (+42%, 0.82% positive impact), AngloGold Ashanti (+39%, 0.67% positive impact), Prosus (+11%, 0.60% positive impact) and Centene (+41%, 0.5% positive impact).

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The largest negative contributors were Auto1 Group (-36%, 0.34% negative impact), Trip.com (-15%, 0.24% negative impact) and PagSeguro (-48%, 0.21% negative impact).

Auto1 has declined nearly 70% since its IPO in February 2021. The business is involved in the buying and selling of cars by using the internet and technology to reduce friction in the consumer experience. Notwithstanding the disappointing stock performance, the business has continued to deliver operationally, with its legacy dealer business (C2B) continuing to grow (revenue is up 49% in the past year) and its retail (C2B2C) segment powering ahead (units sold are up 4.7 times and revenue is up 412%). This good operational performance has been overshadowed by competition concerns. However, it should be noted that the industry remains highly fragmented, with Auto1 representing only c.1% of the market, with the shift to online car buying still in its infancy. This is a long-duration asset, but one that is solving a real problem and dramatically improving the consumer experience, and which we think is attractively valued, with significant potential upside at current levels.

Trip.com is the largest online travel agency in China but still only has a 14% share of the travel market, which continues to shift from offline to online booking channels. Its business has been negatively impacted by the outbound travel market (c.30% of group revenue in 2019) and by effectively being shuttered for nearly two years, along with haphazard lockdowns in China impacting domestic travel. Trip.com has tried to navigate these challenges by investing more in its domestic offerings, which has resulted in the company gaining market share, as many travel peers have struggled in a tough operating environment. While Chinese outbound travel re-opening is highly uncertain, it should be noted that roughly two-thirds of pre-Covid-19 outbound travel was to Hong Kong and Macau, which could normalise in the not-too-distant future, even if other outbound travel takes much longer to do so. Trip.com has also done a good job in optimising its cost structure and thus should achieve structurally higher margins once revenue recovers to 2019 levels.

PagSeguro is a business in Brazil that initially started out as a disruptive merchant acquirer with a focus on smaller businesses that it enabled to accept non-cash payments. It has since added additional financial service offerings by leveraging the merchant-acquiring relationship. The business now has a banking licence and is taking deposits, which should create stickier customer relationships, with the deposit base reducing the company's funding costs. The share has recently come under pressure due to general macro concerns in Brazil, along with rising interest rates, which negatively impact the income PagSeguro earns in certain parts of its business. Notwithstanding these headwinds, the business continues to execute well, with operational results being encouraging, and with the company still going after a very large financial services profit pool that is ripe for disruption. The share is down nearly 60% from its peak, yet the fundamentals of the business are largely unchanged, making PagSeguro a very attractive investment, in our view.

The Fund ended the quarter with 78.5% net equity exposure, slightly higher than the exposure on 30 September 2021, as we bought attractive stocks selectively.

Our negative view on global bonds remained unchanged, as a large portion of developed market sovereign bonds offers negative yields to maturity. The follow-on effect is that most corporate bonds also offer yields that do not compensate for the risk undertaken, and which are increasing due to inflation and rising interest rates. However, we continued to buy South African (SA) government bonds in the quarter, which now represent 4.83% of the Fund. Our view on the SA fiscal situation has improved somewhat, which, coupled with the fact that we are receiving a c.10% yield on these bonds, is attractive in our view. Furthermore, considering that inflation within SA remains controlled, the real yields on SA government bonds are the highest in the world.

The Fund continues to have a physical gold position of 3.26%, a 2.57% holding in AngloGold Ashanti, and a 0.6% holding in Gold Fields. The gold price finished the year down approximately 3.5% in US dollars, but we continue to hold the position for its diversifying properties in what we characterise as a low-visibility world, with increasingly visible inflation risks. AngloGold Ashanti rebounded somewhat in the quarter, as detailed above (+39%), but remains attractive due to the likelihood of operational improvements under the newly appointed CEO, which should lead to improved business performance, with the business trading on an eight times price earnings multiple. The balance of the Fund is invested in cash, largely offshore.

As the outlook for the future remains uncertain and hard to predict, we take comfort in the fact that 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. Also, because the Fund >

is a multi-asset flexible fund, we have access to additional tools with which to take advantage of dislocations in the market, along with risk control measures such as put options. Current Index put-option exposure is 6.3% effective and 27.6% nominal as a percentage of the Fund, which will shield the Fund somewhat in the event of a significant drawdown in equity indices.

Notable buys/increases in position sizes during the quarter were ASML and Centene.

ASML is a semiconductor equipment supplier, making lithography machines that are critical to the production of computer chips. It is arguably the most important company for technological innovation, as its machines are a key enabler in driving continued semiconductor innovation. The company has created a monopoly market position in extreme ultraviolet (EUV) machines, which are needed to produce leading-edge computer chips. This provides the business with significant pricing power, with an EUV machine selling for approximately €130 million each, with future iterations continuing to increase in price due to the value they provide.

The business is supported by a structural growth trend as the demand for semiconductors remains extremely robust, with technology proliferating every aspect of human life. Another unique aspect of ASML's business is revenue visibility due to the business being intertwined with its customers and thus having sight of the latter's capacity roadmaps. This is reflected in the fact that, at ASML's most recent investor day, the company gave scenario guidance to 2030. ASML's near-term earnings multiples are high, but it should continue to grow revenue and earnings at double-digit rates into 2030 while generating a return on capital of more than 20%, driving a fairly rapid unwinding of the high near-term multiple.

Centene is one of the top five US healthcare insurers (managed care), with a focus on Medicaid in particular (government-sponsored healthcare specifically for lower-income individuals) where it is the no. 1 player. This business continues to grow structurally as Medicaid spend shifts from fee-for-service (payments directly to service providers) to managed care (payments to companies like Centene). Historically, Centene's operational performance has been below par, making them a possible target for a takeout, and it has also resulted in an activist shareholder becoming involved. This involvement has already resulted in a recent announcement of five new directors to the board.

Centene has laid out what it calls a 'value creation plan', which details how the business will take EPS from around $5.10 in 2021 to around $7.65 in 2024 due to a range of factors, including platform centralisation, operational efficiencies, margin improvement in certain products, share buybacks and debt paydown. If achieved, this will mean earnings growth over the next three years of 14.4% p.a. Centene trades on 14 times this year's (2022) earnings, which makes it very attractive in our view, given its prospects.

The Omicron variant resulted in renewed worries surrounding Covid-19 and its disruptive effect, but initial data seems to indicate that it is milder but spreads quicker. There remains risk to this view as additional studies are carried out across the world, and thus increasing vaccine coverage remains the best tool to fight Covid-19, especially in lower-income countries that have materially lower vaccination rates, creating a continued risk that further variants develop as the virus continues to spread within communities.

Against this uncertain backdrop, we remain positive on the outlook for the Fund, which has been built bottom up, with a collection of attractively priced assets to provide diversification in order to achieve the best risk-adjusted returns going forward in a variety of future scenarios. ✚

FUND UPDATE

Coronation Global Emerging Markets Fund

By **GAVIN JOUBERT** *and* **SUHAIL SULEMAN**

Gavin is Head of Global Emerging Markets and has 23 years of investment experience.

Suhail is a global emerging markets portfolio manager with 20 years of investment experience.

THE FUND RETURNED -5.79% during the quarter ended December 2021, 4.48% behind the benchmark MSCI Emerging Markets Total Return Index, which returned -1.31% for the period. For the year as a whole, the Fund returned -14.75%, 12.21% behind the benchmark return of -2.54%. This has been the worst (relative) performance year for the Fund since inception, and we apologise to investors for this underperformance. While a year like this is both unpleasant and uncomfortable, it is also not totally out of line with the Fund's history: in 2018, the Fund was 11.66% behind the market (this was followed by 19.76% outperformance of the market in 2019); and in 2015, while the Fund ended the year 6.69% behind the market, there was a point during the year when it was 12% behind on a rolling one-year basis. Calendar year 2015, in turn, was followed by two successive years of 1.0% to 2.5% p.a. outperformance. Over three years, the Fund has now outperformed the market by 2.24% p.a., over five years it is 1.73% p.a. behind and over 10 years the Fund has still outperformed by 0.04% p.a., in spite of the recent tough period. Outperformance since inception stands at 1.22% p.a. over 13.5 years.

The reasons behind the Fund's sometimes uncomfortable swings in relative performance are multifold, with the biggest factors being the high active share (over 80%), off-benchmark exposure typically around 40% since inception, a concentrated portfolio (50-60 stocks), and lastly, the fact that, given our long-term (five year+ time horizon) valuation-driven approach, we are often invested in a number of companies that are disliked or out of favour. Examples of this today would include JD.com (and China internet more broadly), Magnit and AngloGold (all top 10 positions), as well as several others. We also still own 15 of the 20 largest individual stock detractors of 2021 – in other words, over the long term, we believe a large part of 2021's underperformance will be recovered. The weighted average upside of the Fund today is around 70% (well north of the historical 45%) and the Fund's weighted five-year internal rate of return is 20% p.a. (also much higher than where it has been historically).

For the quarter under review, the biggest positive contributor to alpha was AngloGold, up 31% for a +67 basis point (bp) contribution to relative performance. Naspers and Prosus contributed +46bps, while NetEase (Chinese gaming) contributed +34bps. The final two material positive contributors were LVMH (global luxury) and Anglo American (diversified mining). These contributed a combined +61bps, split fairly evenly.

As one would expect in a very negative quarter, there were several material detractors. The biggest among these was Sendas, a Brazilian cash-and-carry retailer and overall the second-largest food retailer in the country, which returned -32% and cost 82bps of relative performance.

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Aside from general weakness in the Brazilian market, Sendas' share price reacted poorly to the group's plan to buy 71 underperforming hypermarket stores from CBD, its former holding company, with a view to turning them around. In addition to the high price tag of R$5.2 billion (c.$1 billion), the lack of shareholder vote when the parties are related (French group Casino is the largest shareholder in both Sendas and Assai) was not well received by investors. We lobbied the board to put this to a vote but were unsuccessful, as the group argued the valuation and due diligence were done by independent parties that ruled that the transaction was priced fairly and in the interests of all parties.

Despite our unhappiness with certain aspects of this transaction, we understand and agree with the strategic rationale (a significant immediate addition to the store base with generally attractive sites that otherwise would take many years to achieve), and we have retained the position in Sendas. In our view, it remains a very attractive asset (very well run, with a resultant return on invested capital of over 25% and in a category that is gaining market share), on a very attractive valuation (around 12 times 2023 earnings).

Two other Brazilian stocks made up the next biggest detractors. PagSeguro (card acquisition and digital banking) halved in the period and cost 74bps, while XP Inc. (securities broking and wealth management) fell 29% and cost 48bps. Rounding up the top five detractors were Yandex (Russian search, ride hailing and general tech), which cost 44bps and Trip.com (Chinese online travel agency), which cost 37bps.

Ordinarily we would spend much of this piece discussing what went right and wrong in the quarter; however, it is more useful to rather look at the year as a whole to understand why the Fund underperformed by such a significant margin. While in summary it was simply a year of poor stock selection, one can break down the drivers of underperformance in 2021 into five categories that each played a role.

1. **China education**: The single biggest impact on relative performance came from the Chinese tutoring/education stocks. These cost the Fund around -3% of relative performance, mostly concentrated in New Oriental Education. The key driver here was the government effectively converting the industry into 'not for profit'. This massive regulatory change was unprecedented and more far-reaching than we had anticipated.
2. **China internet**: Despite Tencent Music Entertainment (TME) being the second-largest detractor for the year (-1.5% impact), and both JD.com (-70bp impact) and Autohome (-51bp impact) also being top 10 detractors, the impact of the China internet sector was not as material as one would intuitively expect. This sector cost the Fund around -1% of performance, considering the performance of the stocks held (which mostly did poorly) and the stocks not held or underweight (which boosted performance). The Fund has around 24% exposure either directly or indirectly (via a fair share of Naspers and Prosus) to China internet, reflecting our conviction on the potential opportunity in several names in this sector, particularly JD.com.
3. **Country weights**: The Fund has no exposure to Saudi Arabia, a market that was up 36% (in US dollars). This cost 1% of relative performance. The Fund also has less in India and Taiwan relative to their benchmark weights, as we saw better opportunities elsewhere from a bottom-up perspective. Unfortunately, these markets did very well (up +/- 25% in US dollars in 2021), and this cost the Fund in relative performance. Some of the stocks we held in India did not perform as well as the Indian market as a whole, which further exacerbated the underweight. The combined impact of India and Taiwan on the Fund was -4%. While the Fund comprises bottom-up stock picks, on occasion the country dynamics can work against it, as was clearly the case in 2021.
4. **Stocks not owned**: The Fund holds less stocks through the cycle compared to a benchmark of over 1 550 stocks. This concentration versus the diluted benchmark is a deliberate part of our process of selecting the best investment opportunities on a risk-adjusted basis within our investment universe. Generally, the stocks we don't own have no material negative impact on performance; often the impact is positive, as the bulk of the benchmark does poorly. In 2021, however, these zero weights cost the Fund just over 3% relative performance. This is an abnormally large amount and proved a difficult headwind to overcome.
5. **Low cyclical sector exposure**: Cyclical industries like energy, basic materials, industrials and banks did relatively well in 2021. We typically do not have as much in these stocks relative to their weight in the investment universe, as we prefer less cyclical assets/'better' businesses. The overall impact on relative performance from having a lot less cyclical exposure was c.-2%.

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PORTFOLIO ACTIVITY

There were several new buys in the quarter, with the largest new buy being Petrobras (1.7% of the Fund at year-end), the Brazilian oil and gas group that trades on four times free cash flow and offers a compelling 20%+ dividend yield. This very attractive valuation provides some comfort in the event that the left-wing former president Lula da Silva returns to power in elections later this year.

The second new buy of note (1% position) was Porsche, the holding company with its stake in Volkswagen (VW) being its main asset. VW's emerging market exposure is over 50%, with China being the biggest part of this through both direct sales and joint ventures (accounted for as associates). The Dieselgate scandal of 2015 is largely behind VW and the firm has made great strides in developing its electric vehicle range, which is arguably among the most impressive of the legacy car manufacturers. Of great attraction to us is the high premium share of profits, with the Audi and Porsche brands making up half of operating profit. VW, with a large part of its earnings coming from premium brands, trades on a lowly six times 2022 earnings, with an attractive 4.5% dividend yield, and Porsche, in turn, trades at a discount to this, given the discount to the value of its stake in VW. Although not strictly comparable, a pure luxury car player like Ferrari trades on more than 40 times forward earnings.

The Fund also purchased a 1% position in Taiwan-based MediaTek, a well-diversified fabless (it designs chips but outsources production) semiconductor company. Revenue at MediaTek has grown 19% p.a. cumulatively over the last 10 years, making it the fourth-largest in the world and the largest mobile chip system vendor by volume, overtaking Qualcomm.

MediaTek has navigated the evolution of demand for its products very well, with management having steered the company through multiple product transitions, from optical disk drivers to TVs, feature phones, smartphones and others. MediaTek trades on 15 times forward earnings and generates returns on investment of 25%. With free cash flow conversion of over 100%, it also offers an attractive 6% dividend yield.

Other new buys worth noting, but all smaller so far (60-90bps), are Southeast Asian gaming and ecommerce operator SEA Ltd, Chinese sportswear retailer Anta, Eastern European low-cost airline Wizz Air and Russian lender TCS Group. In the case of all four of these stocks, we already covered them but didn't own them, largely due to valuation, and it was sharp price declines that brought them into buying range: SEA from a $365 share price peak to the current $195 price, Anta from a HK$190 peak to HK$107, Wizz Air from £55 to £40 and TCS from $120 to $79.

To fund the above purchases, a variety of positions were sold. Most notably, we took the decision to divest entirely from tobacco, which was around 3.5% of the Fund in total in four holdings at the beginning of the quarter. Three other small positions were also sold entirely, namely the insurer Prudential plc (consolidating the pan-Asian insurance exposure in AIA), Turkish hard discount retailer BIM (Turkey is uninvestable for now, in our view, given its unconventional monetary policy), and the Chinese online vehicle portal Autohome (to add more to higher-conviction China internet stocks without increasing overall China internet exposure). ✚

Please note that the commentary is for the US dollar retail class of the Fund. For detailed information on this Fund and our range of unit trust funds, including highest and lowest annual return ranges, please visit our fund centre on www.coronation.com.

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 C-SWIX†
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	95% 5%	55.4% 44.6%	34.5% 65.5%	24.9% 75.1%	0.2% 99.8%
LAUNCH DATE	Jul 2001	Mar 2007	Jul 2001	Apr 1996	Oct 2000
ANNUAL RETURN (Since launch)	9.7% 7.4%†	9.3% 5.7%†	11.5% 5.6%†	14.1% 13.1%†	17.1% 13.7%†
QUARTILE RANK (Since launch)	2nd	1st	3rd	1st	1st
ANNUAL RETURN (Last 10 years)	7.9% 5.8%†	9.0% 5.0%†	8.5% 5.0%†	11.1% 12.0%†	11.6% 11.8%†
STANDARD DEVIATION (Last 10 years)	2.2% 0.3%†	5.6% 1.3%†	7.1% 1.3%†	9.6% 8.5%†	14.0% 13.5%†
FUND HIGHLIGHTS	The Fund remains the top-performing fund in its category since launch in 2001 and outperformed cash by 2.4% over this period.	Outperformed inflation by 3.7% p.a. (after fees) since launch, while producing positive returns over 12 months more than 98% of the time.	The Fund outperformed inflation by 5.9% p.a. (after fees) since launch in 2001.	No. 1 balanced fund in South Africa since launch in 1996, outperforming its average competitor by 2.0% p.a.. Outperformed inflation by on average 8.0% p.a. since launch and outperformed the ALSI on average by 1.0% p.a (since launch).	The Fund added 3.4% 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 R2.8 million by end-December 2021. The Fund is a top quartile performer since launch.

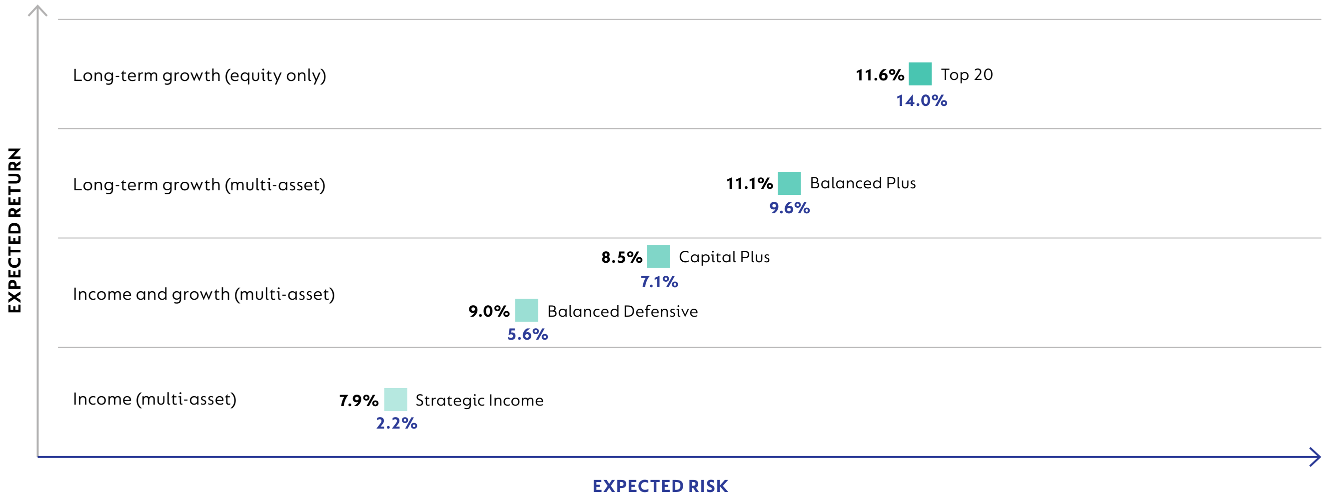
[1] *Income versus growth assets as at 31 December 2021. Growth assets defined as equities, listed property and commodities (excluding gold).*

For detailed information on our range of unit trust funds, including highest and lowest annual return ranges, please visit our fund centre on www.coronation.com.

Figures are quoted from Morningstar as at 31 December 2021 for a lump sum investment and are calculated on a NAV-NAV basis with income distributions reinvested.

RISK VERSUS RETURN

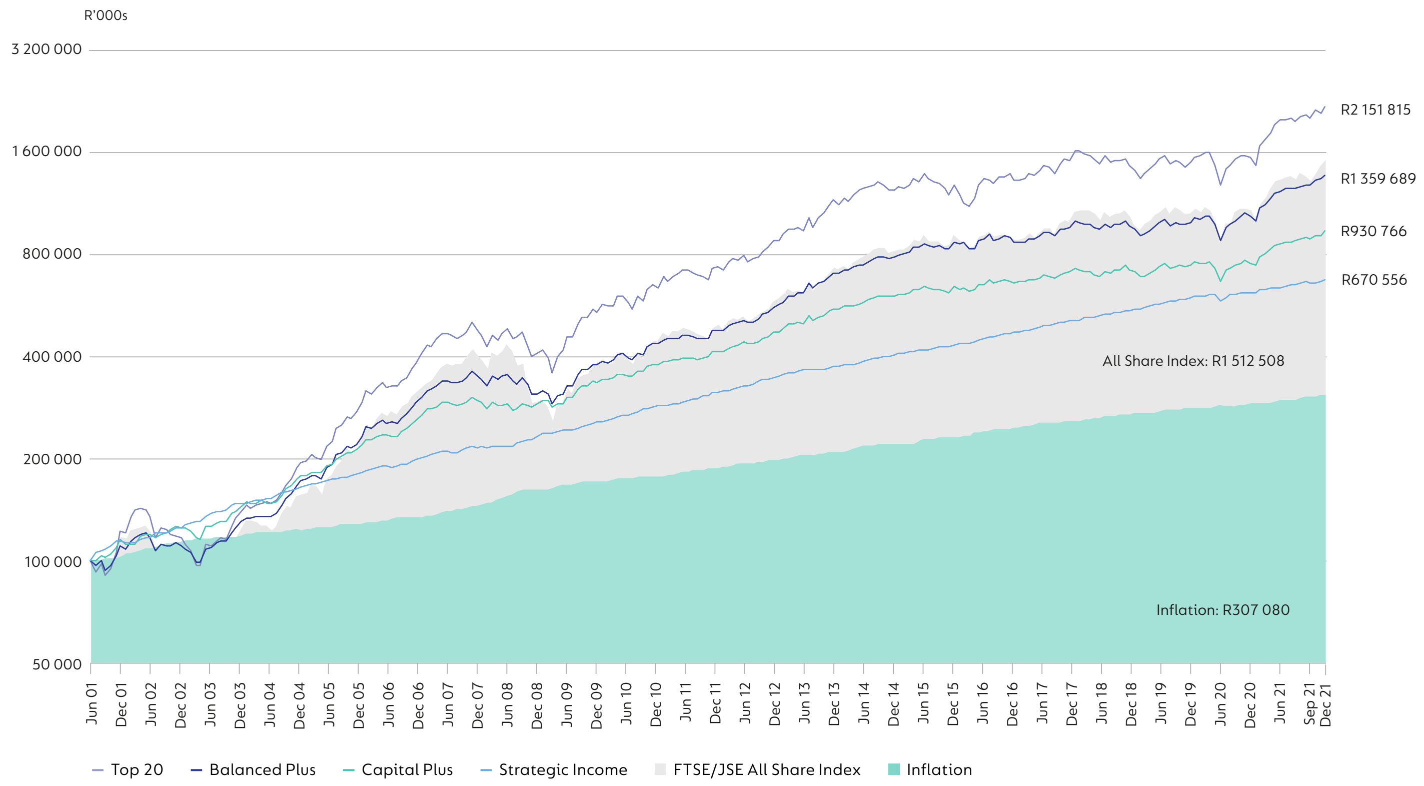
10-year annualised return and risk (standard deviation) quoted as at 31 December 2021.
Figures quoted in ZAR after all income reinvested and all costs deducted.



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 31 December 2021. 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 globally diversified portfolio with exposure to both developed and emerging markets across multiple asset classes. Our intent is to provide competitive after-inflation returns 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	98.2% 1.8%	53.4% 46.6%	19.2% 80.8%	17.4% 82.6%	0.4% 99.6%
LAUNCH DATE OF OLDEST FUND	Jan 2012	Sep 2008	Oct 2009	Apr 1999	Apr 2015
ANNUAL RETURN[3] (Since launch)	2.3% 0.9%†	5.0% 0.8%†	6.6% 7.7%†	9.3% 7.3%	6.3% 10.6%
QUARTILE RANK (Since launch)	–	1st	2nd	1st	3rd
ANNUAL RETURN[3] (Last 5 years)	1.8% 1.4%	4.2% 1.4%	6.6% 10.2%	8.9% 9.4%	10.0% 14.4%
ANNUAL RETURN[3] (Last 10 years)	2.3% 0.9%	4.0% 0.9%	6.8% 8.2%	7.7% 6.5%	- -
QUARTILE RANK (Last 5 years)	–	1st	3rd	1st	3rd
FUND HIGHLIGHTS	Outperformed US dollar cash by 1.4% p.a. (after fees) since launch in December 2011.	The Fund has outperformed US dollar cash by 4.2% p.a. (after fees) since launch in 2008.	Ranks as a top-quartile 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 continues to seek attractively valued shares to maximise long-term growth.

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 31 December 2021 (for US dollar funds). Growth assets defined as equities, listed property and commodities (excluding gold).

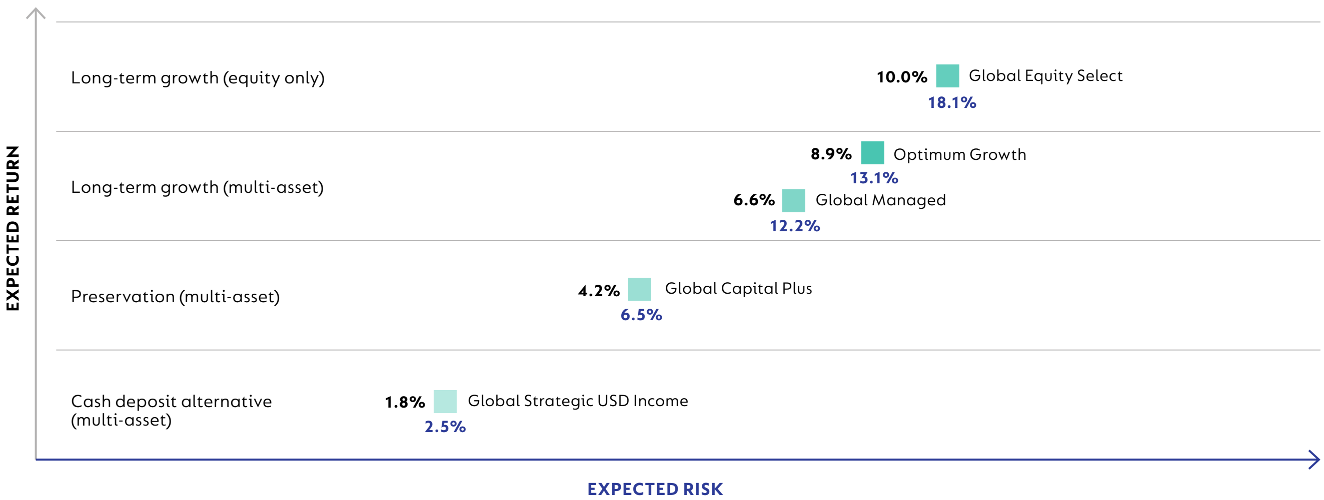
3 Returns quoted in US dollar for the oldest fund.

For detailed information on our range of unit trust funds, including highest and lowest annual return ranges, please visit our fund centre on www.coronation.com.

Figures are quoted from Morningstar as at 31 December 2021 for a lump sum investment and are calculated on a NAV-NAV basis with income distributions reinvested.

RISK VERSUS RETURN

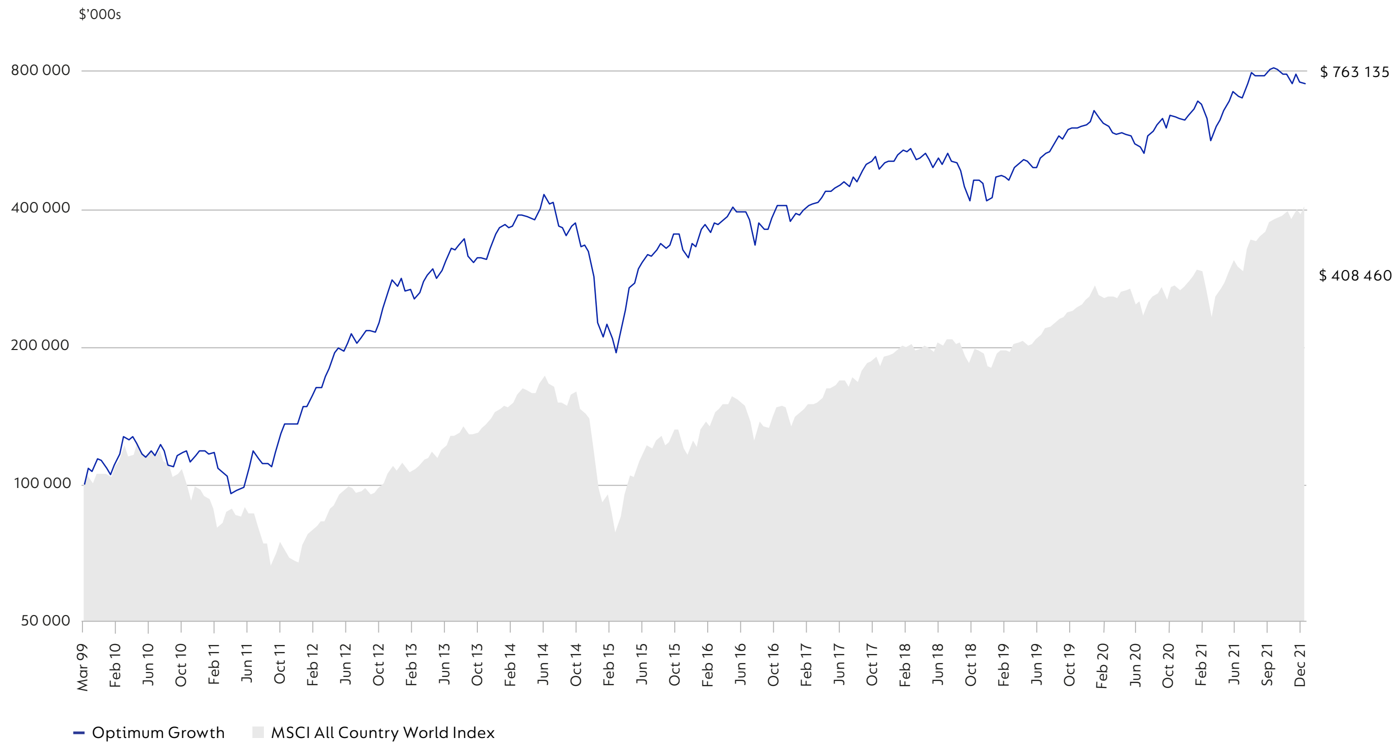
Five-year annualised return and risk (standard deviation) quoted as at 31 December 2021. Figures quoted in USD (for the oldest fund) after all income reinvested and all costs deducted.



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.



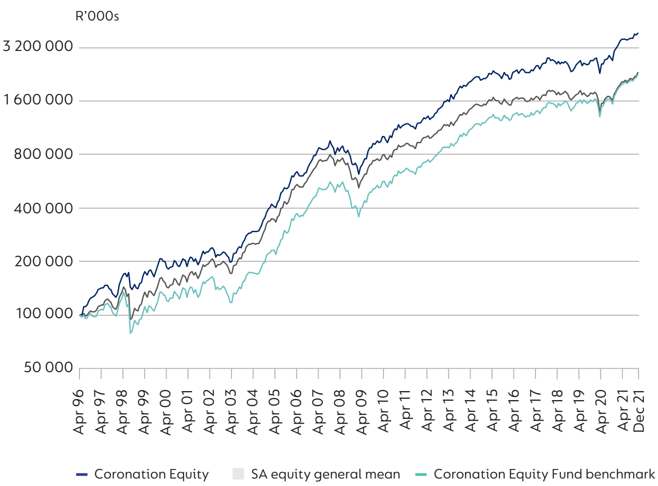
Source: Morningstar

Long-term investment track record

CORONATION EQUITY RETURNS VS AVERAGE COMPETITOR[1]

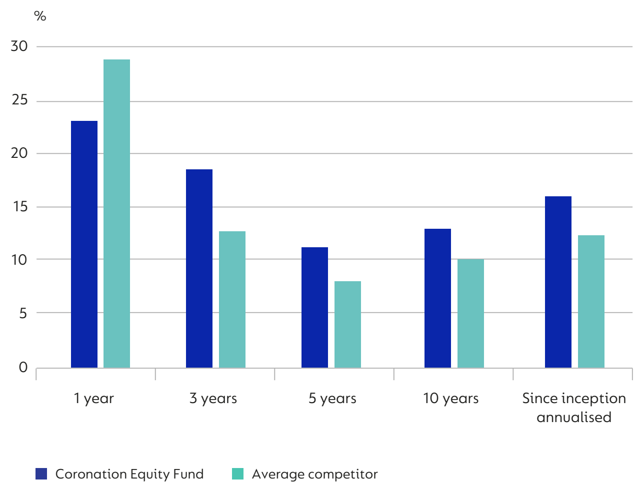
10-YEAR ANNUALISED RETURNS	CORONATION EQUITY	AVERAGE COMPETITOR	OUTPERFORMANCE OF AVERAGE COMPETITOR
2006	19.38%	17.09%	2.30%
2007	21.45%	19.23%	2.22%
2008	17.62%	18.47%	(0.84%)
2009	16.53%	16.68%	(0.15%)
2010	19.59%	19.14%	0.45%
2011	18.03%	16.98%	1.05%
2012	21.12%	18.94%	2.19%
2013	21.60%	18.68%	2.92%
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%
2020	10.48%	7.10%	3.38%
10 years to December 2021	12.46%	9.77%	2.69%
ANNUALISED TO 30 SEPTEMBER 2021	**CORONATION EQUITY**	**AVERAGE COMPETITOR**	**OUTPERFORMANCE**
1 year	22.13%	27.63%	(5.50%)
3 years	17.79%	12.22%	5.57%
5 years	10.83%	7.80%	3.03%
10 years	12.46%	9.77%	2.69%
Since inception in April 1996 annualised	15.35%	11.85%	3.49%
Average outperformance per 10-year return			1.93%
Number of 10-year periods outperformed			14.00
Number of 10-year periods underperformed			2.00

CUMULATIVE PERFORMANCE



Source: Morningstar

ANNUALISED RETURNS TO 31 DECEMBER 2021



Source: Morningstar

An investment of R100 000 in Coronation Equity on 15 April 1996 would have grown to **R3 902 454** by 31 December 2021. By comparison, the returns generated by the Fund's benchmark over the same period would have grown a similar investment to **R2 281 947**, while the SA equity general sector would have grown a similar investment to **R2 320 880**.

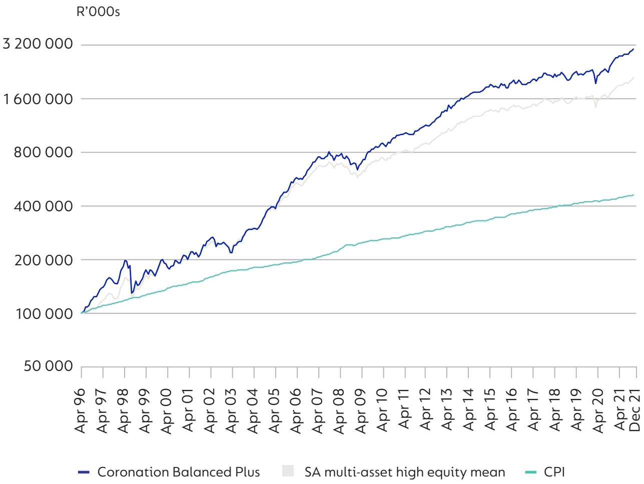
For detailed information on our range of unit trust funds, including highest and lowest annual return ranges, please visit our fund centre on www.coronation.com.

[1] Average of performance of the SA – Equity – General category, ex-Coronation Funds

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

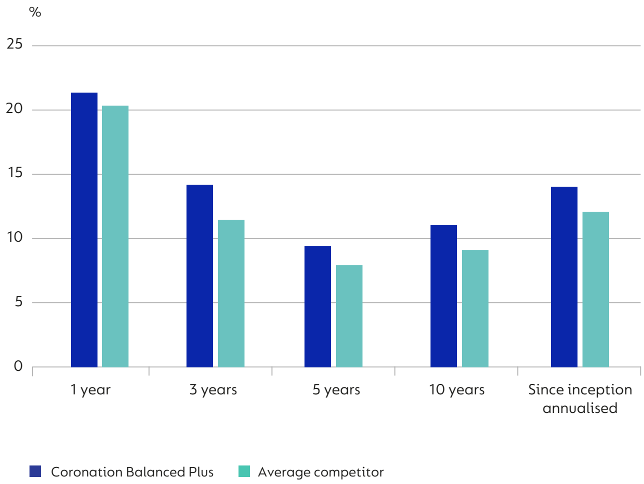
10-YEAR ANNUALISED RETURNS	CORONATION BALANCED PLUS	INFLATION	REAL RETURN
2006	18.33%	6.47%	11.86%
2007	17.81%	6.59%	11.22%
2008	16.96%	6.87%	10.09%
2009	15.69%	6.75%	8.94%
2010	17.20%	6.28%	10.93%
2011	15.78%	6.24%	9.54%
2012	17.85%	5.76%	12.09%
2013	18.63%	5.90%	12.73%
2014	16.58%	6.00%	10.57%
2015	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%
2020	9.66%	5.07%	4.58%
10 years to December 2021	11.08%	5.04%	6.04%
ANNUALISED TO 30 SEPTEMBER 2021	**CORONATION BALANCED PLUS**	**AVERAGE COMPETITOR**	**OUTPERFORMANCE**
1 year	21.48%	20.44%	1.04%
3 years	14.25%	11.53%	2.72%
5 years	9.50%	8.02%	1.48%
10 years	11.08%	9.18%	1.90%
Since inception in April 1996 annualised	14.15%	12.16%	1.98%
Average 10-year real return			8.59%
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%			7.00
Number of 10-year periods where the real return is 0% - 5%			2.00

CUMULATIVE PERFORMANCE



Source: Morningstar

ANNUALISED RETURNS TO 31 DECEMBER 2021



Source: Morningstar

An investment of R100 000 in Coronation Balanced Plus on 15 April 1996 would have grown to **R2 986 056** by 31 December 2021. By comparison, the SA multi-asset high-equity sector over the same period would have grown a similar investment to **R2 056 044**.

[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.*