# CORONATION SA INCOME FUND

Fund Information as at 30 April 2024

CORONATION

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## WHAT IS THE FUND'S OBJECTIVE?

SA Income Fund aims to achieve a higher return than a traditional money market or ultra-short duration income fund.

## WHAT DOES THE FUND INVEST IN?

SA Income can invest in South African bonds, fixed deposits, and other interest- bearing securities which have a fixed maturity date and either have a predetermined cash flow profile or are linked to benchmark yields.

The fund does not invest in any equity securities, real estate securities or cumulative preference shares. The fund will not invest in any assets deemed offshore for SARB reporting purposes.

The fund is mandated to use derivative instruments for efficient portfolio management purposes.

## IMPORTANT PORTFOLIO CHARACTERISTICS AND RISKS

Risk Profile

2/10
Conservative

Maximum growth/
minimum income exposures

- Growth Assets: 0%
- Income Assets: 100%

SA Income is tactically managed to secure an attractive return, while protecting capital. The fund's weighted average modified duration is limited to a maximum of two.

Its investments are carefully researched by a large and experienced investment team and subjected to a strict risk management process. The fund is actively positioned to balance long-term strategic positions with shorter-term tactical opportunities to achieve the best possible income.

While the fund is managed in a conservative and defensive manner, there are no guarantees it will always outperform cash over short periods of time. Capital losses are possible, especially in the case of negative credit events affecting underlying holdings.

## HOW LONG SHOULD INVESTORS REMAIN INVESTED?

The recommended investment term is six months and longer. Given its lack of exposure to growth assets, the fund is not suited for investment terms of longer than five years.

## WHO SHOULD CONSIDER INVESTING IN THE FUND?

Investors who

- are looking for an intelligent alternative to cash or bank deposits over periods from 6 to 36 months;
- seek managed exposure to South African income generating investments;
- believe in the benefits of active management within the fixed interest universe;
- do not have appetite for exposure to offshore assets;
- the fund is particularly suited to those who require exposure to South African interest bearing securities as part of a diversified portfolio.

## WHAT COSTS CAN I EXPECT TO PAY?

The annual management fee is 0.65%.

Fund expenses that are incurred in the fund include trading, custody and audit charges. All performance information is disclosed after deducting all fees and other fund costs.

We do not charge fees to access or withdraw from the fund.

More detail is available on www.coronation.com.

## WHO ARE THE FUND MANAGERS?

NISHAN MAHARAJ
BSc (Hons), MBA

MAURO LONGANO
BScEng (Hons), CA (SA)

## GENERAL FUND INFORMATION

| | |
|---|---|
| Launch Date | 29 November 2023 |
| Fund Class | A |
| Benchmark | Alexander Forbes STeFI Composite Index |
| ASISA Fund Category | South African – Interest Bearing – Short Term |
| Regulation 28 | Complies |
| Income Distribution | Quarterly (March, June, September, December) |
| Investment minimum | R5 000 or R500/m debit order |
| ISIN Code | ZAE000327565 |
| JSE Code | CSSIA |

| | |
|---|---|
| **ASISA Fund Category** | South African – Interest Bearing – Short Term |
| **Launch date** | 29 November 2023 |
| **Fund size** | R260.24 million |
| **NAV** | 100.54 cents |
| **Benchmark** | AF STeFI Composite Index |
| **Portfolio manager/s** | Nishan Maharaj and Mauro Longano |

| | 1 Year * | 3 Year * |
|---|---|---|
| Total Expense Ratio | 0.78% | 0.79% |
| Fund management fee | 0.65% | 0.65% |
| Fund expenses | 0.03% | 0.04% |
| VAT | 0.10% | 0.10% |
| Transaction costs (inc. VAT) | 0.00% | 0.00% |
| Total Investment Charge | 0.78% | 0.79% |

## PERFORMANCE AND RISK STATISTICS

### PERFORMANCE FOR VARIOUS PERIODS (AFTER FEES)

| | Fund | Benchmark | Active Return |
|---|---|---|---|
| Since Launch (unannualised) | 3.1% | 3.5% | (0.4)% |
| Year to date | 2.1% | 2.8% | (0.6)% |

| | |
|---|---|
| Yield (Net of Fees) | 9.1% |

### RISK STATISTICS

| Current | Fund |
|---|---|
| Weighted average time to maturity (credit) | 1.8 years |
| Modified Duration | 1.3 years |
| Modified Duration (ex Inflation Linked Bonds) | 0.9 years |

Risk statistics will be published once a 12-month record has been established.

## PORTFOLIO DETAIL

### ASSET ALLOCATION BY INSTRUMENT TYPE

| | % of Fund |
|---|---|
| Cash and Money Market NCDs | 33.0% |
| Fixed Rate bonds | 24.4% |
| Floating Rate bonds | 21.3% |
| Inflation-Linked bonds | 18.4% |
| Credit Linked Notes (CLNs) | 2.9% |
| **Total** | **100.0%** |

### ASSET ALLOCATION BY ISSUER TYPE

| | % of Fund |
|---|---|
| Banks and Insurers: NCDs & Deposits | 33.1% |
| Government | 31.5% |
| Banks: Senior Debt | 16.4% |
| Other Corporates | 11.8% |
| State Owned Enterprises | 2.4% |
| Banks: Subordinated debt (>12m) | 2.3% |
| Insurers | 2.0% |
| Banks: Subordinated debt (<12m) | 0.5% |
| **Total** | **100.0%** |

### CREDIT RATINGS

| | % of Fund |
|---|---|
| AAA+ to A- | 96.3% |
| BBB+ to B- | 0.4% |
| CCC+ to C- | 0.0% |
| CLNs | 2.9% |
| No Rating | 0.4% |

### TOP 5 CREDIT EXPOSURE

| | % of Fund |
|---|---|
| Republic Of South Africa | 33.9% |
| Nedbank Ltd | 15.1% |
| Absa Bank Ltd | 12.4% |
| Standard Bank Of SA Ltd | 11.4% |
| Firstrand Bank Ltd | 9.9% |

### INCOME DISTRIBUTIONS

| Declaration | Payment | Amount | Dividend | Interest |
|---|---|---|---|---|
| 28 Mar 2024 | 02 Apr 2024 | 1.94 | 0.00 | 1.94 |
| 29 Dec 2023 | 02 Jan 2024 | 0.59 | 0.00 | 0.59 |

### TOP 5 REFERENCE ENTITY EXPOSURE

| | % of Fund |
|---|---|
| Republic of South Africa | 2.4% |
| MTN | 0.5% |

100% of CLN exposure is issuer valued with a daily or at worst weekly price frequency

### MONTHLY PERFORMANCE RETURNS (AFTER FEES)

| | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Fund 2024 | 0.8% | 0.4% | 0.3% | 0.7% | | | | | | | | | **2.1%** |
| Fund 2023 | | | | | | | | | | | | 1.0% | **1.0%** |

*As this is a newly launched fund, the TER and TC's are based on an estimated calculation.*
*Please refer to page 4 of the Comprehensive Fact Sheet for important additional infomation, including change in cost disclosures.*

***Please note that the commentary is for the retail class of the Fund.***

**Performance and fund positioning**

The Fund returned 0.28% in March, bringing its year-to-date total return to 1.44%, which is behind cash (2%) and its benchmark (2.06%) over the same period. This is a new fund, launched in November 2023, with a return objective of producing cash + 1.5% return objective over the medium to longer term.

Markets started 2024 intoxicated with the euphoria of the Federal Reserve Board's (Fed) impending monetary policy pivot. Risk assets rode high on the wave of optimism for most of the first quarter (Q1-24), with emerging markets doing especially well. Unfortunately, as is generally the case, this optimism faded towards the end of the quarter, with the market's initial pricing of 175 basis points (bps) of rate cuts for 2024 tapering to the Fed's projections of only 75bps. South Africa (SA) has done little to positively differentiate itself from the rest of the emerging market (EM) basket. Uncertainty on the outcome of the local elections, possible coalitions and the policy implications thereof weighed on the performance of the rand and bonds, causing further underperformance relative to EM peers.

The FTSE/JSE All Bond Index (ALBI) was down -1.8% over the quarter, driven by its poor performance in February and March, as bond yields rose by close to 100bps, inching closer to the highs last seen during the Covid crisis. Most of this poor performance was driven by the performance of the long end of the yield curve (>12 years). Inflation-linked bonds (ILBs) performed slightly better, returning -0.37%, as elevated real yields and stubborn inflation continued to help the asset class. However, over the last 12 months, both the ALBI's (4.19%) performance and that of ILBs (5.74%) remain significantly behind cash (8.15%). Given that the rand was also down c.4.69% versus the US dollar over the last 12 months, SA bond performance translated to dollars would have fared only marginally better than global bond performance over the same period (FTSE World Government Bond Index [WGBI] was down -0.84% in US dollars).

In SA, the economy expanded by 0.1% quarter on quarter (q/q) in the fourth quarter of 2023 from a contraction of 0.2% q/q in the third quarter of 2023. From the production side, mining and manufacturing production increased while agriculture, construction and domestic trade declined. On the expenditure side, household consumption and inventory accumulation increased, but this was offset by weak net trade, reduced government expenditure, and a decline in gross fixed capital formation. Overall, the economy grew by 0.6% in 2023 from a growth figure of 1.2% in 2022.

The South African Reserve Bank (SARB) unanimously voted to leave the repo rate unchanged at 8.25% at the March MPC meeting. The MPC cited sticky inflation and elevated inflation expectations as the main reasons for keeping the repo rate unchanged. Food inflation has been on a decline, but there is concern that prices could rebound following reports of damage to the summer crops due to dry and hot weather conditions. The SARB slightly updated headline inflation to 5.1% from 5.0% for 2024 and left its projections unchanged for 2025 and 2026 at 4.6% and 4.5%, respectively.

Headline inflation increased to 5.6% y/y in February from 5.3% y/y in January while core inflation ticked up to 5.0% y/y from 4.6% y/y. The increase in inflation was driven by higher medical aid insurance tariffs, and an uptick in service inflation. Food inflation slowed down due to base effects, while transport costs increased on the back of high fuel prices. Elsewhere, prices were generally soft with modest gains in apparel, household services, restaurants, and hotels.

As at the end of December 2023, the market was pricing that the SARB's Monetary Policy Committee would cut the repo rate by 75bps by the end of 2024, but recent pricing suggests that the repo rate will remain unchanged until the end of 2025. Market expectations for inflation are for it to average 4.5% in 2025, which implies a real repo rate of c.3.5% for most of the forecast period. We expect inflation to remain stickier and average 5.4% in 2025. Our stickier inflation forecasts are all supply-side based due to higher food prices driven by the effects of El-Niño, a weaker rand translating into higher imported inflation and the higher cost of doing business in SA as a consequence of inadequate network infrastructure. However, as we have previously argued, with real growth struggling to break above 1.5%, policy settings could be regarded as excessively restrictive and as such, we would view a reduction in the policy rate of 0.5%-0.75% starting in November 2024. This would still maintain a real policy rate of 2.0% based on our inflation forecasts.

At the end of March, shorter-dated fixed-rate negotiable certificates of deposit (NCDs) traded at 9.17% (three-year) and 9.82% (five-year), higher compared to the end of the previous month. Our inflation expectations suggest that the current pricing of these instruments remains attractive due to their lower modified duration and, hence, high breakeven relative to cash. In addition, NCDs have the added benefit of being liquid, thus aligning the Fund's liquidity with the needs of its investors. The Fund continues to hold decent exposure to these instruments (fewer floating than fixed), but we will remain cautious and selective when increasing exposure.

The significant reduction in rate cut expectations over the last quarter has tainted the enthusiasm for risk assets. However, the monetary policy pivot remains in play and, as such, emerging markets should continue seeing supportive flows into their markets. Idiosyncratic SA factors have led to further underperformance of SA assets relative to the peer group. Low growth, sticky inflation and burgeoning deficits will continue to weigh on SA's longer-term outlook unless reform implementation is accelerated through increased private sector participation. SA's bond yields remain elevated but still provide an attractive alternative to cash, given their high embedded risk premium. We would advocate slightly overweight positions in bond portfolios, focused on maturities of less than 12 years, together with decent allocation to sub-10-year maturity ILBs and very little allocation to local credit.

ILBs are securities designed to help protect investors against inflation. They are indexed to inflation so that the principal amount invested and, hence, the interest payments rise and fall with the inflation rate. ILBs have offered protection to investors over the last quarter. However, current breakeven inflation across the ILB curve averages between 5.5% and 6.0%, which is well above even our own expectations for inflation over the medium term. It is only the shorter-dated ILBs (I2029, six years to maturity and I2033, 9 years to maturity) that flag as cheap from a valuation perspective. Risks on the inflation front remain elevated, and these shorter-dated ILBs warrant a decent allocation within portfolios due to their inherent inflation protection.

Corporate credit is an incredibly effective tool that can be used to enhance the yield and longer-term performance of fixed income portfolios. However, it is important to understand that yield is earned over a multiyear investment horizon, and a long-term focus is essential when analysing and investing in the asset class. Managing credit risk is broader than just focusing on the specifics of an individual lender. Instead, we must consider the incremental risk that a corporate credit adds to a portfolio in relation to its overall risk profile and the effect on portfolio liquidity and then ensure that positions are sized correctly.

Low levels of issuance and tightening spreads have created a guise of safety when it comes to investing in the local credit markets. SA credit remains an illiquid market that necessitates detailed scrutiny of underlying fundamentals and relative attractiveness, especially within a deteriorating macroeconomic environment like SA.

We believe that allocating significant amounts of capital to the local credit market is unwise and would represent a substantial opportunity cost in the face of attractive valuations in other, more liquid asset classes. The current level of credit spreads on offer are at historically compressed levels, despite SA being in its weakest economic position. Corporate profitability and creditworthiness are inevitably tied to economic outcomes, with significant polarisation in performance. SA is a sub-investment grade economy; thus, local credit should trade at high yield spreads. However, SA trades as an investment-grade issuer. The only spreads that trade at the high yield equivalent are riskier issuances coming from taxi financing, subordinated tranches of securitisations and bank debt. This also shows how much better the value is in offshore credit, which offers higher credit quality and better diversity at much more attractive valuation levels.

The use of structured products, such as credit-linked notes (CLNs), has become ubiquitous within the local market. This sector of the market has grown exponentially over the last five years and has reached a market size of over R100 billion, but only a third of this market reprices, creating an inaccurate representation of asset volatility and pricing. CLNs mask the underlying/see-through credit risk as the issuing entity (predominantly local banks) is seen as the primary credit risk. The increased usage of CLNs has not expanded the pool of borrowers; instead, it has only served to concentrate it. This is due to the ability to limit the volatility of these instruments through not marking them to market[1] based on the underlying asset price movements. This is why CLN repacks of SA government bonds have become so popular over the last five years. The combination of attractive yields and no volatility is an opportunity that not many would pass up unless, of course, pricing transparency is important to the underlying investor. As a result, there can be significant unseen risks within fixed income funds. Investors need to remain prudently focused on finding assets of which the valuations are correctly aligned to fundamentals and efficient market pricing.

**Outlook**

We remain vigilant of the risks from the dislocations between stretched valuations and the local economy's underlying fundamentals. However, we believe that the Fund's current positioning correctly reflects appropriate levels of caution. The Fund's yield of 9.87% (gross of fees) remains attractive relative to its duration risk. We continue to believe that this yield is an adequate proxy for expected Fund performance over the next 12 months. As is evident, we remain cautious in our management of the Fund. We continue to invest only in assets and instruments that we believe have the correct risk and term premium to limit investor downside and enhance yield.

**Portfolio managers**
**Nishan Maharaj and Mauro Longano**
as at 31 March 2024

[1] Valuations are not regularly adjusted to mirror their current value

## IMPORTANT INFORMATION THAT SHOULD BE CONSIDERED BEFORE INVESTING IN THE CORONATION SA INCOME FUND

Unit trusts should be considered medium- to long-term investments. The value of units may go down as well as up, and therefore Coronation does not make any guarantees with respect to the protection of capital or returns. Past performance is not necessarily an indication of future performance. Fluctuations or movements in exchange rates may cause the value of underlying investments to go up or down. The asset allocation by instrument type are reflected on a look-through basis. The asset allocation by issuer type and top issuer exposures are not reflected on a look-through basis. The yield shown is an estimate in part based on market assumptions and forecasts. The yield is calculated by taking the interest and income receivable of all the instruments in the fund divided by the net asset value, expressed as a nominal annual rate. It is provided to give an approximate indication of the achievable yield for an investment made at the reporting date. Actual experience may differ, based on changes in market values, interest rates and changes in costs actually experienced during the investment period. The yield disclosed on the MDD is current and calculated as at the MDD reporting date.

Coronation Management Company (RF) (Pty) Ltd is a Collective Investment Schemes Manager approved by the Financial Sector Conduct Authority in terms of the Collective Investment Schemes Control Act. Portfolio managed by Coronation Asset Management (Pty) (FSP 548) Ltd, an authorised financial services provider. The Management Company reserves the right to close the fund to new investors if we deem it necessary to limit further inflows in order for it to be managed in accordance with its mandate. Unit trusts are allowed to engage in scrip lending and borrowing. Standard Chartered has been appointed as trustees for the fund (www.sc.com/za; 011-2176600). Coronation is a full member of the Association for Savings & Investment SA (ASISA).

## HOW ARE UNITS PRICED AND AT WHICH PRICE WILL MY TRANSACTION BE EXECUTED?

Unit trusts are traded at ruling prices set on every trading day. Fund valuations take place at approximately 15h00 each business day, except at month end when the valuation is performed at approximately 17h00 (JSE market close) and forward pricing is used. Instructions must reach the Management Company before 14h00 (12h00 for the Money Market Fund) to ensure same day value. The payment of withdrawals may be delayed in extraordinary circumstances, when the manager with the consent of the fund trustees deem this to be in the interest of all fund investors. These circumstances may include periods when significant underlying markets suspend trading which will prevent accurate valuation of the instruments held in the fund. When the suspension of trading relates to only certain assets held by the fund, these assets may be side-pocketed. This process allows normal liquidity on the assets that can be valued, but will delay liquidity on the affected portion of the fund. If the fund is faced with excessive withdrawals, the affected withdrawals may be ring-fenced, which is the separation and delayed sale of the assets reflecting the interest of the liquidity seeking investors. It ensures that the sale of a large number of units will not force Coronation to sell the underlying investments in a manner that may have a negative impact on remaining investors of the fund.

## HOW WAS THE PERFORMANCE INFORMATION INCLUDED IN THIS FACT SHEET CALCULATED?

As this is a new fund the fact sheet does not include performance information yet. Once performance information is available the following will apply:

Performance is calculated by Coronation as at the last day of the month for a lump sum investment using Class A NAV prices with income distributions reinvested. All underlying price and distribution data is sourced from Morningstar. Performance figures are quoted after the deduction of all costs (including manager fees and trading costs) incurred within the fund. Note that individual investor performance may differ as a result of the actual investment date, the date of reinvestment of distributions and dividend withholding tax, where applicable. Annualised performance figures represent the geometric average return earned by the fund over the given time period. Unannualised performance represents the total return earned by the fund over the given time period, expressed as a percentage.

## WHAT IS THE TOTAL EXPENSE RATIO (TER) AND TRANSACTION COSTS (TC)?

The TER and Transaction Costs cannot be determined accurately because of the short life span of the Financial Product. Calculations are based on actual data where possible and best estimates where actual data is not available.

TER is calculated as a percentage of the average net asset value of the portfolio incurred as charges, levies and fees in the management of the portfolio over the period referenced. The TER charged by any underlying fund held as part of a fund's portfolio is included in the fund expenses portion of the TER, but trading and implementation costs incurred in managing the underlying fund are excluded. A higher TER does not necessarily imply a poor return, nor does a low TER imply a good return. The current TER may not necessarily be an accurate indication of future TER's. The 1 year TER is for the 12 months to end of the previous financial year (updated annually). The 3 year TER is for a rolling 36-month period to the last available quarter end (December, March, June and September).

Transaction costs are a necessary cost in managing a fund and impacts the fund's return. They should not be considered in isolation as returns may be impacted by many other factors over time including market returns, the type of fund, the investment decisions of the investment manager and the TER.

The Total Investment Charge is the sum of the Total Expense Ratio (TER) and transaction costs.

## ADVICE AND PLATFORM COSTS

Coronation does not provide financial advice. If you appoint an adviser, advice fees are contracted directly between you and the adviser. For more information please contact the relevant platform (Linked Investment Service Provider or Life Assurance Provider).

## WHERE CAN I FIND ADDITIONAL INFORMATION?

Additional information such as daily fund prices, brochures, application forms and a schedule of fund fees and charges is available on our website, www.coronation.com

## IMPORTANT INFORMATION REGARDING TERMS OF USE

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