corospondent

The Personal Investments Quarterly

CORONATION
TRUST IS EARNED™

APRIL 2020 AUTUMN EDITION

IN THIS ISSUE

CORONATION FUND UPDATES

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Notes from my inbox

"Sorrow is better than fear. Fear is a journey, a terrible journey, but sorrow is at least an arrival. When the storm threatens, a man is afraid for his house. But when the house is destroyed, there is something to do." – Alan Paton, author and activist

By **PIETER KOEKEMOER**

Pieter is Head of Personal Investments

THIS EDITION OF *Corospondent* provides you with consolidated and comprehensive information on the Covid-19 pandemic, its economic and financial markets impact, and our portfolio management actions during the initial crisis period in February and March.

All our lives have changed dramatically, and, in some ways, perhaps permanently, over the past two months. We are in the midst of an epoch-defining moment, challenging all of us with the dual quandary of limiting the loss of life to a novel disease while managing the extreme economic fallout caused by the containment measures – the only currently viable response we have to the virus. While these challenges are requiring sacrifices from everyone, our thoughts are with those on the dual frontlines: the healthcare, food production, retail and logistics workers who are keeping us going through the lockdown; and also the business owners, employees, informal traders and their families who are most affected by the economic hardship caused by the revenue and job losses that are the result of the lockdown.

SHUTDOWN BLUES

It is now clear that we are facing the biggest economic disaster since the Great Depression of the 1930s. Unemployment claims in the US have spiked by nearly 22 million (c.14% of the workforce) over the four weeks to 16 April, roughly equal to all the new jobs created since the Global Financial Crisis (GFC) a decade ago. While we do not have equivalent data for South Africa yet, the impact of the local lockdown on employment is likely to be, at best, similar. In Table 5 overleaf, Google's mobility data show a 75% decline in local retail and recreational visits since the lockdown began, significantly higher than the global average of 61% and the US's 45%. Although government announced a R40 billion temporary employee relief scheme via the UIF, administrative bottlenecks mean that many vulnerable workers in sectors such as construction and hospitality may not receive a paycheque at the end of this month. In addition, there are more than 1.5 million informal businesses in South Africa that are not covered by this safety net, most of which either cannot trade or are severely restricted. The stark reality is that up to half of our population may be faced with food insecurity in the coming weeks and months, unless there is a dramatic step-up in relief efforts. Government initially announced economic support of around 1% of GDP to date, a fraction of the aid packages introduced in most of the developed world. Despite a precarious national balance sheet and significant fiscal constraints, a comprehensive R500 billion aid package, partly funded by loans from the World Bank and the IMF, was announced as we were finalising this issue of *Corospondent*. This package includes a R200 billion loan guarantee scheme for medium-sized businesses, R100 billion to support jobs, R50 billion in additional social grants, and R20 billion in additional healthcare expenditure. The challenge now is in execution – efficiently getting the money to where it is needed, by when it is needed.

Coronation contributed R5 million to the Solidarity Fund at launch. In our view this is one of the most effective and high-impact channels for those businesses and individuals with the ability to contribute to South Africa's efforts to deal with the pandemic. Last week, our team responded to the President's announcement that Cabinet will take a 33% pay cut for three months. A total of 90 employees (representing close to 30% of Coronation's head count) >

and our non-executive directors elected to donate a portion of their salaries over the next three months. Our senior leadership team are all contributing 33% of our salaries. It may be just a few drops in a very large bucket, but every little bit helps.

THIS TIME *IS* DIFFERENT …

Carmen Reinhart is the co-author of the seminal work on financial crises, which put the GFC in perspective through a detailed review of historical financial mishaps in 66 countries over a period of 800 years. The authors' key conclusion at the time was that, while the challenges of the day may feel unique in the moment, they share a lot of commonality with what has gone before. Recently, Reinhart published an article concluding that this time is *truly* different, stating that she can find no historical parallel that can serve as a guide in the current crisis. While this is partly due to the unknown duration of the economic hard stop required to combat Covid-19, the bigger differentiator is the policy response. In the 1918-1919 influenza pandemic around 50 million people died worldwide, but no formal lockdowns were introduced. She reports that the US economy grew by 9% in 1918, bolstered by the World War I production effort. This is also a much more synchronised recession than experienced in 2008/2009, when emerging markets were largely protected from the fallout as a result of China's then-strong economic growth. Counterbalancing this is that the fiscal and monetary responses to the current crisis are also completely unprecedented. Support packages already announced in developed countries often exceed 10% of GDP and quantitative easing programmes are at several multiples of the post-GFC level. Central banks around the world are firmly in 'whatever it takes' mode.

… BUT THE INVESTOR PLAYBOOK REMAINS LARGELY THE SAME

Our focus in this edition is to try and contextualise what all of this means for investors. The key take-out for us is that a disciplined commitment to long-term valuation-based investing remains the correct response. Getting this process right is what we focus on every day. For our clients, the core message, as always in tough times, is to remain committed to a well-diversified portfolio that is appropriately balanced between growth and income as well as domestic and offshore assets. How to get this allocation right depends on your personal ability to take risk and the time horizon that you have. If it is at all possible in a time of hardship to remain committed to your original plans, we think you will be well served over time.

One key observation that is worth highlighting is that return prospects for retirees that are correctly positioned have improved markedly. Over the past four years, there was a big rotation out of conservative balanced funds such as Capital Plus and Balanced Defensive, in favour of lower risk options, including a move to cash. This was an understandable reaction to disappointing returns produced by local equities and listed property, with cash outperforming the conservative balanced funds over the past five years. However, the probability that the conservative balanced funds will produce better performance over the next several years has increased markedly. In South Africa, yields on cash and shorter-dated bonds have declined significantly after a 2.25% cut in the policy rate and are now only in line with inflation, while equity valuations worldwide are now much more attractive and longer-dated local government bonds also still provide attractive real yields. Retirees with both income and growth needs can therefore expect very different future outcomes compared to what they currently see when perusing statements and historical performance tables.

Table 1

DECLINE IN RETAIL AND RECREATION VISITS, SELECTED COUNTRIES

Bond	%
South Korea	(16%)
Japan	(30%)
Australia	(40%)
United States	(45%)
Brazil	(59%)
Average across 129 countries	(61%)
New York State	(62%)
South Africa	(75%)
India	(80%)
United Kingdom	(81%)
Italy	(86%)

Source: Google Community Mobility Report as at 11 April 2020

LIKE ALWAYS, WE ARE HERE FOR YOU

We know this is a trying moment for most of our clients. We also have to prepare ourselves for an extended period of disruption while we wait for a comprehensive medical response to dealing with the pandemic. We are as focused as we have always been on managing your capital to the best of our ability and to provide you with the client service that you expect of us. In this moment, it is worth reminding ourselves of Franklin Delano Roosevelt's words when he squared up to fight the Great Depression: *The only thing we have to fear is fear itself*.

Pieter

Key performance indicators and fund performance

AS AT 31 MARCH 2020

	QTD	YTD	1 YEAR	3 YEARS	5 YEARS	10 YEARS	15 YEARS	20 YEARS
DOMESTIC INDICES								
CAPI (J303T)	(22.9%)	(22.9%)	(20.1%)	(3.5%)	(0.8%)	7.4%	11.6%	-
ALSI (J203T)	(21.4%)	(21.4%)	(18.4%)	(2.1%)	(0.1%)	7.7%	11.6%	12.5%
Top 40 (J200T)	(19.2%)	(19.2%)	(6.2%)	(0.4%)	0.5%	7.8%	11.5%	12.3%
SWIX (J403T)	(23.3%)	(23.3%)	(20.9%)	(4.6%)	(1.9%)	7.6%	11.5%	-
ALSI Industrials (J257T)	(8.4%)	(8.4%)	(7.2%)	(1.9%)	0.5%	12.4%	15.1%	13.2%
ALSI Financials (J580T)	(39.5%)	(39.5%)	(38.8%)	(12.2%)	(8.0%)	5.8%	8.5%	8.9%
ALSI Resources (J258T)	(25.3%)	(25.3%)	(18.5%)	8.4%	2.1%	0.1%	7.0%	10.9%
All Property Index (J803T)	(48.1%)	(48.1%)	(48.9%)	(23.9%)	(14.8%)	1.9%	-	-
BEASSA (TR) All Bond Index	(8.7%)	(8.7%)	(3.0%)	5.3%	5.2%	7.4%	7.6%	9.9%
Short Term Fixed Interest 3 Month Cash Rate	1.6%	1.6%	6.8%	6.9%	6.8%	6.2%	7.1%	7.9%
CPI	1.6%	1.6%	4.2%	4.2%	5.0%	5.1%	5.7%	5.9%
INTERNATIONAL INDICES								
MSCI ACWI (USD)	(21.4%)	(21.4%)	(11.3%)	1.5%	2.8%	5.9%	5.2%	-
MSCI WORLD (USD)	(21.1%)	(21.1%)	(10.4%)	1.9%	3.2%	6.6%	5.3%	3.2%
MSCI GEM (USD)	(23.6%)	(23.6%)	(17.7%)	(1.6%)	(0.4%)	0.7%	5.4%	5.1%
S&P 500 (USD)	(19.6%)	(19.6%)	(7.0%)	5.1%	6.7%	10.5%	7.6%	4.8%
BGBA (USD)	(0.3%)	(0.3%)	4.2%	3.6%	2.6%	2.5%	3.3%	4.4%
3 Month Libor (USD)	0.4%	0.4%	2.1%	2.1%	1.5%	0.9%	1.8%	2.1%
MSCI ACWI (ZAR)	0.3%	0.3%	9.3%	11.7%	11.1%	15.8%	12.9%	-
MSCI WORLD (ZAR)	0.7%	0.7%	10.4%	12.1%	11.5%	16.6%	13.0%	8.5%
MSCI GEM (ZAR)	(2.6%)	(2.6%)	1.4%	8.2%	7.6%	10.1%	13.1%	-
3 Month Libor (ZAR)	28.0%	28.0%	25.8%	12.3%	9.6%	10.4%	9.2%	7.3%
SPOT RATES								
Rand Dollar exchange rate	14.0	14.0	14.5	13.4	12.1	7.3	6.2	6.5
Rand Dollar % change	(21.6%)	(21.6%)	(18.8%)	(9.1%)	(7.4%)	(8.6%)	(6.8%)	(4.9%)
Rand Euro exchange rate	15.7	15.7	16.3	14.3	13.1	9.8	8.1	6.2
Rand Pound exchange rate	18.6	18.6	18.9	16.6	18.0	11.0	11.8	10.4
Gold price (USD)	1 523.0	1 523.0	1 295.4	1 244.9	1 187.0	1 115.5	427.5	276.8
Oil price (USD barrel)	66.2	66.2	67.6	53.5	55.1	82.7	55.0	24.8

	QTD	YTD	1 YEAR	3 YEARS	5 YEARS	10 YEARS	15 YEARS	20 YEARS	SINCE LAUNCH
DOMESTIC FUNDS (PERFORMANCE IN RANDS)									
Coronation Top 20 Fund	(20.5%)	(20.5%)	(16.3%)	(3.3%)	(0.5%)	7.8%	13.1%	-	15.5%
ASISA Mean of South African Equity General	(22.9%)	(22.9%)	(21.1%)	(5.6%)	(2.8%)	5.5%	9.7%	-	11.9%
Coronation Market Plus Fund**	(17.7%)	(17.7%)	(14.2%)	(2.8%)	0.7%	8.2%	11.1%	-	13.6%
ASISA Mean of South African Multi-Asset Flexible	(15.2%)	(15.2%)	(12.7%)	(2.4%)	(0.1%)	7.0%	9.1%	-	9.7%
Coronation Balanced Plus Fund	(15.4%)	(15.4%)	(12.0%)	(1.0%)	0.9%	8.0%	11.2%	12.3%	13.1%
ASISA Mean of South African Multi-Asset High Equity	(13.5%)	(13.5%)	(10.3%)	(0.7%)	1.1%	7.0%	9.6%	11.7%	11.5%
Coronation Capital Plus Fund	(12.1%)	(12.1%)	(9.3%)	(0.9%)	1.2%	6.5%	9.0%	-	10.6%
ASISA Mean of South African Multi-Asset Medium Equity	(10.5%)	(10.5%)	(6.9%)	1.0%	2.0%	6.7%	8.2%	-	9.9%
Coronation Balanced Defensive Fund	(9.5%)	(9.5%)	(5.8%)	2.0%	3.5%	8.0%	-	-	8.3%
ASISA Mean of South African Multi-Asset Low Equity	(7.1%)	(7.1%)	(3.1%)	2.7%	3.6%	6.9%	-	-	7.0%
Coronation Strategic Income Fund	(3.5%)	(3.5%)	2.0%	6.2%	7.0%	8.1%	8.6%	-	9.8%
ASISA Mean of South African Multi-Asset Income	(1.4%)	(1.4%)	4.3%	6.7%	6.9%	6.9%	7.3%	-	8.8%
INTERNATIONAL FUNDS (PERFORMANCE IN USD)									
Coronation Global Opportunities Equity Fund	(30.6%)	(30.6%)	(24.0%)	(3.9%)	(1.6%)	3.9%	-	-	2.7%
Coronation Global Emerging Markets Fund	(23.3%)	(23.3%)	(13.8%)	(0.5%)	(0.3%)	2.1%	-	-	3.1%
Coronation Global Managed Fund	(16.4%)	(16.4%)	(7.2%)	(1.0%)	0.6%	4.3%	-	-	4.5%
Coronation Global Capital Plus Fund	(9.7%)	(9.7%)	(3.3%)	0.4%	1.2%	2.7%	-	-	3.2%
Coronation Global Strategic Income Fund	(4.5%)	(4.5%)	(2.0%)	0.5%	0.7%	-	-	-	1.9%

* All ASISA averages exclude Coronation funds in that category

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

Figures as at 31 March 2020; for detailed fund performance, refer to pages 42 and 44.

Meaningful periods

A time of crisis

A butterfly flaps its wings in Wuhan, China

By KARL LEINBERGER *and* JOHN PARATHYRAS

Karl is Chief Investment Officer and has 19 years of investment industry experience.

John is an investment analyst with eight years of investment industry experience. He holds an MSc. in Genetics.

This article is updated from the original publication date of 3 April 2020.

THE COVID[1] PANDEMIC is first and foremost a human tragedy. At the time of writing, there have been more than 2.5 million confirmed cases and more than 170 000 confirmed deaths. As we all become increasingly numb to these large numbers, we need to keep reminding ourselves that behind each of those numbers is a human story.

As the coming weeks pass, the depth of the economic devastation and full impact of the virus and its containment measures will be revealed. For those who argue that human lives come first and economics second, the evolution of the economic fallout into a humanitarian crisis will become increasingly clear.

The Covid pandemic is a unique event that is unprecedented in modern times. Consequently, we must be careful, as deeply frustrated citizens, when we harshly judge the decisions made by governments. Although life is always more uncertain than we like to acknowledge, in this case there is just so much we don't know. We have had 22 calls with epidemiologists since early February.

[1] Note from the authors: for simplicity we have used the term Covid to describe both the virus ('SARS-CoV-2') and the disease ('COVID-19') caused by the virus.

The most striking outcome for us has been not what we know about the virus, but what we don't – with a last count of 14 important unknowns.

What does seem clear is that Covid is a virus with a set of characteristics that makes it highly transmissible and fiendishly effective at overwhelming healthcare systems and killing a not insignificant number of people that it infects. And, given that it is a novel virus, humans have no herd immunity, nor do we have any effective treatments or vaccines against it. But, if you don't have the answers to the most basic questions, such as how many people have already been infected, the infection fatality rate, how seasonal the virus is, or whether or not those infected gain immunity, how does a government make the impossible choice between suppression strategies over the alternative – pursuing herd immunity by allowing the virus to spread through the population?

How does the government of a low-income country, without a social safety net, manage the balancing act of controlling the virus and keeping the economy going, especially since these are fundamentally competing interests? In some of these countries, will the all-in damage to society of a national lockdown exceed that of simply letting the virus run its course? How do you even measure these things?

Countries have managed the epidemic in very different ways. This matters enormously, for both the long and the short term.

Due to the lack of any immunity or treatments, governments have resorted to 'non-pharmaceutical interventions' to limit the spread of the virus. These range from targeted measures such as large-scale testing for the virus, isolation of infected individuals, contact tracing of people with whom they have come into contact, and quarantining people who have been exposed to the virus; to more indiscriminate measures such as social distancing. The most extreme form of this is restrictions on the movement of all people via regional, or even nationwide, lockdowns.

The choice of which measures to implement, and when, has varied across countries. First prize is the early use of targeted measures, which, if executed well, reduce the need for more heavy-handed and indiscriminate measures later. This is the path taken by most of Asia (China, Hong Kong, Japan, Singapore, South Korea and Taiwan). Responses differed, but the region has, to date, handled the epidemic well and, consequently has added to our conviction that Asian equities offer great value. The region benefited from:

- The experience it had with the outbreaks of SARS in 2002/2003 and MERS in 2015;
- More compliant societies (often with less civil liberties); and
- Superior surveillance capabilities and very digitised societies (for example, in China, a QR code on your smartphone changes from green to red if someone you have been in close contact with subsequently tests positive).

South Korea and Taiwan have thus far avoided the extent of lockdowns seen across much of the world by acting early (crucially important given the exponential transmission of the virus) and decisively. They deployed widespread testing, contact tracing and quarantine measures in a very effective manner. Singapore has done a similarly exemplary job, only instituting stricter social distancing measures in early April.

China was initially slow to react and therefore had to implement a combination of the measures used by South Korea and Taiwan, and some drastic restrictions on the movement of people in the affected areas. All of these Asian territories have thus far controlled their outbreaks, with much fewer cases per capita than some hard-hit western countries, despite having been nearer to the initial epicentre of the pandemic. Across parts of Asia, freedom of movement is improving, and economies are slowly recovering.

The main reason for Asia's success is that they acted early and with the full gamut of targeted interventions, especially the widespread testing of suspected cases. Countries that do not, or cannot, do something similar are at risk of much more extensive outbreaks. The cruel feedback loop is that the worse the outbreak becomes in a country, the exponentially more difficult it becomes to control. And as it overwhelms the healthcare system, the worse the disease's infection fatality rate is likely to become.

This has left many countries with seemingly little option but to enact unprecedented restrictions on the movement of people. The US is a great example of this. It wasted precious time and squandered its many advantages, and is likely to be a case study of government failure in crisis management:

- Being further from the epicentre, it had more time to take decisive action early on.
- Although wealthier than South Korea (with a roughly 50% higher GDP per capita on a purchasing power parity basis) and with deep institutional knowledge of the control of infectious diseases, it failed to roll out the necessary testing, contact tracing and quarantining processes.

The US is now seeing rapid growth in case numbers. This has left it with little option but to use lockdowns to contain the outbreak. As we write, more than 90% of Americans are now under orders to stay at home, causing significant disruption to everyday life and the economy.

In the UK, the government initially proposed a strategy of gradual restrictions to allow for herd immunity to build up in its population. It then swiftly changed course, adopting strict social distancing measures when it became evident from epidemiological modelling that their initial strategy could quite easily overwhelm their healthcare system. The UK subsequently entered a three-week lockdown on 23 March, which on 16 April was extended by a further three weeks to 7 May.

Both the US and the UK wasted precious time and squandered an opportunity to respond to the virus in a manner much less damaging than the measures they have ultimately been forced to take.

Developing countries, most of which are in earlier stages of their outbreaks, face substantial challenges. Although they have the benefit of younger >

populations and a slight headstart in preparing for the virus' arrival, in many instances these countries are unlikely to have the resources to carry out mass testing of suspected cases as well as other measures, such as contact tracing and isolation/quarantining, at the necessary scale. Many also have high disease burdens, and health-care systems that are more fragile and with less spare capacity to absorb the added burden from a flood of Covid patients.

As such, developing countries have fewer tools available and may be more inclined to resort to heavier-handed tactics, and sooner in their outbreak timelines. For example, on 24 March, India declared a three-week nationwide lock-down of all 1.3 billion of its citizens, despite having only around 500 confirmed cases of Covid at the time. This was later extended by a further three weeks. This is a staggering move by the world's second most populous country.

It is also an unfortunate reality that many developing countries don't have the ability to implement the unprecedented fiscal and monetary stimulus being deployed in many developed countries. The citizens of these countries are also, in general, less able to insulate themselves from the economic fallout that measures such as lockdowns will unleash. And, regarding the question of social unrest, although lockdowns may be effective in developed countries, one must question whether this is possible in the more cramped and unsanitary conditions of many emerging nations.

Sadly, unless their demographic advantage turns out to be material, many developing countries are likely to see significant damage from a public health and economic perspective. Some may have little option but to prioritise their economies and choose the herd immunity route that the UK abandoned.

HOW THE PANDEMIC IS LIKELY TO PLAY OUT

Many decisionmakers around the world are now grappling with what happens next. The first point we should make here is that no-one knows how this will play out. Anything could happen. The only way, therefore, that we can think about it is probabilistically.

Lockdowns in most countries look likely to go on for longer than their initial three-week goal (for context, the lockdown in Wuhan lasted for more than two months before slowly unlocking). Prolonged lockdowns are likely to be ruinous for the global economy though, and many are now asking if the remedy is not worse than the disease. The conundrum is obvious: if restrictive social distancing measures are relaxed too far or too fast then, as has been seen in past pandemics, there will be second 'waves' of infection. There is no easy way out.

The ultimate exit is a vaccine; this will provide the necessary herd immunity to protect the global population, especially the most vulnerable within it, without having to rely on them having been infected with the virus itself. There are currently a few dozen vaccine candidates in development, some already in clinical trials in humans. There is a high probability that an effective vaccine will be developed; the problem, though, is how long it will take.

Vaccine development timelines are typically measured in years, not months, with the average vaccine taking eight to 10 years to develop. There are numerous measures being implemented, as well as unprecedented amounts of capital available, to compress this significantly. Experts are relatively confident that there will be, with a bit of luck, a Covid vaccine within 18 months. It may take some time beyond that to scale its production to a global level. There are newer vaccine technologies that are being looked at that could yield a vaccine sooner than this, although they are relatively unproven in humans and their likelihood of success is lower (and regulatory scrutiny is higher) than traditional vaccine approaches.

There are also numerous existing drugs (for example, antiretrovirals used in HIV patients) that are being explored for 'repurposing' as a treatment for Covid infection. They have the benefit of already having been approved by regulators for treating other diseases, so, if effective against Covid, they could be approved and rolled out rapidly. These treatments will not prevent infection, but only treat it and, in so doing, improve patient outcomes – they are only a stopgap, we will likely still need a vaccine.

A few of these drugs have displayed promising results in lab and animal studies, and some even in small-scale human clinical trials, but more trial data is required before we will know for sure if any of them will work. This data should start being released in the weeks ahead.

If one or more of the above treatments prove effective, it could materially change the current status quo. But it is not a given that any will be successful; drug research and development is an endeavour with a notoriously high failure rate. If none prove to be a game-changer, then the only light at the end of the tunnel is a vaccine.

MANY DEVELOPING COUNTRIES ARE LIKELY TO SEE SIGNIFICANT DAMAGE FROM A PUBLIC HEALTH AND ECONOMIC PERSPECTIVE.

UNLOCKING THE LOCKDOWNS

Must we all now sit at home for 18 months waiting for a vaccine? This isn't an option. Most likely we will see a period of rolling restrictions on movement that snap on and off when certain triggers (e.g. ICU bed utilisation rate or growth of new case numbers) are breached. We wonder whether societies have the endurance this would require. The economic and social costs will likely be staggering. Conversely, allowing the virus to spread unfettered would almost surely be a public health disaster and carry with it its own social and economic costs. Barring a breakthrough on the treatment front near-term, there is seemingly no obvious way to break this impasse.

The lockdowns won't end the pandemic, but they will buy us time. Much will depend on which countries use the time well. Those that use it to build the infrastructure and processes needed to contain future spread of the virus when lockdowns are eased and to win citizens over, will come through this immeasurably better.

WHAT DOES THIS ALL MEAN FOR SOUTH AFRICA?

The spread of the epidemic to South Africa sparked a market crisis that has felt just as serious and existential as the Global Financial Crisis (GFC) did in 2008/2009. For a few days, South Africa was the only major country in the world to have announced Covid suppression measures without the requisite fiscal and monetary emergency measures that any modern economy requires if it is to survive an economic full stop of this nature.

At work we found ourselves, for a brief period, having to navigate a simultaneous paralysis of four systemically important markets (the interbank, the repo rate, and the corporate and government bond markets).

Nonetheless, as stressful as financial markets and the lockdown period have been, we are bracing ourselves for greater difficulties ahead. We see the period of virus containment as more akin to a marathon than a sprint. For South Africa, this makes for a long and difficult road ahead given:

1. **A long list of obvious vulnerabilities,** namely high levels of poverty that compel people to work through illness; densely populated townships; large numbers of people with compromised immune systems; a dependence on crowded public transport; a limited social safety net; a public healthcare system that was already failing before this; and finally, the onset of winter (notwithstanding uncertainty of how seasonal the virus is, winter isn't good for respiratory diseases).

2. **Use of the lockdown period.** As mentioned, a lockdown cannot stop an epidemic, all it can do is buy time. In the case of South Africa, we question whether government has the funding and the organisational structures needed to execute the testing, contact tracing and quarantine infrastructure that it will need if it is to successfully release society from a national lockdown.

3. **Managing the epidemic after the lockdown.** Aside from our doubts that we lack the testing, contact tracing and quarantine infrastructure to execute on a national scale, the bigger question is probably: with so many people on the breadline, would we have the societal endurance for a prolonged fight against the epidemic anyway (while we await a medical breakthrough)?

4. **The economy and government finances were on a knife-edge before this.** This is the one that worries us the most. In contrast to the healthy growth that most of the rest of the world was enjoying, South Africa has been in recession for some time. Job losses, fiscal deficits and government levels of indebtedness were all at alarming levels to start with. As a consequence, we simply don't have the financial wherewithal needed to absorb and counter the coming economic and humanitarian fallout. Will this end up dwarfing the Covid crisis? Is the cure worse than the disease itself? It's a question we too ask ourselves every day.

WE SIMPLY DON'T HAVE THE FINANCIAL WHEREWITHAL NEEDED TO ABSORB AND COUNTER THE COMING ECONOMIC AND HUMANITARIAN FALLOUT.

This is not to say that South Africa has no chance in fighting this:

1. We had the precious headstart of time because the virus took longer to hit Africa. This is crucially important when you are fighting an exponential growth curve. Recent infection data confirm this, with South Africa stacking up well against other countries.

2. We have a very young population by global standards (fatality rates are very low for people under the age of 50).

3. Our hospital bed/population ratio stacks up well against international peers.

4. We have been encouraged to see the government acting more decisively of late (perhaps because the crisis has made it easier to put aside

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the worst of its paralysing factionalism). There even appears to be a determination to use this crisis to drive through some of the structural reforms that South Africa desperately needs.

5. The public and private sectors are working well together to fight this, something that we never really got right in the past.

PORTFOLIO POSITIONING AND CONCLUDING THOUGHTS

Notwithstanding a barrage of bad news since the client note (18 March) we wrote almost a month ago, I'm sure it would surprise many to hear that, at the time of writing in mid-April, most markets have delivered strong positive returns (the S&P +17%, the FTSE/JSE Capped Shareholder Weighted All Share Index +21% and the All Bond Index +6%). In times of crisis, the market always acts as an efficient discounting machine, hence the ruthless manner in which the Covid tragedy was priced into risk assets, with all sorts of records broken by the extent and the speed with which markets collapsed in February/March.

Many clients have asked us whether one shouldn't prioritise preservation of capital in these uncertain and trying times. This is a difficult question to answer, regardless of what we think the right answer is. This is not an easy time for anyone. Tragedy surrounds us all. Every stakeholder in our society (citizens, business, government) faces unprecedented uncertainty as they watch their incomes dwindle and their balance sheet stresses build. In times like this, watching one's life savings get hammered is a galling experience.

The temptation to give in to one's emotions is enormous. But to do so would be a big mistake. Investing is always an exercise in conquering one's emotions. In times of bad news, asset prices will almost always be low. The primary objective of investing is to own more when prices are low and to own less when prices are high. As tempting as it is to 'go to cash', we do not believe that this is the right answer. As tragic as the Covid epidemic is, we will come out the other side. And when that happens, most economies will benefit from pent-up demand, unprecedented fiscal and monetary stimulus, and record-low oil prices. Markets always rally when we all least expect it. Will it be a medical breakthrough (which could happen at any time)? Was it the point of peak infections? Will it be the lifting of lockdown? Who knows?

A long time horizon has been the cornerstone of Coronation's success of many decades. Every crisis we have lived through (and the list is getting long!) has presented an outstanding opportunity for those investors prepared to take the long view. We currently find ourselves swimming in stunningly cheap assets. We have been astounded by some of the long-term opportunities that have been on offer in the last few weeks. The list of stocks, in both domestic and global markets, that our analysts believe offer more than 100% upside (to their underlying intrinsic value) is a long one. This valuation process has been updated for our entire universe of stocks, fully capturing our best estimate of the economic downturn, and the path dependence that companies with stretched balance sheets often experience in times of stress.

Although positions will vary, the following key features are common across our portfolios:

In our multi-asset class strategies we have moved from an underweight to an overweight equity position. We have closed out the puts that protected us from the worst of the early declines and bought some equity exposure at lower levels. Notwithstanding this, we don't feel that we have reached the point of capitulation quite yet, and we have therefore put cash aside to buy in more meaningful size, should that point come.

We believe that both domestic and global equities are attractive to any long-term investor. This is in contrast to our view throughout 2019, where we felt that global equities were fully priced.

The current turmoil is providing a unique opportunity to buy high-quality stocks at great prices. This is the case across both domestic and global markets, and we have taken advantage of it across all our equity mandates. It is not often that one gets the opportunity to buy great businesses, with excellent management teams, at low prices. We are confident that these stocks will give investors good risk-adjusted returns, even if the tough economic environment endures. As an example, the Coronation Equity Fund currently has a 77% exposure to high-quality companies. This is the highest it's been in 20 years.

In our multi-asset class strategies, we have held, and even increased, our domestic bond holdings. These now offer double-digit yields. The risks are clearly high, given worryingly high levels of government indebtedness, but we think this is compensated for in yield.

We remain concerned by thin credit spreads in the local fixed income market. Elsewhere in the

EVERY CRISIS WE HAVE LIVED THROUGH HAS PRESENTED AN OUTSTANDING OPPORTUNITY FOR THOSE INVESTORS PREPARED TO TAKE THE LONG VIEW.

world, credit spreads have blown up, as investors who were reaching for yield are being forced to price in a significantly higher risk of default. In South Africa, the market is thinly traded, and fairly limited re-pricing has happened. If the market does become stressed, we would actively look to deploy cash into attractively priced credit, be it new issues or credit that has to be sold in the secondary market. The GFC provided a once-in-a-lifetime opportunity to do just that. We hope to get that chance again.

We remain extremely negative about developed market bonds. We are very uncomfortable with government levels of indebtedness and we question whether future generations will be able to service this level of debt.

And, finally, inflation. We have become concerned that the very long-term consequence of all this fiscal and monetary stimulus will be monetary debasement. We have all lived through two decades of declining inflation. Most central bankers have never experienced inflation. Their jobs have become one of stimulating economies and bailing markets out of crises. The risks feel very asymmetrical to us and we think it makes sense to avail oneself of long-term inflation protection, even if it is not something that is likely to be rewarded in the next year or two. ✚

ECONOMIC COMMENT

What will be the cost?

"Battles are never the end of the war" – former US President James Garfield

By **MARIE ANTELME**

THE QUICK TAKE

- End-March data from around the world show the devastating economic fallout of Covid-19
- China and developed markets may partially recover by end of Q2-20; emerging economies will bear the brunt
- SA's already considerable headwinds have intensified; our fiscal position is precarious
- Will this be the impetus for the policy action that has thus far been lacking?

Marie is an economist with 19 years of experience in financial markets.

THE CORONAVIRUS IS at once a health crisis and an economic crisis, which has already pushed the world economy into a recession. By trying to limit the human cost of the virus, governments are imposing a massive economic cost through lockdowns that close economies, which may well have longer lasting and more deeply damaging consequences that we cannot yet foresee. It's possible that the ultimate socioeconomic price that the economic crash exacts will be hard to balance with the actual human cost of the virus. This is the tragedy we face.

The sudden halt in economic activity over the past three months is unprecedented, and there is enormous uncertainty about the path ahead. With the oil price collapse, further demand-shock complexity is added to the mix. Early activity indicators have recently been published, showing the depth of the economic impact. Most charts look like the latest data point is an error (Figure 1, page 13). At the time of writing, China's GDP for the first quarter of 2020 (Q1-20) contracted -6.8% year on year (y/y).

In the US, data measuring initial weekly jobless claims – the first indication of applications for unemployment benefits – double-spiked to never-before-recorded levels, dwarfing all crises since 1967 when the data starts. Cumulatively, weekly claims increased to over 22 million over the past four weeks, implying a spike in US unemployment to 20% in April – a level last seen in the Great Depression (Figure 2, page 13).

In response, economists who started revising global growth forecasts lower when China was hit by the virus at the start of the year, assuming supply chain and demand-related disruptions, are now in an ongoing cycle of downward forecast revisions. This latest set of data will show a deepening deterioration in coming months, given the tightening policy response that is widening the net of lockdowns during that time.

This places us squarely in the realm of the unknown, with not much more than (educated) guesswork informing forecast revisions.

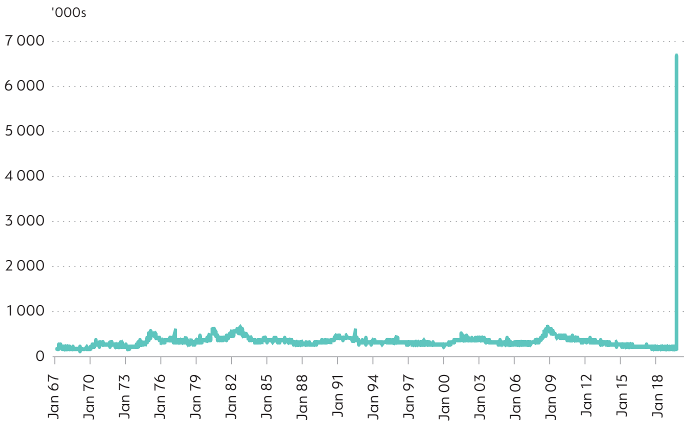
Figure 1

US ECONOMIC ACTIVITY INDEX

Source: New York Federal Reserve Bank

Figure 2

US WEEKLY JOBLESS CLAIMS



Source: St Louis Federal Reserve Board

WHAT WE THINK WILL HAPPEN

Part of the challenge in assessing the economic impact of these shocks is, first and foremost, the 'novel' aspect of this virus: it's new, and we simply don't know how the pandemic will evolve. It's also extremely difficult to untangle the complex inter-relationships between the uncertain evolution of both the severity and the duration of the economic shock, and what these mean for future recovery. Further, the effects of the swift and unprecedented global monetary and fiscal responses need to be considered, and the degree to which these measures can protect underlying economic resilience and assist recoveries on the other side.

What we know about the economic crisis currently unfolding is broadly shaped by the following assumptions:

1. **Asia**
   China's economic growth collapsed in Q1-20. Early data suggests a modest second-quarter (Q2-20) recovery. Countries within Asia that are closely integrated into Chinese supply chains and trading patterns should suffer coincident weakness, but to varying degrees. For instance, with the early enactment of containment policies, South Korea and Taiwan have shown relatively lower infection rates and, to date, less severe cases, and stand to benefit as China recovers.

2. **The developed West**
   Western Europe and the US are likely to see the depth of their economic slowdowns straddle Q1-20 and Q2-20. Growth had probably already contracted in Q1-20, based on what we are seeing in PMI and employment data. However, the intensity of the weakness is most likely to be felt in Q2-20 (and perhaps beyond), as public policies aimed at containing contagion were implemented at different paces and with different intensities in these regions.

3. **Non-Asian emerging markets**
   The impact on non-Asian emerging markets remains uncertain, but these countries will certainly not be immune. The full impact on Southern Hemisphere countries is mostly yet to be seen. Initial transmission lagged, and government responses have varied widely. Emerging economies have different socio-economic profiles but, broadly, have weaker healthcare systems; lower quality institutions (including financial); and large proportions of the population – whose immune systems are more likely to be compromised – living in close proximity, making social distancing almost impossible. In addition to the social challenges, emerging markets are facing tighter financial conditions and are more likely to suffer the consequences of a return-to-normal demand sooner than developed economies. It's very likely that the economic impact on emerging economies will be more enduring than for their developed counterparts and may linger through year-end.

UNPRECEDENTED STIMULUS

It also isn't clear that the depth of the economic downturn will be any real guide to its recovery; this will depend on the effectiveness of interventions to contain and treat the virus. Importantly, global policymakers have mobilised enormous fiscal and monetary resources, estimated at close to 6% of global GDP. These interventions primarily aim to:

1. Ensure that financial markets are liquid and continue to function – these are the lifeblood of the global economy;

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2. Ensure that companies don't close, forcing a permanent loss of economic capacity; and
3. Protect jobs.

While the depth and breadth of these interventions are unprecedented, it's still too early to estimate their effectiveness. In some cases, the announced policies have yet to be implemented. But the most important issue is that these policy responses aim to mitigate the demand shock that has come as a result of lockdowns.

Mitigating the supply shock, namely enabling people to return to work, requires a resolution to the health crisis. At this stage, this would require a much broader base of testing for the virus so that governments, companies and households are comfortable enough to start a slow pace of normalisation. Again, we are hostage to its unknown prevalence, and this remains a weak link in any assessment of an economic recovery.

The IMF recently published its *Spring World Economic Outlook*. Amidst great uncertainty and predicated on a moderate recovery in the second half of 2020, global GDP is expected to shrink -3.0% in 2020, and then recover to an above-trend 5.8% in 2021. Within advanced economies, the US economy is forecast to contract -5.9% in 2020 and then recover to growth of 4.7% in 2021. In Europe, the impact of the pandemic has been more severe, with a recession measuring -7.5% this year, to recover 4.5% in the next. The uncertainty regarding emerging markets is acute – in many cases the worst is likely still to come, with considerable health and economic vulnerabilities. Emerging market growth is expected to contract 1.0% in 2020, and to rebound 6.6% in 2021, led by a 9.2% growth recovery in China. Despite these strong growth recovery forecasts, neither developed nor emerging market GDP is expected to recover to pre-crisis levels over the forecast period.

THE LOCAL SITUATION

South Africa faces these same challenges, but with even greater health crisis uncertainty and an unfolding economic crisis against which we have very little defence, due to our already weak economic position. Even before the lockdown, most economists had lowered growth forecasts due to severe electricity constraints, and GDP was broadly forecast at below 0.5% in real terms, following a paltry 0.2% growth in 2019.

In February, the Minister of Finance warned that the fiscal deficit would amount to 6.8% of GDP, and that the total funding of this deficit and other fiscal obligations would be even bigger, at 8%.

On 23 March, President Cyril Ramaphosa announced a three-week lockdown starting 26 March to 'flatten the curve' of infection. The decision will most certainly limit the ultimate human cost and better prepare the fragile healthcare services sector for an inevitable escalation in infection. As elsewhere, however, the economic cost may be higher and longer lasting than the health crisis. The lockdown effectively cripples about 45% of the productive economy. While some essential services and small parts of the retail sector remain open, tourism and related industries are not only completely shut, but will take a long time to recover. The export sector will also be hard hit, including agriculture.

Since then, the lockdown has been extended a further two weeks to the end of April, with few changes to the imposed restrictions. Some parts of the mining and agriculture sectors, as well as industries associated with essential services, have seen some conditions lifted, but the lockdown on the rest of the economy, for now, is acute.

Forecast revisions to account for such an unprecedented shock suggest GDP may contract by between 5% and 10% in 2020. Recently, the South African Reserve Bank (SARB) released updated forecasts, which now see GDP contracting -6.1% in 2020, with a modest rebound to 2.2% in 2021. Our estimates suggest a -13% y/y contraction in Q2-20, and a weak recovery into year end, given the uncertain progress of the pandemic, both globally and at home. At Coronation, our expectations are for a marginally tighter contraction of -6.4% in 2020 and a more 'robust' rebound of 3.8% in 2021. Again, this still implies that the level of GDP at the end of 2021 will be below where it was in 2019 (Figure 3, page 15).

Such weak economic growth, coupled with a much lower oil price, should keep inflation at low rates in the short to medium term, although some pass-through from the weaker currency and supply disruptions seem likely as things normalise. Consumer price inflation is forecast to average 3.4% in 2020 and 4.0% in 2021.

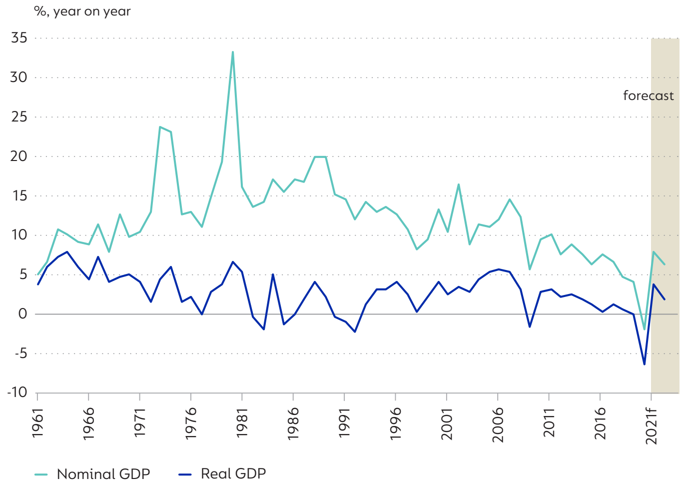
POLICY ACTION

Policymakers have been quick to respond. The SARB's Monetary Policy Committee announced a cumulative 225-basis point cut in the repo rate this year, from 6.50% to 4.25%, enabled by weak economic growth, low inflation and well-anchored expectations. In addition, the SARB has acted to ensure that the financial markets continue to function properly and that there is sufficient liquidity to meet cash demand. The SARB has introduced twice-daily repo operations and increased the term of its refinancing operations

THE SARB HAS ACTED TO ENSURE THAT THE FINANCIAL MARKETS CONTINUE TO FUNCTION PROPERLY AND THAT THERE IS SUFFICIENT LIQUIDITY TO MEET CASH DEMAND.

Figure 3

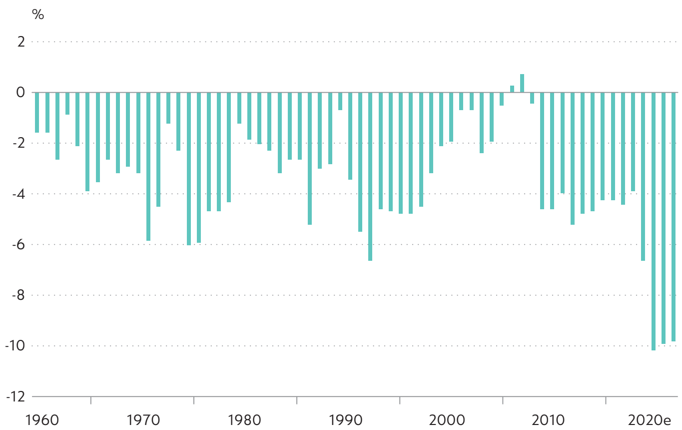
SOUTH AFRICA'S GDP AND FORECASTS



Sources: Statistics South Africa, Coronation

Figure 4

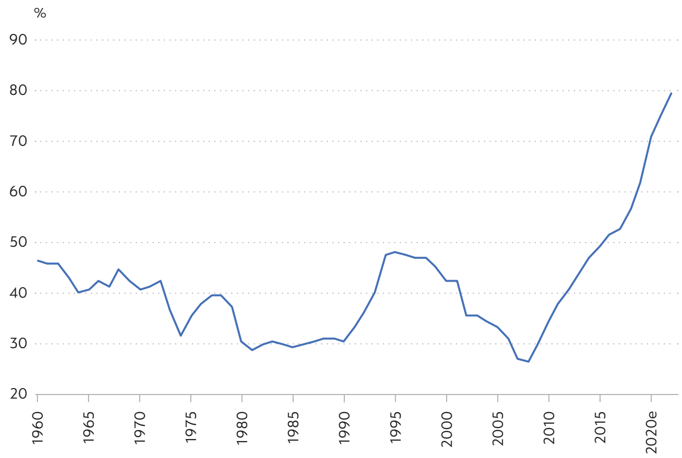
SOUTH AFRICA'S FISCAL DEFICIT, % GDP



Sources: National Treasury, South African Reserve Bank, Coronation

Figure 5

SOUTH AFRICA'S DEBT TO GDP



Sources: National Treasury, South African Reserve Bank, Haver, Coronation

by up to 12 months. It also announced that it will purchase government securities in the secondary market, should dislocations arise.

On the evening of 21 April, the President announced a R500 billion (~10% of GDP) government response package. This aims to meet a range of needs, including support for the vulnerable (extended Unemployment Insurance Fund (UIF) payments and direct transfers to households), wage support, protection for companies via loan guarantees and tax relief, municipal assistance, and financial support for the healthcare sector. Of the R500 billion, R200 billion is for a loan guarantee scheme, R100 billion is to create and protect jobs, and R70 billion will go towards tax relief through the granting of deferred payments.

Final funding arrangements have yet to be published by the Minister of Finance in a pending Appropriation Budget. But, as far as we can account, of the total R500 billion, R130 billion will be reprioritised from existing Budget allocations, while multilateral funding from a combination of loans from the IMF, the World Bank and the New Development Bank could yield about R120 billion. The loan guarantee scheme of R200 billion is through partnership with the local banks and the SARB. This is likely to be a contingent liability at first, with an uncertain drawdown – so the actual cost is uncertain, and the impact on government's contingent liabilities will also depend on whether the full scheme is taken up.

Future deficits will be affected by the proportion of loans that turn bad. The remaining resources include the UIF, which we think will fund some of the job protection and wage support allocations. Overall, additional funding is likely to be significantly less than the total package implies, but will, on balance, add to the large fiscal fall out of the crisis.

In addition, the ultimate fiscal cost will depend on the economic recovery after the lockdown, which is, in part, dependent on the duration of the lockdown. However, the fiscal intervention is a welcome support that should materially assist in limiting the downside risk to economic growth from this crisis.

FISCAL SQUEEZE

The fiscal implications of this are extremely negative. The fiscal deficit is expected to exceed 10% of GDP in our baseline and will be greater once we include the details of government's response the crisis (Figure 4). The sharp drop in revenue and the likely very-low nominal growth that follows a shock like this, makes funding the shortfall extremely difficult. Under our baseline, the public sector borrowing requirement will exceed 11% of GDP in each of the next three years (Figure 5). Government >

debt will continue to accumulate, with nominal growth well below nominal funding costs, with the latter likely to rise.

A THREE-PEAK CHALLENGE

Policymakers are going to face three material challenges in coming months: the impact of the pandemic on the people and economy of South Africa, with a structurally damaged fiscal position that requires funding; ongoing pressure on capital flows from the financial account, which complicates that funding; and the likely pressure this will place on the financial system.

While government's crisis response is a necessary intervention, it remains to be seen whether it has enough credibility to anchor market expectations about the effectiveness of the programme and the likely impact on fiscal sustainability in the longer term. The SARB has shown willingness to respond timeously to financial constraints and has the capacity to do so. We expect these interventions to increase in coming months, but warn that they are not without risk, and we expect SARB policy to remain prudent. In this regard, some external funding arrangement(s) seem inevitable, both in the short and the longer term.

CAN WE FIND OUR FOOTING?

In such an uncertain environment, it's difficult to know what to do, but where possible – and especially in light of South Africa's fragile fiscal position – proactive contingency planning can go a long way to support confidence and reduce uncertainty. In the eye of the crisis, global financing institutions are more likely to respond more generously than they would otherwise, albeit not without the necessary conditionality.

We are encouraged by President Ramaphosa's timely intervention to mitigate the pandemic's damage; we are aware of the hard work being done by the National Treasury to prepare for the interventions that will be needed; and the partnering of private and public healthcare officials ahead of time will surely improve South Africa's ability to respond. Members of the private sector have also contributed generously to support policymakers, public efforts and small enterprises.

Let this also be an opportunity for government to accelerate and implement its growth strategy with critical vigour, because the best way to address these challenges is to help, by all means possible, the economy to grow. ✚

STOCK ANALYSIS

Naspers

Revisiting the investment case

By ADRIAN ZETLER

THE QUICK TAKE

Naspers' restructuring is a positive step that has created flexibility to unlock significant value for shareholders

Exposure to Tencent, which has proven remarkably resilient during the recent Covid-19-induced economic turmoil, is a significant plus

Tencent is set to capitalise on China's transition to a digital economy and we are very excited about its online payments and fintech business

Naspers trades at a large discount to its intrinsic net asset value and is being grossly mispriced by the market

Adrian is a portfolio manager with 10 years of investment industry experience.

Naspers has formed an integral part of our client portfolios for more than 15 years. Since we last wrote about the company in our September 2015 edition of *Corospondent*, it has been the best-performing share on the JSE (generating a return of almost 20% p.a.) and has contributed significantly to the performance of our portfolios. While the natural temptation after such a strong run is to lock in some of this outperformance, we continue to believe that Naspers is a company that is trading at a substantial discount to its intrinsic value and is one of the most attractive stocks in our market. As such, it remains the largest equity position across our domestic equity and multi-asset class portfolios.

THE CREATION OF PROSUS

In September 2019, Naspers undertook a major internal restructuring and injected all of its international internet assets (including Tencent, which comprised the bulk of its intrinsic value) into a new vehicle, Prosus, which is separately listed in Amsterdam with a secondary listing on the JSE. Naspers then proceeded to unbundle 26% of its shareholding in Prosus directly to its shareholders. We thought this restructuring initiative was a positive step, because, apart from providing Naspers with access to international capital markets, it also created a very tax-efficient entry point for investors to gain exposure to Tencent, as well as a portfolio of other high-growth internet assets in the online classifieds, payments, etail and food delivery sectors. Furthermore, the structure provides Naspers with additional tools to manage the large discount to intrinsic value at which it currently trades. This was highlighted when they recently sold a portion of their Prosus holding to execute a Naspers share buyback – thereby unlocking over R3 billion in value for Naspers shareholders. Naspers currently owns 72% of Prosus, which comprises virtually all of Naspers' intrinsic value.

TENCENT – THE JEWEL IN THE CROWN

Weixin (or WeChat), Tencent's main social network, is as central to the company as it is to Chinese life. It has over one billion monthly active users, and is used

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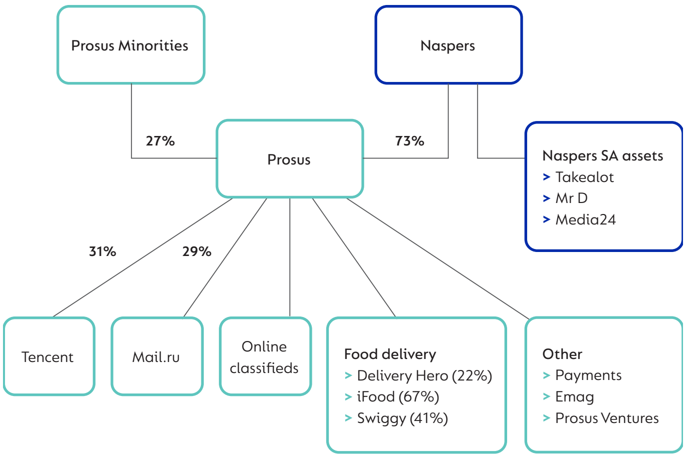
Figure 1

NASPERS GROUP STRUCTURE



Source: Coronation

for business and personal communication, content consumption, payments and utility services. It has become an indispensable tool for everyday life in China. The average user spends 77 minutes per day on the app and Weixin has a roughly 30% share of total internet time spent in China. Weixin's value to Tencent is primarily as a powerful distribution platform for its various other business lines, including gaming and payments.

THE GAMING BUSINESS OFFERS ATTRACTIVE EARNINGS POTENTIAL, WHICH WILL GENERATE SUBSTANTIAL FREE CASH FLOW TO FUND TENCENT'S OTHER GROWTH INITIATIVES.

Tencent has become the leading developer and publisher of PC and mobile games globally, and gaming currently generates c.30% of its revenue and 40% to 50% of its earnings before interest and tax, respectively. The company has been very successful in developing and publishing hit games such as 'Honour of Kings' and 'PlayerUnknown's Battlegrounds' (PUBG, or Peacekeeper Elite as it's called in China), both of which have exceeded a massive 50 million daily active users (DAUs). As the Chinese market leader, Tencent has a formidable position in gaming, but what many people underappreciate is that they now also own stakes in four of the most successful mobile game development studios in the world – Riot Games, Supercell, TiMi and Quantum, and currently has five of the top 10 DAU games in the world sitting in their portfolio. While the gaming business is undoubtedly exposed to increasing regulatory oversight in China, we still believe it can grow earnings in the mid-teen percentages over the next few years and, importantly, generate substantial free cash flow to fund Tencent's other growth initiatives.

The most exciting area within Tencent at present is undoubtedly its digital payments and financial service businesses. We believe that there is still a huge misperception in the market that Tencent can't be profitable in payments. Our view is that Tencent is currently in an incredibly strong market position versus its competitor, Alipay, and has recently taken steps to increase commission rates and reduce channel fees to ramp up profitability. We think this business will contribute significantly to group profits over the next three to five years. Similarly, Tencent is rolling out other financial services products, such as banking, wealth management and insurance. Given Tencent's distribution capabilities, together with their enviable treasure trove of user data, we think they are very well positioned to build a substantial and very profitable business.

Tencent also owns a number of nascent businesses that are still being significantly undermonetised, as detailed below:

- It operates the largest online video, music and literature platforms in China, all of which are growing very strongly. It has a near monopoly in music and literature, but vies for leadership in video with iQiyi, a Baidu subsidiary. Video is still heavily loss-making, as Tencent is investing in premium content, and competition has kept subscription fees abnormally low (around $2 per month). However, we believe it can be profitable over time as Tencent gains leverage on its content investments and the competitive environment stabilises. Netflix, which currently has 167 million users (versus Tencent Video's 106 million users), has a market cap of $167 billion, highlighting the value that can be unlocked from this business in time.
- Weixin remains a largely untapped advertising opportunity. Tencent monetises Weixin at around 20% of Facebook's monetisation of its Asia Pacific audience, despite their much higher levels of engagement, suggesting significant upside potential.
- Cloud remains a very fast-growing segment within Tencent. Although they lag the market leader (Alibaba), they are particularly well placed to capitalise on the growing demand for cloud services driven by the gaming and online video industries. As this business scales, it will also turn to profitability.
- Tencent has quietly built up the largest internet/tech investment portfolio in China, with over 800 investments. This is currently contributing very little to group profitability, despite the company owning stakes in Chinese internet behemoths like Meituan-Dianping (food delivery), JD.com and Pinduoduo (etail),

58.com (classifieds), Didi Chuxing (taxi) and Kuaishou (video sharing), and also some global names such as Tesla and Snap. Over time we believe Tencent will realise significant value from this portfolio.

The Tencent share price has proven remarkably resilient this year (flat in US dollars and up 22% in rands). As the world's largest videogame company, their core business will be boosted by China's measures to contain the spread of the Covid-19 pandemic. While their advertising, payments and cloud businesses will not be immune to the short-term negative economic effects caused by Covid-19, we see these as transitory hurdles and we believe that recent events, which are a consequence of the pandemic (such as working from home, video meetings and online education), will actually accelerate China's shift to a digital economy. Furthermore, given Asian countries' relatively efficient handling of the pandemic outbreak, we expect economies like China to recover relatively more quickly than most other countries in the West, and therefore believe that the risk of Covid-19 undermining the Chinese economy and Tencent's business to be relatively low.

Tencent is currently trading on 28 times one-year forward earnings (23 times excluding its investment portfolio). This is attractive for a business that we believe can continue to compound revenues and earnings at 20%+ over the next five years.

ATTRACTIVE OPTIONALITY IN THE REMAINING PORTFOLIO

Outside of Tencent, Prosus primarily invests in three key areas – online classifieds, food delivery and payments/fintech. As a collective they are currently loss-making; however, we believe that this masks the true quality and long-term profit potential of this portfolio of assets:

- **Online classifieds:** Prosus has one of the broadest online classifieds' portfolios globally, with a presence in most major emerging markets, and dominant positions in Russia, Brazil and Poland. We believe the classifieds model is very attractive, as strong network effects, once dominant, allow the winner to enjoy high margins and low capital expenditure, and therefore high free cash flow conversion. The shifting of advertising budgets from offline to online continues to provide a structural tailwind for the business. In this vertical, there are also a number of consolidation and bolt-on merger and acquisition (M&A) opportunities that we believe can add significant value.
- **Food delivery:** This is the vertical that will attract the majority of Prosus' future capital investment. In food delivery, Prosus has three major assets: a 22% stake in Delivery Hero (Global), a 41% stake in Swiggy (India) and a 67% stake in iFood (Latin America, primarily in Brazil). Many of the markets in which these businesses operate lend themselves to a successful food delivery model, i.e. high income inequality and a well-developed culture of eating out. Food delivery has a large total addressable market and the runway for future growth is certainly long, but as yet unestablished. We also see the food delivery platform model as becoming a natural monopoly once clear leading positions are established; we are therefore very excited about the portfolio of assets that Prosus has established.
- **Payments (PayU):** Prosus has been growing its portfolio of payment service companies through the acquisition of regional gateway players and technology platforms that facilitate cross-border transactions, and by expanding into adjacent verticals such as lending, remittances and wealth management. India has now become PayU's largest and fastest growing market, and it offers merchants a solution that can accept and process many different forms of payment with the highest approval rates. The big opportunity for PayU is to leverage its strong position in payments into the large consumer and small to medium credit opportunity sets currently available in the Indian market. While many in the market might disregard the value of this vertical within Prosus, we think it could be a very attractive acquisition target to large global payments players.

FOOD DELIVERY HAS A LARGE TOTAL ADDRESSABLE MARKET AND HAS A LONG RUNWAY FOR FUTURE GROWTH.

THE NOTORIOUS DISCOUNT

Due to its holding company structure, many market participants believe that Naspers (and Prosus) should trade at a large discount to the value of its underlying assets. Our view is quite different. While a small discount can be justified to account for certain frictional costs inherent in the structure, we think it's important to remember that this is a company that is run by a management team with a proven ability in identifying and capitalising on major media and technological trends. Naspers pioneered pay-TV services in South Africa and was a founding investor in MTN, the largest mobile operator in Africa. It went on to become a major investor in Tencent and Mail.ru, two of the largest internet companies in China and Russia, respectively. More recently, they have embraced ecommerce and built fantastic online classifieds and food

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delivery portfolios. Furthermore, we think that capital allocation discipline under CEO Bob van Dijk has been excellent. Some examples of this include:

- They have refined their investment portfolio and focused on verticals with the most attractive economics, large addressable markets and where they have the assets with which they can build market-leading positions. In this process they have exited the majority of their etail investments, specifically Allegro, Flipkart and Souq – all at very attractive prices.
- In 2019, Naspers unbundled 100% of MultiChoice and 26% of Prosus to their shareholders.
- In 2018, they sold a small portion of their Tencent stake at a good price and raised US$10 billion. They have been extremely disciplined in how they deployed this capital and today still have $4.5 billion in cash on their balance sheet. This cash pile is incredibly valuable in the current environment and gives them significant financial flexibility, should attractive M&A opportunities arise.
- Naspers recently sold a portion of their Prosus stake (c.1.5% of Prosus) and used the proceeds (amounting to R22 billion) to fund a buyback of Naspers shares that were trading at a much larger discount to its intrinsic value than Prosus.

ESG ENGAGEMENT DRIVING SHAREHOLDER VALUE

As a large Naspers shareholder, we have engaged extensively with management and the Board of Directors on a number of environmental, social and governance (ESG)-related issues in recent years. One particular area of focus has been executive remuneration and engaging with the Board in order to improve remuneration structures, transparency and disclosures around the Remuneration Policy.

In this regard, we note the significant improvements that have been made to date:

- management incentivisation is now more balanced between the value created within Tencent and the value created within the rest of the investment portfolio;
- significant improvements have been made with respect to disclosure and providing a clearer link between strategy, performance, remuneration design, and remuneration outcomes; and
- a share buyback programme has been implemented in order to neutralise the shareholder dilution of share options granted to management.

One ongoing point is that Naspers continues to use long-dated options in order to incentivise management. We believe such long-dated options are significantly more expensive for shareholders than shorter-dated options, and therefore continue to engage with the Board in order to shorten the tenure of such instruments.

CONCLUSION

Prosus currently trades at a c.35% discount to its intrinsic net asset value, while Naspers trades at c.50%. We find these discounts puzzling, given the long-term investment track record as discussed above. As such, we think the market is grossly mispricing these stocks at current levels and has therefore created a fantastic opportunity for long-term investors. ✚

Market review

A brutal quarter for financial markets

SINCE JANUARY, THE Covid-19 outbreak has overtaken our lives and transformed our world, presenting a medical, economic and human challenge that is unprecedented in our lifetime. The outbreak of this pandemic has impacted financial markets with swiftness and ferocity. Most asset classes experienced steep declines, providing very few places for investors to hide. Even gold, often viewed as a safe asset class in a time of crisis, had fallen 12% at trough. Cryptocurrencies also did not exhibit defensive qualities, with bitcoin declining by 50%.

Equity markets declined faster, and volatility spiked higher than ever before. From 19 February to 23 March, the US stock market, as measured by the S&P500 Index, saw a cumulative loss of 34%. The following three trading days saw gains of 18%, marking the best three-day stretch since the 1930s. This experience was repeated in equity markets around the world. The MSCI All Country World Index ended the quarter down 21.3%, and the MSCI Emerging Markets Index was down 23.6%. Global property markets around the world declined by 28% to 33% (all global returns expressed in dollar).

Overall, the JSE experienced a very tough quarter, with the FTSE/JSE Capped All Share Index and the FTSE/JSE Capped Shareholder Weighted All Share Index (SWIX) declining by 22.8% and 26.6%, respectively (both in rand). No part of the market was left unscathed, but the economically sensitive sectors, such as property (-48.1%) and banks (-39.4%), bore the brunt of the pain as they were sold off aggressively. Industrials (-8.5%) and resources (-25.3%) performed relatively better.

The All Bond Index (ALBI) ended the quarter down 8.7% and inflation-linked bonds (ILBs) declined by 6.6%. The rand, declining by 22% against the dollar, has been one of the worst-performing currencies so far this year, as the global demand shock compounded South Africa's existing structural headwinds. Adding to the negative news, Moody's Investor Service finally joined Fitch and S&P in downgrading South African debt to subinvestment grade, with all three rating agencies also retaining us on a negative outlook. Cash, yielding 1.6%, was the only domestic asset class to yield a positive return over the quarter.

With investors fleeing risk assets in search of safe havens, developed market bond yields fell to record lows. The FTSE World Government Bond Index (WGBI) appreciated by 2% in dollars as a result. Global credit sold off in line with other riskier assets, with global investment-grade bonds declining by 6% and high-yield bonds by 15%. ✚

FUND UPDATE

Coronation Balanced Plus and Coronation Equity Funds

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

Karl is Chief Investment Officer and has 19 years of investment industry experience.

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

Adrian is a portfolio manager with 10 years of investment industry experience.

THE BALANCED PLUS and Equity funds declined by 15.4% and 17.5%, respectively, in the first quarter of 2020 (Q1-2020). While we did not escape the brutal realities of declining markets, our domestic equity exposure declined less than the benchmarks due to a bias to rand hedge shares and low exposure to South African domestic shares.

In Balanced Plus, we became more constructive on global equities during the quarter, given the sharp sell-off and more attractive valuation levels. While short-term news flow remains poor, once Covid-19 is behind us, corporates will be operating in an environment of unprecedented fiscal stimulus and record-low interest rates, with the tailwind of low energy prices. Combined with pent-up consumer demand when lockdown measures are over, we believe that corporate profitability could look very different in 12 months' time. During the quarter, we moved from an underweight to an overweight equity position as we closed out puts that protected us from the worst of the early declines before adding some equity exposure at lower, after decline levels.

The Equity Fund's large weighting in global equities also helped relative performance. One of its largest international holdings, ecommerce retailer JD.com, delivered very strong returns over the past quarter (+46% in rand). While many traditional brick-and-mortar retailers in China were left reeling, as the Covid-19 lockdown in that country brought consumer demand to a near standstill, JD.com stepped into the void and demonstrated the resilience of its business model and its self-run internal logistics network, ensuring that they were one of the few players that could offer 'locked-down' consumers an uninterrupted supply of essential goods and services. This demonstration of its competitive advantage has allowed the company to build significant goodwill, which bodes well for its future. During the first quarter of 2020, JD.com released excellent fourth-quarter results in which revenues grew 27% and operating profit grew 125%. We continue to believe this is a high-quality business with a long runway for growth and, notwithstanding its strong performance, it remains one of the funds' largest positions.

In an environment with extreme price moves, individual stock selection proved critical. Our two highest conviction local equity ideas in the funds – Naspers/Prosus and British American Tobacco – both came through strongly during the quarter.

Naspers (+11%) and Prosus (+17%) benefited from their exposure to Tencent, whose business proved incredibly resilient during the economic disruption caused by Covid-19. Demand for digital services (such as communication tools, social networking, mobile games, online video, and food and grocery delivery) exploded during the lockdown period.

This is just one reason why we continue to be positive on Naspers. (For more details, please read Adrian Zetler's article on page 17 of this edition of *Corospondent*).

British American Tobacco (+2%) held up well during the quarter. As expected, consumer demand for cigarettes has remained remarkably defensive during this unanticipated economic shock. It's steady growth algorithm of high single-digit revenue growth, driven by strong pricing power, continued cost savings and deleveraging, remains intact and is once again being appreciated by investors. The company is still trading on only 7.5 times one-year forward earnings and an 8% dividend yield. We believe this to be very attractive for a share of this quality and it remains the second biggest local equity position in the funds.

Shares exposed to the domestic economy came under significant pressure during the quarter, as the announcement of South Africa's national lockdown was another body blow for businesses already struggling in a 'no-growth' economic environment. Our preference for holding the high-quality defensive food retailers (Shoprite, Spar and Pick n Pay), together with Dis-Chem, rather than the more economically sensitive clothing retailers, contributed to relative performance. The food and drug retail sector was down only 13% for the quarter, while the general retailer sector was down a whopping 44%.

Our underweight position in the banks also helped during the quarter. Although there is no doubt that their earnings will come under pressure as they struggle to grow advances and their net interest margins will contract on the back of lower interest rates, their real pain will come in the form of higher credit losses, as consumers and businesses buckle under the strain of being leveraged in a very weak economy. However, we have full confidence in the stability of our banking system and, given their conservative past lending practices, together with their healthy capital adequacy levels, we believe the banks are well placed to handle the economic shock we are currently experiencing. Our preferred bank holding is FirstRand, which trades at nine times our assessment of normal earnings.

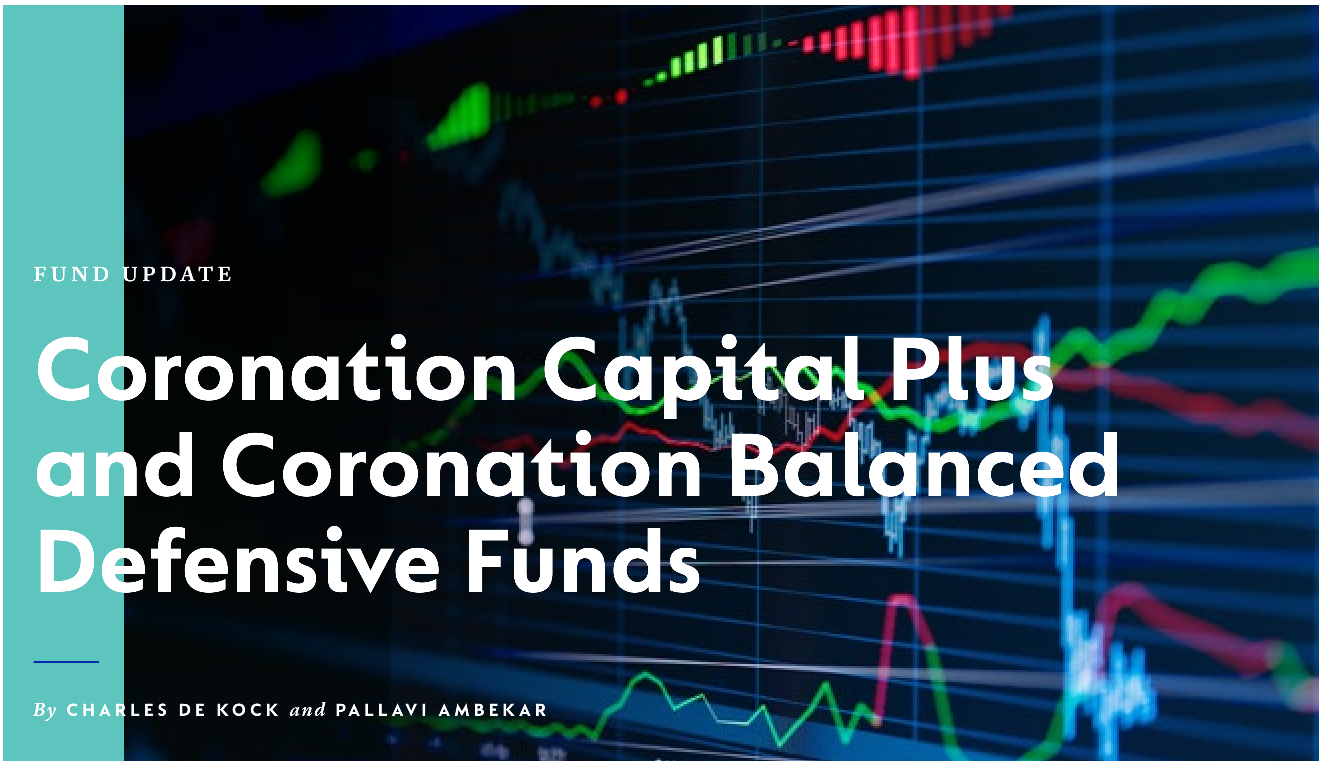
ONE OF THE BIG BUYS FOR THE FUNDS DURING THE QUARTER WAS ANHEUSER-BUSCH INBEV.

One of the big buys for the funds during the quarter was Anheuser-Busch InBev. Its share price collapsed on the back of poor results, which were then compounded by the impact of Covid-19 (reduced beer consumption and weaker emerging market currencies), coupled with concerns around its high debt levels, which we still think are easily manageable. We bought our position at a price of less than 10 times our assessment of normal earnings. This is an incredible price for one of the world's best businesses, which is engaged in a stable and long-lived industry that has superior economics.

Other buying for the quarter was focused on adding to our existing high-conviction ideas such as Quilter, Anglo American and Shoprite on share price weakness. As funding, we sold down our Pick n Pay position and exited our Richemont position.

We are cognisant of the risks around South Africa's worsening fiscal position but believe that South African government bonds (SAGBs) remain a reasonably attractive investment opportunity, given their high yields and absence of near-term inflation pressures in the local economy. Balanced Plus therefore continues to hold healthy exposure to SAGBs. Globally, record-low bond yields come at a time of record levels of government indebtedness and significant monetary policy expansion by central banks around the world, which carries the risk of stoking inflation in years to come. At this point, we are very negative on the outlook for global bonds, given their unattractive risk-versus-return payoff profile.

Notwithstanding the uncertainties that abound, we remain focused on building diversified portfolios for the long term. We will seek to take advantage of this extreme market volatility to invest in attractive opportunities that the market may present to us, and in so doing, generate inflation-beating returns for our investors over the long term. We are happy with the current portfolio positioning and, given compelling valuations, we are excited about future return prospects. ✚



FUND UPDATE

Coronation Capital Plus and Coronation Balanced Defensive Funds

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

Charles heads up the Absolute Return team and has 34 years of investment industry experience.

Pallavi is a portfolio manager with 16 years of investment industry experience.

THE WORLD IS in an unprecedented crisis. We now have mandatory lockdowns in many countries, global travel has been banned and social distancing has become the norm. These actions will no doubt lead to a deep global recession. The depth of the recession is likely to be severe, but we cannot know the duration. This uncertainty will weigh on investors' expectations of when a recovery might start. Investors have tried to find parallels with other global crises, such as wars and the 2008 Global Financial Crisis, but there is no easy comparison. We have never had such a long period of mandated economic inactivity.

Policymakers, led by the US Federal Reserve Board and the European Central Bank, have responded with aggressive monetary stimulus that has provided much-needed liquidity to panicked markets. Economies that can afford it have also introduced extraordinary fiscal measures. It is too early to say whether these measures will be successful or not, but the speed and co-ordination of global policy actions provide a small level of comfort.

Despite these measures, the economic implications of forced lockdowns are enormous. Do companies that are forced to close still pay rentals to landlords? Do they pay interest on loans to banks, or rates and taxes to local authorities? Do they continue to pay employees, and for how long? The answers will be different depending on the country and the company, but it has created huge uncertainty in the minds of investors of how to value banks and property companies, for example.

Against this backdrop, Balanced Defensive and Capital Plus delivered disappointing performance of -5.8% and -9.3%, respectively, over the last year. We have not been able to protect capital, as most asset classes (except for cash) have delivered deeply negative returns. Going into this crisis, the funds were reasonably conservatively positioned, with Balanced Defensive at a 44% weighting in risk assets compared to a maximum weighting of 50%, and Capital Plus at a 57% weighting compared to a maximum of 70%. We were also below our maximum 30% offshore exposure in both funds, with Balanced Defensive at 22% and Capital Plus at 26%. This was because we felt that:

- Global equity markets were expensive after a number of years of strong multiple re-rating. In February, we felt that the market was being too complacent about rising Covid-19 risks, so we bought some put options on the S&P 500 Index.

- Global bond markets were yielding negligible to negative real returns.

- We were cautious on the earnings prospects of our domestic South African equity counters in a constrained growth environment. Within local equity exposure, the bulk of our holdings sat in the global rand hedge shares such as Naspers/Prosus and British American Tobacco/Reinet. We also protected some of our overall local equity exposure by owning domestic put options.

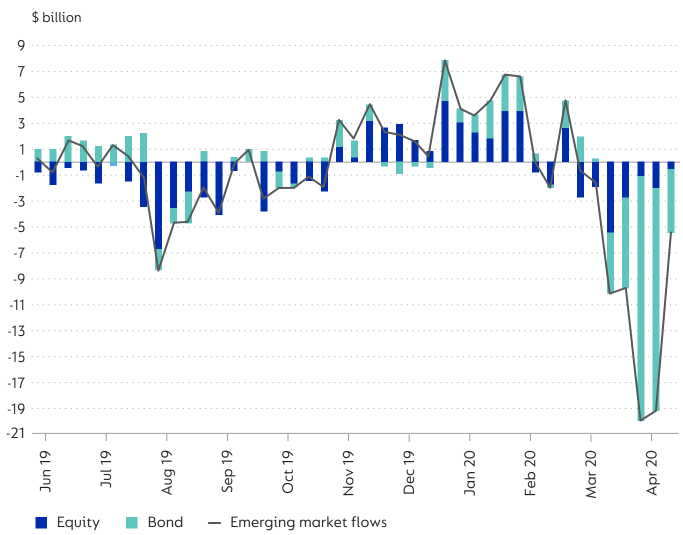
- We have been concerned about the ability of South African property companies to defend and grow their distributable earnings. Consequently, we had a very small exposure to the sector, which was mainly focused on those counters with defensive balance sheets.

- Local fixed income bonds were offering us attractive real returns, with our carve-out yielding more than 9%. With long-term inflation expected to remain in the 4% to 5% range, this yield met our inflation plus 3% to 4% return hurdle. The lower risk asset and offshore weighting was made up with the allocation to domestic fixed income.

Unfortunately, this positioning was not nearly cautious enough and did not provide the capital protection or the stability in returns that we expected. Extreme global risk aversion led to a scramble for safe-haven assets and punished not just traditional risk assets but also led to wholesale outflows from emerging market bond funds (Figure 1). Foreign and local investors used relatively liquid South African fixed income assets as a source of funding. The volatility in the local bond market can be demonstrated by the 10-year SAGB yield swinging from 9.5% at the beginning of March to a high of almost 13% on 24 March. Our fixed income selection, which includes inflation-linked bonds (ILBs) and floating credit, performed far better than the ALBI, but was still negative for the quarter.

Figure 1

EMERGING MARKET EQUITY AND BOND FLOWS



Source: Barclays Capital

Within equities, our selection was also defensive. The two largest holdings, Naspers and British American Tobacco, held up well, as did the food retailers. However, the banks were very weak and detracted from returns. Overall, the equity portion delivered -18.3% and 19.4% for Capital Plus and Balanced Defensive, respectively, compared to the -24.5% of the FTSE/JSE Capped Shareholder Weighted All Share Index benchmark.

HOW ARE WE POSITIONED NOW AND WHAT CHANGES HAVE WE MADE?

1. We have increased our South African fixed income allocation. With the repricing in yields and by adding to our exposure, our fixed income allocation is now sitting at a yield close to 11%, which we think is extremely attractive when compared to a return from cash of c.4.25% expected at the end of this year. We also do not expect a material increase in inflation over the next year or two, as the economy will be very weak. We acknowledge that domestic fundamentals have deteriorated with the Covid-19 crisis, but virtually every country in the world is facing a similar situation. Lower growth will contribute to an increased government debt burden and a widening fiscal deficit. We think local bonds have more than priced in these risks. Spreads look attractive versus South African cash, and real yields look compelling when compared to emerging market and developed market peers. We have a balanced mix of exposure across government and corporate nominal bonds and ILBs.

2. We have removed our S&P 500 Index put position and, in the case of Capital Plus, some of our domestic equity put positioning as markets fell away. Other than these moves, there has been no increase in our global or local equity exposure yet. We will remain true to our investment style of adding to holdings where we see compelling long-term value. Once the contagion is contained, global equities could start to look past the short-term economic hit, especially with the support from large quantitative easing programmes, fiscal stimulus and low oil prices. Within local equities, equity selection will be critical. Many domestic companies will see their earnings bases severely re-set, with the Covid-19-related restriction of economic activity and the slump in global trade. After struggling with a muted economy for many years, the ability to >

cut costs and capital expenditure even further is simply not there or will materially hamper their recovery prospects. After rebasing our internal fair values, as well as our earnings and dividend expectations for the Covid-19 shock, our current basket of South African equity holdings gives us an upside to fair value of north of 60%. This is still very much skewed to the global rand hedge shares and, if valuations are compelling, we will recycle some of this into domestic companies.

3. Global bonds remain terribly unattractive and, while property stocks have suffered an enormous derating, we have not added in this uncertain climate yet. As mentioned earlier, the knock-on effects of enforced lockdowns on landlords are still unclear and one of the consequences is far lower or no dividends for a period of time.

Social distancing measures, if enforced, should lead to a slowing in Covid-19 infection rates over the next month or so. It is hoped that they will spread the burden on the healthcare system and give more time for a combination of herd immunity to build, and for medical treatment, and finally, a vaccine to be developed. At some point, a slow return to normality (although there are still likely to be some social distancing measures in place) will start. Markets are forward looking and will anticipate a recovery. Investors should not wait for good news to be clear. By then the markets will have rallied already. Many companies' share prices have reacted as though the current crisis is permanent and trade far below our assessment of fair value. There may well be more short-term pain, but trying to time the exact bottom is impossible.

In conclusion, the lack of capital protection from the funds over the last year was deeply unsatisfactory, coming mainly from the adverse events over the last month. The fixed income component performance was especially disappointing. Our expectation from this point is for asset prices to normalise, which will allow the funds to recover materially. It has been a volatile time in markets, but attractive valuations and yields cannot be ignored. We remain committed to only adding assets to our clients' portfolios that we believe offer a sufficient margin of safety and are adequately priced for the underlying risk. +

Coronation Market Plus and Coronation Top 20 Funds

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

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

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

THIS QUARTER WILL be remembered for a number of records; none of which we would ever want to repeat. Globally this will go down as the worst first quarter in stock markets in recorded history. In the US, the S&P 500 Index recorded the fastest bear market (defined as a 20% fall) in history, compared to 1929 when it took 36 days. This was followed shortly thereafter by the highest ever print in unemployment claims in the US.

What this has meant for the funds is that it has been a torrid quarter for absolute performance, with Market Plus and Top 20 declining by 17.7% and 20.5%, respectively, since the beginning of the year. It is cold comfort to us that we have managed to outperform benchmarks (the Top 20's benchmark fell by 22.9% this year).

One of the best performing counters has been our large overweight position in Naspers/Prosus. Despite being domiciled in China, where the original virus outbreak occurred, this company benefited, as its main source of revenue is virtual products (gaming, video, music, online content, etc.), all of which was uninterrupted and, in fact, generally boosted by a move to self-isolation.

Naspers has appreciated by around 11% so far this year, benefiting from the much weaker rand as much as from its holding in Tencent. It has also proved fortuitous that their attempt to buy Just Eat for a cash purchase price of $8 billion fell through, so that they were not saddled with a new food delivery business during a lockdown. They now have that cash war chest to pick up potential casualties from the global rout in markets.

Given that Tencent has actually increased by around 23% in rand terms so far this year (and by implication, Naspers has underperformed this move) and the Naspers group is in such a solid position with a very strong balance sheet, we remain holders despite the very strong relative outperformance in the funds. By our calculations, Naspers trades in excess of a 50% discount to its underlying assets.

The second-best performer for the quarter was the funds' large holding in British American Tobacco. After having been a major underperformer in 2018, we increased our holding to a top three position in both funds. A global staple, trading on a single-digit earnings multiple, seemed to be a very attractive proposition. It has proven to be a very defensive stock to own through this period of global volatility. With a globally diversified footprint and strong cash generation, British American Tobacco remains one of our top three holdings.

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The third best performer was our holding in Shoprite, which managed to eke out a small gain for the quarter. This position was built up last year as the market turned sceptical on the growth prospects for the African retailing giant, after a couple of quarters of poor performance. Our analysis indicated that most of these tough results were from one-off factors, and that the core underlying franchise remained exceptionally strong. While its African business will always remain susceptible to economic cycles on the continent, it represents a compelling retail footprint that you were not paying for in the share price. Since self-isolation and then lockdown were implemented, fast-moving consumer goods (FMCG) retailers have benefited from a huge burst in 'pantry stocking', and they are also continuing to trade during the lockdown period. While this is ultimately just a case of future purchases being brought forward and will impact sales later on, the FMCG retailers should be one of the few business sectors that will emerge from this period relatively unscathed. Our other FMCG retail holding, Spar, was our fifth best-performing share in the period.

PMGS TARNISHED, BANKS HURTING

The greatest disappointment during the quarter was the performance of our platinum shares. While the rand platinum group metal (PGM) basket was up in excess of 50% for the quarter, the share prices of Northam and Impala have fallen around 44% and 46%, respectively. A starker divergence between the economic fundamentals and the actual share prices would be hard to find. There are many factors at play, both for and against the outlook of these companies, yet the share prices appear to be only pricing the most negative of outcomes. Based on our assessment of normal PGM prices (much lower than today's levels), platinum shares are all trading on very low single-digit earnings multiples. The hiatus in demand from the shutdown in global auto manufacturers is offset by a lack of supply from South Africa as a result of the lockdown. Given this favourable outlook for the sector, we added to our holdings in the month of March.

The domestic equity sector that hurt the funds the most has been the banking sector. As the lockdowns came into place, the banks sold off dramatically, with further negative moves post the Moody's downgrade. We think the Moody's downgrade is a non-event for the banks. The real damage to the banking system will come from the lockdown. Any stress in a regional economy always ends up in the banking sector. It is the primary mechanism for extending credit into an economy, and any contraction in that economy will be felt in the banks' credit losses. With every small business now under threat of going out of business, and plenty of mid-size and large enterprises as well, the risks of a major spike in credit losses are very real. On the positive side, the banking system is extremely well capitalised. While South African banks didn't suffer direct fallout in the Global Financial Crisis (GFC), they were required to implement all the new capitalisation standards that were approved post the GFC. This means that banks have very significant capital buffers and can handle a substantial deterioration in credit losses. The South African Reserve Bank (SARB) has also started to relax capital buffers to allow banks to cope with the influx of Covid-19-related bad debts, without having to resort to raising new capital. All of this means that the banks should easily be able to handle the stress, if the lockdown is lifted at the end of April as planned. Should it continue in this extreme form for longer, then the stresses will magnify, and the banks could end up in a loss-making position, which, while not threatening their existence, will take a number of years from which to recover. Given the above, we have continued to hold our positions in the bank shares but have not added to them.

THE SOUTH AFRICAN RESERVE BANK (SARB) HAS ALSO STARTED TO RELAX CAPITAL BUFFERS TO ALLOW BANKS TO COPE WITH THE INFLUX OF COVID-19-RELATED BAD DEBTS, WITHOUT HAVING TO RESORT TO RAISING NEW CAPITAL.

PORTFOLIO ALLOCATIONS

We are keeping an underweight position in pure domestic names, despite the significant sell-off. The economic damage being wrought by the shutdown will continue to be felt for many months, if not years, and on a relative basis we find better value elsewhere.

The Market Plus portfolio was overweight offshore exposure, which benefited from the weaker rand, but within our offshore weighting we were overweight equity, which performed significantly worse than global bonds. Where we did benefit was having a number of S&P 500 Index put options, which reduced our equity exposure into the sell-off. We have judiciously removed most of these options, banking the premium earned and increasing our equity exposure close to the recent market lows. This should stand the fund in good stead as market valuations recover.

In the fixed interest space, US bond yields went from the ridiculous to the absurd, joining the ranks of ultra-low interest rates in most developed economies. In contrast, the South African yield curve blew out spectacularly, as urgent sales for liquidity hit a market and banking sector that were not prepared to take on additional risk. The moves in the local bond market were of an order of magnitude that we have not seen since the GFC. Given that this has been accompanied by a collapse in final demand in the economy and a record fall in the oil price, inflation expectations have dropped as well. The net result is that real yields available in the bond market are truly exceptional, with longer duration bonds offering upwards of 7% real returns. This makes a compelling investment case, risks to the sovereign balance sheet notwithstanding.

We have, therefore, continued to add to South African government bonds in Market Plus. Unfortunately, lost in all the noise around Covid-19 was a very fiscally prudent Budget by our Finance Minister, in which he tackled the key problem – a bloated civil service cost base. We think this is a courageous step and one that would have put us on the path to a more sustainable debt basis. Given the events subsequent to the Budget, this is no longer as clear, and we wait to see what stimulus is ultimately provided to the economy and how it is funded. In the interim, buying into high real yields gives us some measure of comfort. In a world of zero and negative interest rates, the potential to earn a meaningful real yield is very attractive.

The impact of lockdowns is felt most extremely in the property sector. With large tenants refusing to pay rentals and small tenants going insolvent, there is significant pressure on this sector, and it will certainly not emerge unscathed. We expect dividend holidays to be announced and certain counters will require additional equity. In this environment, we have not added to exposure in Market Plus, and remain in holdings with significant balance sheet strength to see them through the tough year ahead.

Lockdowns are in place around the world. In the UK, this has meant that any plans of turning around the fortunes of Intu (the UK-based shopping centre portfolio) have been impaired. Prior to the crisis, the company was already struggling with significant debt levels and tough trading conditions, but they had a plan to largely resolve this. The impact of Covid-19 will see further retailer insolvencies in the UK and further declines in centre valuations. We have therefore decided to sell out the remaining holding in Intu in both funds, which had largely been completed by the quarter-end.

As the Top 20's portfolio stood at the beginning of April, our models show the stocks we own have a total upside of 68% to our analysts' fair values. This is the highest potential total return the portfolio has offered in a decade. Obviously, there are assumptions in these valuations, but we have moved quickly as a team to ensure we have priced in the effects of the pandemic and the lockdown on our fair values. While the moves have been extreme and brutal so far, we think the worst has been priced in and, from here onwards, we expect a sharp rebound. Portfolio quality has continued to improve, and we have used the sell-off to buy high-quality businesses on low ratings, which will stand the funds in good stead over the long term. ✚

Coronation Strategic Income Fund

By NISHAN MAHARAJ *and* MAURO LONGANO

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

Mauro is head of Fixed Interest research and a portfolio manager with nine years of investment industry experience.

IN MARCH, THE All Bond Index was down 9.7%, inflation-linked bonds (ILBs) were down 7.1%, listed property was down 36.5%, preference shares were down 27.0% and the rand was down 12.3% against the US dollar. The magnitude of these moves has not been seen since the Global Financial Crisis (GFC) of 2008/2009 and, importantly, have all occurred in a much shorter time period. During these periods of extreme risk aversion, there are two things that are guaranteed. First, even if the entire portfolio could be converted to cash, the best one could expect is a return below that of cash. Secondly, during these times of indiscriminate risk sell-offs, any diversification in a portfolio does not work, because all asset classes move in unison.

Over the years, we have reiterated that, in order for the fund to be able to generate a return in excess of the risk-free rate, it needs to take an element of risk. Even though the fund was relatively conservatively positioned into the crisis, the magnitude of the moves in such a short period of time adversely affected performance. The fund returned -4.1% in March, bringing its total return to 2.0% for the 12-month period.

From mid-February 2020, the world experienced what can only be described as a near-cataclysmic shock. The double crisis of a global oil price war and the rapid spread of Covid-19 across continents has seen shockwaves of fear and panic penetrating geographical and generational boundaries.

No country has been insulated from this crisis, nor from the concurrent slowing in growth and economic uncertainty. The South African Reserve Bank (SARB) initially reacted by cutting interest rates by 100 basis points (bps), and, in subsequent days, also unveiled an unprecedented number of measures to keep liquidity in the banking sector. These included offering long-term repurchase agreements (repos) of up to one year on government bonds; buying government bonds in the secondary market so as to support market liquidity; lowering certain regulatory bank capital ratios to support the economy; and temporarily adjusting the funding mix in weekly government auctions towards shorter-dated government bonds. These measures helped calm the fixed income markets somewhat, but the downward adjustment in asset prices was already quite severe. After the lockdown was extended at the start of the Easter weekend, the SARB announced a further 100bps emergency rate cut as the severe economic impact of the sudden stop in the economy became clearer.

John F. Kennedy once reflected, *"When written in Chinese, the word 'crisis' is composed of two characters. One represents danger and the other represents opportunity."* We believe this observation holds true for this crisis as well. In assessing it, we need to both ascertain the short-term economic consequences that will manifest over the coming months and identify those investment opportunities that could benefit our client portfolios over the next five to 10 years.

Coronation's bottom-up, valuation-driven research process aims to identify those assets that are mispriced for the underlying risks and that have a sufficient margin of safety. In the context of South African fixed income assets, we have reassessed our fundamental assumptions coming into this crisis in terms of what the unfolding situation means for these assumptions, how this filters into our asset valuations, and, finally, how we position the portfolio in response to these changes.

THE ONSET OF CONTAGION

Prior to Covid-19, our key assumptions were that inflation in South Africa would remain under control (5% average), growth would remain subdued (0.2% for 2020 and 1.1% for 2021) and that government finances would remain constrained, but that the problems were being adequately addressed. We had expected interest rates to move lower by between 50bps and 75bps in order to provide some offset to fiscal tightening and to lend support to growth.

Against this backdrop, we viewed nominal government bonds as attractive, specifically in the longer end of the curve; ILBs in the two- to five-year area were offering good value relative to nominal bonds and cash; and certain counters within the listed property space seemed reasonably attractive. We were very cautious on corporate credit, as we did not believe that valuations accurately reflected the higher risks associated with slowing growth.

Credit spreads compressed aggressively over the past 18 months due to a reduction in supply and a reach for yield by non-traditional credit investors. In our view, this made the asset class very expensive, and hence unattractive. Therefore, our portfolios had a neutral allocation to government bonds (with duration focused in the longer end of the curve), a moderate allocation to ILBs, a historically low allocation to selected listed property stocks and a low allocation to select corporate credit.

UNDERSTANDING THE IMPACT OF COVID-19

The Covid-19 crisis has been likened to the Great Depression of the 1930s, due to the expected effects on global growth. Global GDP declined by 27% during the course of the Great Depression, which lasted just under four years. Global growth is expected to decline by a similar magnitude in the second quarter of this year alone. It is the stimulus measures taken by governments around the world to mitigate the impact of the virus that have caused turmoil in financial markets, as they try to assess the economic consequences of such actions.

One of the big teachings for authorities from the Great Depression and the GFC is the need to act quickly, lest markets lose confidence and the crisis blows up. Global authorities have responded very quickly by dropping interest rates back to zero and committing to large quantitative easing (QE) measures (much greater than those seen in the GFC). In addition, many developed markets have already committed to fiscal spending ranging anywhere from 2% to 10% of GDP, in order to soften the growth slowdown and foster a stronger subsequent recovery.

SOUTH AFRICAN GOVERNMENT BOND MARKET LIQUIDITY DRIES UP

Local assets reacted in lockstep with the global risk aversion sell-off. However, South African government bonds (SAGBs) have been exceptionally volatile during this period and sold off materially. Next to cash, government bonds are the most liquid part of a portfolio. In times of crises, when cash is often required to meet margin calls on less liquid assets and to satisfy redemptions, government bonds are used as the natural funding source.

SOUTH AFRICAN GOVERNMENT BONDS (SAGBS) HAVE BEEN EXCEPTIONALLY VOLATILE DURING THIS PERIOD AND SOLD OFF MATERIALLY.

The aggressiveness of the sell-off in global risk markets and the outflows globally from emerging market bond funds have meant that foreign investors into the local bond market have had to sell their holdings for this exact purpose. This created the first leg of the sell-off in our bond market. In addition, we saw the liquidity in the interbank market evaporate, as local banks (the sole intermediaries of SAGBs) pulled back on risk-taking due to reduced liquidity conditions. In times like these, banks prefer to limit the cash lent in the interbank market and utilised in trading activities in financial markets, primarily to support their corporate and individual customers who may have funding and operational needs. This propagated the irrational market behaviour we have witnessed over the past few weeks.

The SARB played a crucial role by stepping in and injecting liquidity into the market, restoring some calm. This included offering term repos on SAGBs and buying SAGBs in the secondary market.

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MOODY'S DOWNGRADE TO SUBINVESTMENT GRADE

Moody's Investor Service downgraded South Africa to subinvestment grade on 27 March 2020, a day after we went into lockdown. This is not a new development and had been well flagged by the market for a few years. As suggested in previous articles, offshore investors have been decreasing their holdings of SAGBs for some time now, and the South African sovereign spread already trades at levels consistent with subinvestment-grade debt.

Additionally, we have seen the South African risk premium steadily increase, suggesting that even before the onset of Covid-19, the downgrade was already significantly priced in. The one thing that has changed is that market volatility has increased and liquidity in the secondary bond market has decreased. This suggests that the mandated selling of SAGBs might result in a more significant move than initially anticipated. However, the FTSE, which administers the World Government Bond Index (WGBI), has allowed up to the end of April for funds to rebalance, which won't stop the selling but will allow it to be more gradual (previously, funds would have had to rebalance by the end of March). In addition, with the SARB announcing its willingness to purchase SAGBs in the secondary market, the effect of this will be dampened. The more important question is whether this weakness represents a great buying opportunity, or whether fundamentals have shifted to such an extent that a more significant risk premium for SAGBs is justified.

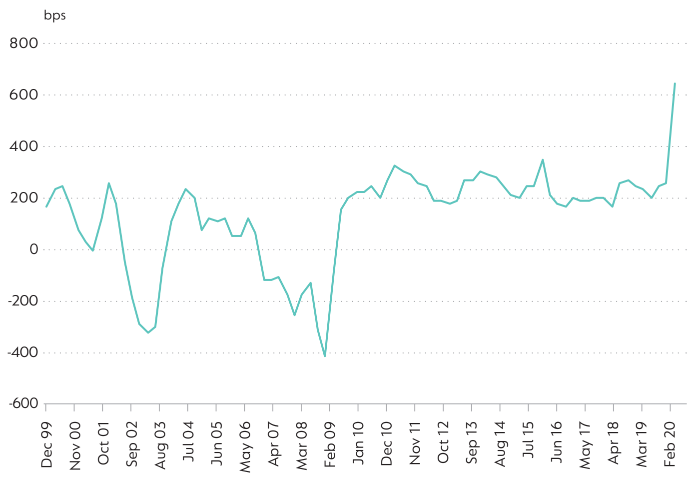
CHANGES TO FUNDAMENTALS

The Covid-19 crisis is still evolving, with many unknowns. Key is the length of time that nations will remain in lockdown and the subsequent economic disruption. This uncertainty is clear in market volatility and the decline in risk appetite. However, there are a few key conclusions that we can draw at this point. First, inflation and growth will be lower than our previous expectations. We expect inflation to average below 4% in South Africa over the next two years. This is due to the impact of the slowdown linked to Covid-19 and the lower oil price. Growth in 2020 is likely to be anywhere from -4% to -7%, rebounding to just over 3% in 2021. This is why the SARB has already cut rates by 225bps this year, moving policy rates lower to 4.25%. This reduced the real yield on cash materially but still kept it in positive territory, which still compares favourably to the negative policy rates prevalent in most of the global developed economies. Unfortunately, given South Africa's poor fiscal starting point and now negative growth expectations, it is very likely that the debt-to-GDP ratio will increase towards 80% and the fiscal deficit will widen to between -8% and -10% of GDP. Further compounding this problem will be the need for government to provide more fiscal support to aid the economy through these trying times, and any additional support for ailing State-owned enterprises (SOEs) such as Eskom. On the positive side, however, lower growth implies lower energy intensity, giving Eskom time to deal with much-needed maintenance. We are hopeful that this situation allows for more drastic measures to be taken at Eskom in order to rectify its financial and operational position.

In many historical instances, crises are what necessitate change. South Africa has been plagued with a slow policy response to its many structural issues. However, the pragmatic approach to the recent

Figure 1

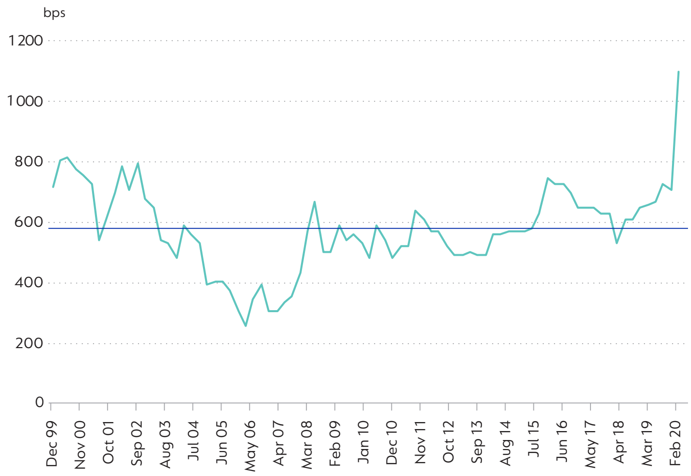
SOUTH AFRICAN 10-YEAR GOVERNMENT BONDS VERSUS THE REPO RATE



Sources: Bloomberg, Coronation

Figure 2

THE SOUTH AFRICAN 10-YEAR GOVERNMENT BOND VERSUS THE US 10-YEAR TREASURY BOND



Sources: Bloomberg, Coronation

crisis will hold our political leaders in high esteem when we finally emerge from it. In an uncertain world, and in an economy that has lost all hope, if the leadership uses this crisis to make the necessary hard decisions, the country could very likely emerge stronger post-Covid-19. However, as investors, we cannot bank on hope and must instead ensure that we position our clients' portfolios for the risks and opportunities that are arising.

THE VALUATION OF SOUTH AFRICAN GOVERNMENT BONDS REMAINS ATTRACTIVE

10-year SAGBs currently trade at a yield of 11% compared to cash, which we expect to be around 4.25% by the end of this year. The spread between SAGBs and cash is at the widest it has been since the start of inflation targeting (2001) and implies that 10-year SAGBs can sell-off by 100bps over the next year before they start to underperform cash. In addition, with inflation expected to average close to 4% over the next two years, the implied real yield on the 10-year SAGB is close to 7% (Figure 1, page 32).

Global policy rates have moved to zero and are expected to remain there for some time to come. As mentioned, developed market central banks have restarted their QE programmes on a scale larger than those implemented during the GFC, and the level of monetary policy accommodation and support that has been pushed into the global economy is unprecedented. Global developed market bonds either trade in deeply negative territory or very close to zero. 10-year SAGBs now trade in excess of 10% above developed market bonds (Figure 2, page 32).

Emerging market local currency bonds have all moved weaker during the crisis, but South Africa remains the cheapest real yield and the cheapest tradeable nominal yield among its peers (Table 1).

The SARB's commitment to keep liquidity in the system and the National Treasury's adjustment to the funding profile over this period have seen the yield curve flatten quite aggressively past 20-year maturity. In running our total return calculations, we believe that bonds in the 10- to 12-year bucket offer the most value. Table 2 shows how much bonds can sell off before their return equals that of the ALBI, and how much they can sell off before they can match the return of 10-year SAGBs (Figure 3).

Globally, credit spreads have blown out. South Africa's sovereign credit spread was already trading at a level consistent with other subinvestment grade countries, but is now trading 100bps wider than even the Subinvestment Grade >

Table 1

EMERGING MARKET YIELD MOVES

	Nominal yield	Implied real yield	5-year change in nominal yield	5-year change in real yield
Turkey	12.74	2.07	5.05	1.28
South Africa	**11.65**	**6.79**	**4.15**	**4.89**
Brazil	8.62	4.84	(3.34)	(0.61)
Mexico	7.96	4.37	2.04	2.06
Indonesia	7.84	4.44	0.15	2.80
Russia	7.06	3.36	(3.65)	(0.44)
India	6.13	2.00	(1.84)	(0.73)
Average	**5.57**	**1.92**	**(0.07)**	**0.37**
Chile	3.87	0.74	0.700	0.87
Malaysia	3.30	1.50	(0.58)	1.18
China	2.60	(0.10)	(0.94)	(1.11)
Hungary	2.27	(0.95)	(1.32)	(1.92)
Poland	1.80	(0.97)	(0.70)	(1.96)
Czech Republic	1.28	(1.12)	0.57	(0.09)
Israel	0.95	(0.05)	(1.26)	(1.04)

Sources: Bloomberg, Coronation

Figure 3

THE 10-YEAR VERSUS THE 30-YEAR SOUTH AFRICAN GOVERNMENT BOND SPREAD

Sources: Bloomberg, Coronation

Table 2

SOUTH AFRICAN GOVERNMENT BOND BREAKEVEN RATES

Bond	Maturity	Yield	Breakeven relative to ALBI	Breakeven relative to R2030
R186	21 Dec 26	10.60%	(1.1%)	(1.4%)
R2030	31 Jan 30	11.68%	0.1%	
R2032	31 Mar 32	12.12%	0.4%	0.2%
R2035	28 Feb 35	12.24%	0.4%	0.2%
R2040	31 Jan 40	12.35%	0.4%	0.2%
R2044	31 Jan 44	12.35%	0.4%	0.2%

Sources: Bloomberg, Coronation

Index, as shown in Figure 4. Even if one assumes this is correct, the absolute level of sovereign credit spreads is very much elevated, suggesting potential room for compression.

In constructing a fair value estimate for 10-year SAGBs, we use the global risk-free rate (the US 10-year Treasury Bond), the inflation differential between South Africa and the US, and the South African sovereign credit spread. In Table 3, both based off current market variables and expected values for those variables, we believe 10-year SAGBs are trading at levels 120bps to 220bps above fair value. This is just one of the many models we use to determine the fair value for the 10-year SAGB, but it is the simplest and easiest to understand.

FIVE- AND 10-YEAR INFLATION-LINKED BONDS ARE ATTRACTIVE

ILBs have sold off, both in sympathy with nominal bonds and due to lower inflation expectations. However, given the higher modified duration of most of these bonds, they have underperformed their nominal counterparts. In Table 4, we list a few key ILBs, their current real yield, and their implied breakeven (where inflation has to average in order for their return to equal that of the nominal bond equivalent). In five- and 10-year ILBs, real yields are close to 6%, with breakeven inflation well below 5%. We consider these to be very attractive and they warrant a healthy allocation in our portfolios.

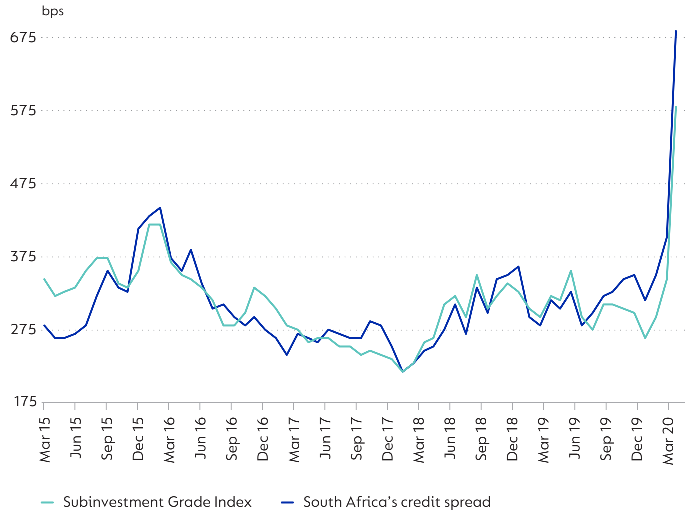
OUR BIGGEST CONCERN IS THE LOCAL CREDIT MARKET

Fundamentally, we believe that South African corporate credit spreads should already have been under pressure, given the poor economic fundamentals of the country and the clear evidence that the probability of default for most borrowers is on the rise. A clear indication of this was shown in the rising credit loss ratios reported by all our local banks during their last updates. However, there has been a drop in corporate issuance due to the poor growth backdrop and the lack of the funding needed by banks and corporates (due to the lack of investment in the country). Leading into the crisis, with issuance lower and a reach for yield in the local market spurred by the reduction in the return expectations of many other asset classes, local credit spreads compressed aggressively. The economic fallout of the Covid-19 crisis will add further stress to balance sheets of South African companies, hence lowering their credit quality. As such, it is reasonable to expect a widening of credit spreads just based on the fundamental deterioration. Add to this the repricing we are seeing in global credit markets, the drop in risk appetite, an acceleration of redemptions from fixed income funds in lieu of cash and a tightening of credit spreads over the last 12 months, and one can easily see that this is a market that needs sobering.

Coronation's bottom-up, valuation-driven credit research process takes both fundamentals and liquidity into consideration in its assessment of risk and return. This ensures that we build a level

Figure 4

SOUTH AFRICA VERSUS THE SUBINVESTMENT GRADE INDEX



Sources: Bloomberg, Coronation

Table 3

SOUTH AFRICAN 10-YEAR GOVERNMENT BOND VERSUS US 10-YEAR TREASURY BOND FAIR VALUE

	Current	Normalised
US 10-year inflation expectations	0.68	1.75
South African 10-year inflation expectations	4.50	4.50
US yield	1.00	2.00
South Africa's credit spread	6.140	5.140
Fair value	**10.320**	**9.390**
Current South African 10-year	11.60	11.60
	1.28	2.21

Sources: Bloomberg, Coronation

Table 4

INFLATION-LINKED BOND YIELD AND BREAKEVEN

	Real yield	Implied breakeven inflation
2-year	3.4000	2.42
5-year	5.6000	3.04
9-year	6.2000	4.81
18-year	6.5500	5.44
30-year	6.3000	5.64

Sources: Bloomberg, Coronation

of conservatism into our pricing expectations to deal with the illiquid nature of certain assets. In addition, liquidity plays a vital role in our portfolio construction process. Over the last 18 months, we have endeavoured to reduce our exposure to listed credit by reducing our exposure to new-style bank subordinate debt (AT1 and AT2), certain bank senior issues and not actively purchasing new issues in the primary market. Our current holdings of credit instruments are shorter dated in nature, predominantly issued by the big four banks and are listed on the JSE, making them tradeable in some part.

Globally, credit spreads have widened tremendously, as have the credit spreads of South African companies that issue offshore debt. The Sasol two-year bond trades at a yield of 22% in US dollars, and Standard Bank and First Rand Limited Tier 2 sub-debt bonds now trade at yields of 10% in US dollars. In the local market, however, these bonds have not re-marked at all, with Sasol two-year debt still marked at 134bps over Jibar (6.8% all-in yield) and the banks' four-year sub debt still marked at 250bps over Jibar (8.1% all-in yield).

These bonds are generally illiquid and are held by local institutions. We expect them to only re-mark in the secondary market when they are sold. We view it as just a matter of time before we see a significant re-mark in these debt instruments as redemptions intensify and forced selling pushes spreads to levels like those seen in the offshore market.

At the end of February, shorter-dated fixed-rate negotiable certificates of deposit (NCDs) traded at 6.89% (three-year) and 8.25% (five-year). Shorter-dated NCDs have pulled lower due to the significant cut in interest rates by the SARB, while the five-year levels have pushed wider, due to the widening in credit spreads and sell-off in bond yields. The spreads of floating-rate NCDs have been unappealing to the fund over the last few quarters. Covid-19 will place the economy under severe pressure, leading to a broad-based deterioration in credit quality. In addition, interbank liquidity has reduced significantly, which has resulted in significant movements in bank NCD floating rate spreads. The entire curve has shifted wider by between 35bps and 45bps, putting five-year floating rate NCDs at 3mJ+150bps and one-year floating rate NCDs at three-month Jibar+112bps. Short-dated fixed-rate NCDs continue to hold appeal due to the inherent protection offered by their yields and relative to our expectations for a lower repo rate. In addition, NCDs have the added benefit of being liquid, thus aligning the liquidity of the fund with the needs of its investors. Longer-dated NCDs, although at fairly extended levels, are still at risk of further widening, which keeps the fund cautious in adding them to the portfolio.

LISTED PROPERTY LOOKS CHEAP AT FACE VALUE, BUT YOU NEED TO LOOK UNDER THE HOOD

The local listed property sector was down 36.5% in March, bringing its return for the rolling 12-month period to -48.1%. Listed property has been the largest drag on the fund's performance, despite a low allocation of 3.2% at the start of the quarter. The local listed property sector has grown tremendously over the last 10 years into a meaningful part of financial markets, with a market capitalisation of almost R300 billion. However, not all listed property companies are the same. Each one has varying exposure to different sectors (retail, office and industrial), varying underlying asset quality and varying financial constraints. In the last five years, many have chosen to diversify away from South Africa and enter highly leveraged plays on offshore property. This has resulted in a general rise in balance sheet risk across the sector. The current crisis will reduce rental income, put pressure on asset values, increase the cost of borrowing for lower-quality businesses and test inexperienced management teams. It is entirely possible that most of the companies will require additional capital and that dividends are suspended to preserve capital. Currently, dividend yields are eye-watering, touching close to 30% in some of the large-cap names. However, one must be cautious not to take these at face value and understand how the key issues mentioned above affect that yield. Dividends could be suspended and a 30% historic yield could become zero one year out. We believe there are a few select large-cap counters that satisfy our stringent conditionality. These include Growthpoint, Liberty Two Degrees and Redefine. These are all counters in which we currently have holdings across our multi-asset funds and in which we would take more meaningful stakes in time to come.

THE LOCAL LISTED PROPERTY SECTOR HAS GROWN TREMENDOUSLY OVER THE LAST 10 YEARS INTO A MEANINGFUL PART OF FINANCIAL MARKETS, WITH A MARKET CAPITALISATION OF ALMOST R300 BILLION.

The FTSE/JSE Preference Share Index was down 27.0% over March, bringing its 12-month return to -22.3%. The change in capital structure requirements mandated by Basel III will discourage banks from issuing preference shares. This will limit availability. Despite attractive valuations, this asset class will continue to dissipate, given the lack of new issuance and because it risks being classified as eligible loss-absorbing capital (only senior to equity). Over the month, we have seen a significant reprice in instruments that rank equivalent to preference shares in their capital structure,

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suggesting there might be further downside for this illiquid asset class. The fund maintains select exposure to certain high-quality corporate preference shares, but will not actively look to increase its holdings.

POSITIONING OF THE PORTFOLIO: CAUTIOUS AND VIGILANT

We view 10-year SAGBs as the most attractive asset in the fixed income universe, with five- to 10-year ILBs coming in a close second. Listed property looks attractive, but allocations need to be made on a stock-specific basis, with careful consideration paid to the issues outlined above. Local credit markets are very unattractive, and we would wait for a significant widening in credit spreads before allocating more capital. We will instead use the little credit that we have, given that it is shorter dated, as a funding source for the other more attractive asset classes.

We remain vigilant of risks emanating from the dislocations between stretched valuations and the underlying fundamentals of the local economy. However, we believe that the fund's current positioning correctly reflects appropriate levels of caution. The fund's yield of 9.08% 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.

We remain committed to only adding assets to our clients' portfolios that we believe offer a sufficient margin of safety and are adequately priced for the underlying risk. We are constantly on the prowl for valuation dislocations relative to fundamentals, which we believe will benefit our client portfolios over the longer term. In this volatile period, asset price behavior tends to be irrational, which will adversely affect short-term performance. It is during times like this that once-in-a-lifetime opportunities present themselves, and one has to stand ready to act with conviction in order to take advantage of these opportunities.

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. +

Global Equity Select, Global Managed and Global Capital Plus Funds

By NEIL PADOA, LOUIS STASSEN and HUMAIRA SURVE

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

Louis is a founding member and former chief investment officer of Coronation, with 30 years of investment industry experience.

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

IN LAST QUARTER'S commentary we wrote, *'2019 was a year to make money'*. However, we also cautioned that, *'after a sustained period of strong equity returns, declining interest rates, reduced tax rates, expanding profit margins, and rising valuation multiples, investors should recalibrate return expectations lower. The conditions in place today are quite different to those in place a decade ago. We have no insight into short-term market moves but feel that absolute returns could very well be lower over the next ten years compared to the last ten.'*

Well, we didn't have to wait long. Risk assets plunged over the quarter as the economic consequences of the Covid-19 pandemic started to become apparent (for a full discussion, please see Coronation's commentary on page 6). Economic activity in many countries and sectors around the world has come to a halt. This unprecedented 'full stop' caused stress and market dislocations across the spectrum. Volatility was back with a vengeance, and, in both credit and equity markets, indicators spiked to levels above those seen in the Global Financial Crisis (figures 1 and 2).

With this as a backdrop, Global Equity Select declined -22.6% in US dollars for the quarter, slightly behind the benchmark's -21.4%. Given the weak rand, this translated into a rand decline of -1.9% for the Global Equity Select Feeder Fund. Quarterly returns will inevitably be noisy, but we were cognisant of the high relative base of performance coming into the year following a strong 2019, which delivered 11% outperformance, and are reasonably satisfied to have at least protected these relative gains.

Global Managed declined -16.4% for the quarter compared to -13.3% for the benchmark, while the Global Managed Feeder Fund returned 6.5% in rand. The fund's equity holdings were marginally behind the benchmark over the quarter. Global Capital Plus declined -9.7% for the quarter compared to 0.8% for the benchmark, while the Global Capital Plus Feeder Fund returned 14.8% in rands. This fund's equity portfolio was appropriately sized, selected and hedged. The negative contribution from equities was just over 5%. The stocks themselves performed in line with the overall market, and index-level hedges reduced losses by a quarter.

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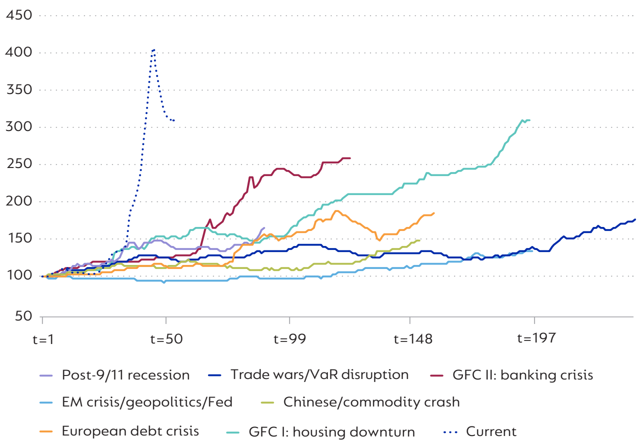
Figure 1

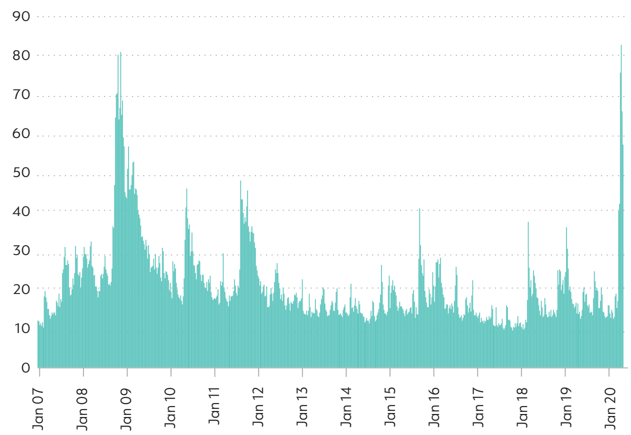
US INVESTMENT GRADE CREDIT SPREADS (RE-BASED TO THE START OF VARIOUS CRISES)



Source: ICE Bank of America

Figure 2

THE VOLATILITY INDEX (MEASURES EXPECTED VOLATILITY OF THE S&P500 INDEX)



Source: Bloomberg

The underperformance in both funds was primarily due to the non-equity securities in their portfolios. The lack of developed market government bond exposure was the primary culprit, as we have chosen instead to take some credit risk, which sold off as credit spreads increased. Importantly, these are mark-to-market losses, not permanent impairments, as we either still hold those securities or have rotated into issues with a more favourable risk-reward profile. While the quarterly declines are disappointing, it follows on a strong 2019, with alpha of 5% and 10% for Global Managed and Global Capital Plus, respectively. Although we are never satisfied with underperformance, we are excited by a much-improved opportunity set, which is most important for potential future returns. Following such a dramatic quarter, it is also worth reflecting on some of the additional aims for managing Global Capital Plus and Global Managed as outlined in last quarter's commentary. In particular the third point:

'Do not expose the funds to excessive risk, even if such exposures represent large asset classes which, in a normal environment, would be well-suited to their strategies (such as developed market government bonds today).'

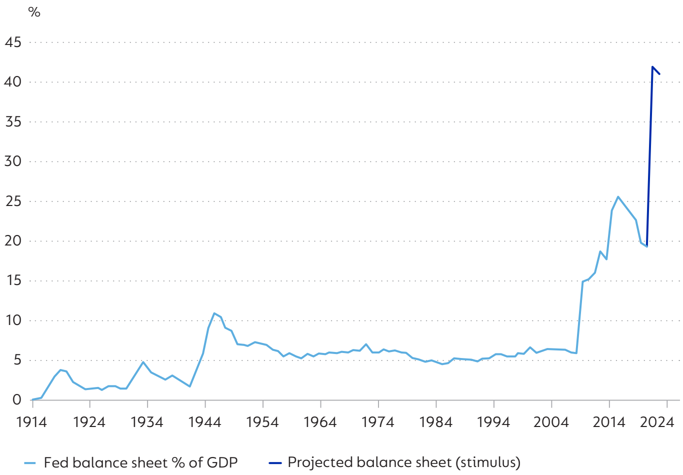
The fiscal and monetary response to the Covid-19 pandemic is unprecedented. Aggressive monetary measures are pumping vast amounts of liquidity into the system, causing central bank balance sheets to surge, while fiscal deficits are also set to explode once economic support is factored into government finances. Data for the US is shown in figures 3 and 4, but it is mirrored (to varying degrees) in Europe, Japan, China and the UK.

Notwithstanding the current recessionary conditions, which Morgan Stanley believes could be the fastest and steepest recession in history, resulting in spare capacity and economic slack, the world will eventually get back to work. From this low base of activity, pent-up demand (combined with huge stimulus) could be highly inflationary. In this scenario, the US experience after World War II is instructive and highlights the material underperformance, and declining purchasing power, of cash and government bonds (Figure 5). This is in stark contrast to the last few decades, during which bonds have been the ultimate low volatility, low risk, uncorrelated, and real return-generating asset:

- Since 1990 (30 years), the global bond index returned 5.7% p.a., less than 1% behind global equities, with a fraction of the volatility and drawdown risk.
- Since 2000 (20 years), the global bond index has beaten equities by c.0.5% p.a.

Figure 3

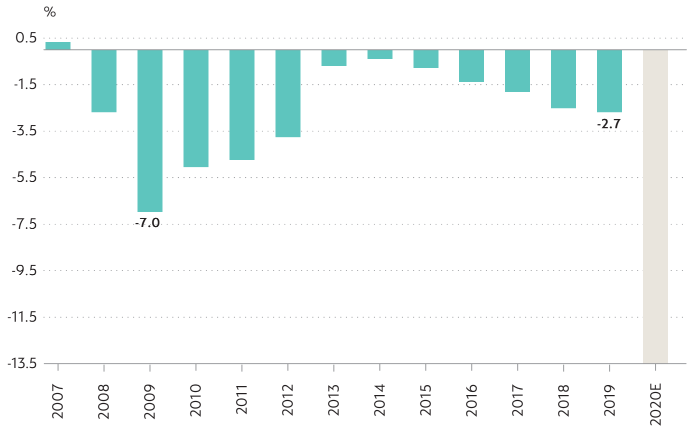
US FEDERAL RESERVE BALANCE SHEET (% OF GDP OVER LAST 100 YEARS)



Source: Bank of America Global Research

Figure 4

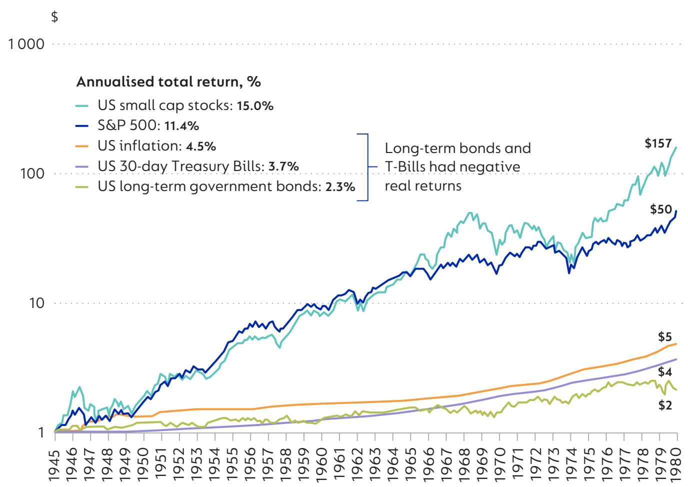
US PRIMARY BALANCE (% OF GDP, CYCLICALLY ADJUSTED)



Sources: Haver Analytics, Morgan Stanley Research forecast

Figure 5

CUMULATIVE TOTAL RETURN OF $1 FROM 1945-1980



Sources: Morgan Stanley Wealth Management GIC using data provided by Morningstar/©2020 Morningstar. Inc

As bonds approach the zero bound, the asymmetry of returns skews increasingly one way. Yields cannot be forever compressed, so the upside potential is limited (bond prices go up when yields go down). However, poor prospective returns from rates simply staying where they are, negative real returns from monetary debasement and negative absolute returns from a rise in interest rates are all possibilities.

While the inflationary scenario outlined above is only one potential outcome, it does inform our positioning and we continue to hold no developed market government bonds in Global Managed and Global Capital Plus. In turn, we have built positions in assets that should perform well in an inflationary environment. Aside from the allocation to risk assets (equity, property and infrastructure), which comprised 64% in the case of Global Managed and 37% in the case of Global Capital Plus at quarter-end, we also have 10% to 11% of the funds' portfolios in gold and inflation-protected securities.

KEY PORTFOLIO ACTIONS

1. Active management of equity exposure

Walking through the changes in a volatile quarter such as this will help to illustrate the process. Global Managed started the quarter with 60% effective exposure to equities. On 27 February, with markets not far off their highs (the MSCI All Country World Index was 522), exposure troughed below 55%, as we grew concerned about the potential fall-out from the virus amidst fairly widespread complacency in the market. Equity exposure peaked at 64% on 25 March (index level 428, c.20% lower). Global Capital Plus started the quarter with 30% effective exposure to equities. On 27 February, exposure troughed at 25% and peaked at 32.7% on 31 March (index level 442, c.15% lower). Considering the decline in the markets and the increase in exposure, one can see the funds were meaningful net buyers into the decline. While we will never time these actions perfectly, with a disciplined, rational process and a valuation philosophy that is rooted in the long term, we aim to have lower equity exposure when risks and valuations are high, and higher exposure when prospective returns are higher. Simple, but not easy.

2. Changes in equity holdings

Most of our large holdings going into the quarter were well positioned for the coming economic stress. In the top 10, Chinese internet businesses Tencent (via Naspers) and Alibaba are arguably net beneficiaries, being leaders in gaming and ecommerce. Charter Communications, a broadband provider in the US, is seeing much higher demand for their essential internet service, although the business is not immune, and cord-cutting will accelerate and subscriber growth will slow as the unemployment wave hits. Tobacco businesses Philip Morris and British American Tobacco have seen stable demand. Airbus is an obvious exception. With entire countries in lockdown and many airlines around the world facing bankruptcy, orders of new aeroplanes are being delayed and cancelled. The stock ended down more than 50%. Airbus has a net cash balance sheet, which should see it through this crisis. Deliveries will be cut substantially over the next couple of years, but, looking through this extended period of disruption, our estimate of normalised earnings power justifies a significantly higher share price.

AIRBUS HAS A NET CASH BALANCE SHEET, WHICH SHOULD SEE IT THROUGH THIS CRISIS.

The funds took advantage of a few anomalies – good businesses that initially sold off in line with the market, but whose prospects had only changed marginally. Unilever is a case in point. The stock traded close to 14 times earnings, and with a dividend yield of nearly 4.5% at the lows, which we thought provided good value – in particular when the potential range of outcomes for the average business had widened so considerably. We also re-entered Diageo and bought stocks such as Intercontinental Exchange and Thermo Fisher.

Earlier in the quarter we exited or reduced holdings that had performed strongly and approached our estimates of fair value. Adidas, Blackstone and Apollo were all sold.

3. Other changes

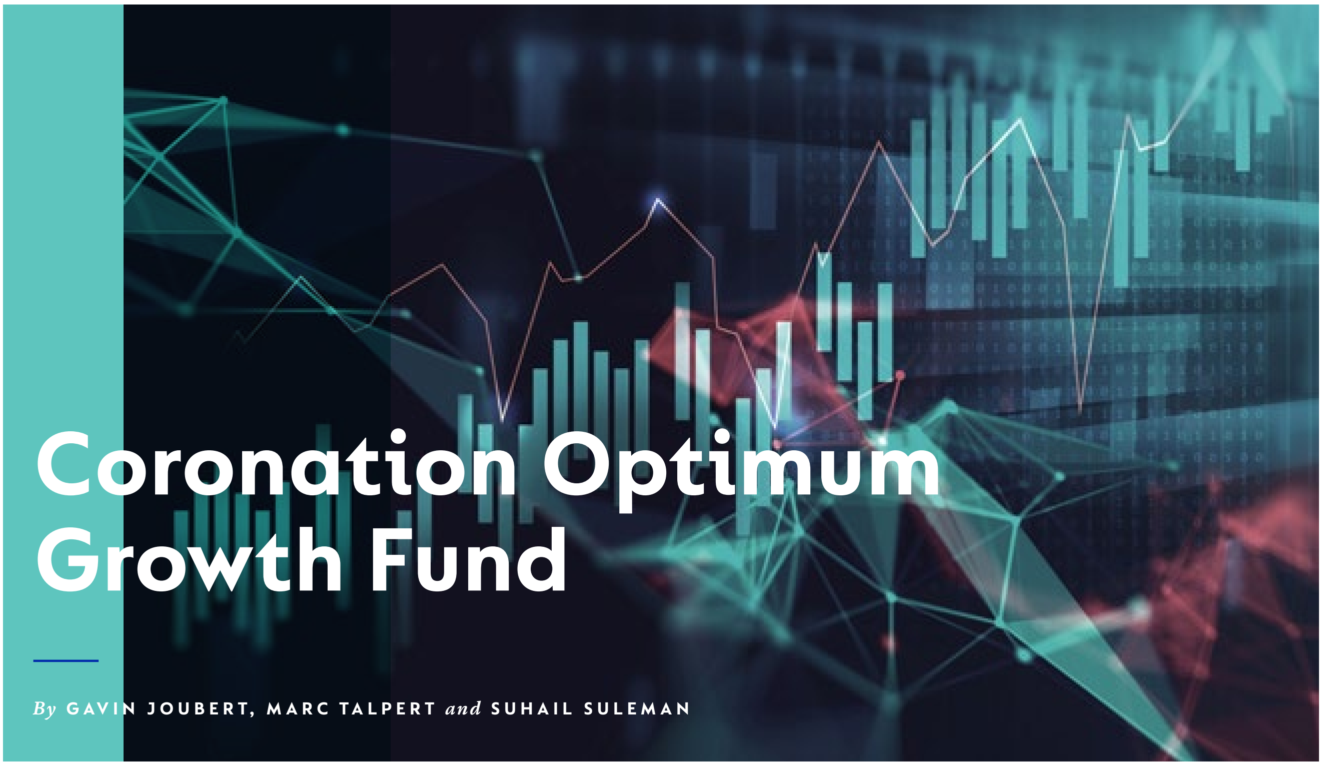
Within credit, the most meaningful portfolio actions centred on investment-grade credits to take advantage of dislocated credit spreads (as shown in Figure 1, page 37). While these actions don't dramatically change the return profile of the portfolio, they help at the margin. Examples of near-dated issues that were purchased include:

- Berkshire Hathaway (AA-rated) August 2021s were bought at a credit spread of 250 basis points (bps) over Treasuries.
- GlaxoSmithKline (A-rated) May 2022s were bought at a credit spread of 290bps.

OUTLOOK

Markets could very well remain volatile as the nature of the pandemic evolves and progresses. As a team, we are focused (as always) on researching individual businesses, assessing their long-term earnings power, understanding the potential impact this black swan event may have on the investment case, managing risk and adjusting the portfolio accordingly. While the backdrop has changed dramatically, our process hasn't.

Thank you for your continued support and interest in the funds. +



Coronation Optimum Growth Fund

By GAVIN JOUBERT, MARC TALPERT *and* SUHAIL SULEMAN

Gavin is Head of Global Emerging Markets and has 21 years of investment industry experience.

Marc is a portfolio manager with six years of investment industry experience.

Suhail is a portfolio manager with 18 years of investment industry experience.

THE FUND APPRECIATED 4.7% in the first quarter of 2020, compared with the benchmark's negative 6.0% return, resulting in 10.6% alpha for the period. During a very volatile period with extreme downward moves, it was pleasing to both generate alpha and a positive absolute return.

With the fund being a fully flexible fund, it was encouraging to see asset allocation was a large contributor towards the quarter's performance. A collection of index put options was the largest contributor (4.4% positive impact), as various global indices turned heavily negative, and these options provided valuable protection. This was followed by a US dollar cash position (+28%, 1.5% positive impact), with the final noteworthy positive contributor being a gold bullion holding (+33%, 0.8% positive impact). Unfortunately, the fund still incurred losses on a few individual positions, with the largest being Unibail-Rodamco-Westfield (-51%, 1.4% negative impact), followed by Airbus (-44%, 1.1% negative impact) and Capri Holdings (-61%, 1.0% negative impact).

Over the past five years, the fund has generated a positive return of 10.7% p.a., 14.7% p.a. over 10 years and 14.3% p.a. (3.4% annualised outperformance) since inception over 20 years ago[1].

[1] Launch date: 15 March 1999
Highest annual return 51.1% Jan 2013 - Dec 2013; Lowest annual return (31.5%) Mar 2008 - Feb 2009

The fund ended the quarter with 73% net equity exposure, slightly more than at the end of December. However, it should be noted that, during the quarter, net equity exposure was as low as 59%, with this having increased towards the end of the quarter as the fund started buying equities post the sell-off. Of this, approximately 54% of the equity exposure was invested in developed market equities and 46% in emerging market equities.

Our negative view on global bonds remained unchanged, as a large portion of developed market sovereign bonds offer negative yields to maturity, with the follow-on effect that most corporate bonds also offer yields which do not compensate you for the risk undertaken. Only 1.3% of the fund is invested in bonds, which is largely made up of a 0.7% position in L Brands (owner of Victoria's Secret) corporate bonds.

The fund also has c.4.5% invested in global property, largely Unibail (European and US retail property) and Vonovia (German residential property). Lastly, the fund has a physical gold position of 2.7%, along with a 1.5% holding in Barrick Gold Corp., the largest gold miner globally. The balance of the fund is invested in cash, largely offshore. As has been the case for many years, the bulk of the fund (over 90%) is invested offshore, with very little exposure to

South Africa, barring some small new buys made during the quarter which collectively amount to just over 3% of the fund.

The disappointing performance of Unibail was driven by government-imposed lockdowns across Europe, forcing many of their tenants to close, with many now either refusing to pay rent or requesting some form of relief. We acknowledge that some sort of relief will most likely be granted, which will negatively impact cashflow in the short term; however, we are encouraged by Unibail proactively enhancing their liquidity position while cancelling the second half of their previously announced dividend. This provides them with enough liquidity to ensure they can meet all their obligations, even in a severely stressed scenario. The extreme downward share move (down c.60% in euro since January 2020) is unwarranted in our view – the business now trades at levels last seen over 20 years ago, reflecting a 75% discount to net asset value. Notwithstanding the very real pressures on retail property during this crisis, we feel Unibail will survive the crisis and ultimately, the share will begin to trade at a price more reflective of its underlying fundamentals.

Notable buys during the quarter were Phillip Morris International (PMI), Barrick Gold Corp. and EssilorLuxottica.

PMI was an existing holding in the fund, which was increased materially (247 basis points bought) over the quarter as the stock fell 30% (in US dollars) from its peak in the Covid-19-induced panic. As the business is exposed to a consumption habit which is addictive and has largely been defensive in weak economic environments, we felt that the fall, which was in excess of the total market, was not warranted, as we feel there is little fundamental long-term impact to the business. It currently trades on c.13 times forward earnings with a 7% dividend yield, which we view as highly attractive.

Barrick Gold Corp. is the product of a merger between legacy miner Barrick and Randgold, with Mark Bristow, the former Randgold CEO, taking the helm of the combined entity. This is notable, as Mark Bristow brings with him both a track record of exceptional operational execution and good capital allocation - a skill very hard to find in the gold mining industry. We expect Mark to apply his expertise to the legacy Barrick assets, which should generate a significant amount of value in the long term.

EssilorLuxottica is the global leader in design, manufacture and distribution of ophthalmic lenses, frames and sunglasses. The merger of Essilor and Luxottica created a vertically integrated player with extensive distribution and global retail reach. The segments which drive their long-term business, being corrective eyewear and sun protection eyewear, have large structural tailwinds due to increasing penetration of their products, along with a growing addressable market due to increasing incidences of myopes (near-sightedness) and presbyopes (age-related far-sightedness). The share fell 30% (in euros), allowing the fund to purchase a stake in a high-quality business at a reasonable price. The business should be able to consistently grow earnings at mid- to high single-digits over the foreseeable future as its end-market expands, it realises synergies from the merger and leverages the significant Luxottica global retail footprint to sell Essilor lenses.

The future is always inherently difficult to predict, and this has been further compounded by Covid-19. However, we feel the fund has been constructed in a manner to ensure the highest risk-adjusted returns are achieved, while considering a very uncertain backdrop. As always, our greatest focus is delivering to our client expectations, and during this current crisis, this focus is as strong as ever. ✚

THE MERGER OF ESSILOR AND LUXOTTICA CREATED A VERTICALLY INTEGRATED PLAYER WITH EXTENSIVE DISTRIBUTION AND GLOBAL RETAIL REACH.

Domestic flagship fund range

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

INVESTOR NEED

	INCOME ONLY	INCOME AND GROWTH		LONG-TERM CAPITAL GROWTH	
FUND	**STRATEGIC INCOME** Cash†	**BALANCED DEFENSIVE** Inflation†	**CAPITAL PLUS** Inflation†	**BALANCED PLUS** Composite benchmark† (equities, bonds and cash)	**TOP 20** FTSE/JSE CAPI†
FUND DESCRIPTION	Conservative asset allocation across the yielding asset classes. Ideal for investors looking for an intelligent alternative to cash or bank deposits over periods from 12 to 36 months.	A lower risk alternative to Capital Plus for investors requiring a growing regular income. The fund holds fewer growth assets and more income assets than Capital Plus and has a risk budget that is in line with the typical income-and-growth portfolio.	Focused on providing a growing regular income. The fund has a higher risk budget than the typical income-and-growth fund, making it ideal for investors in retirement seeking to draw an income from their capital over an extended period of time.	Best investment view across all asset classes. Ideal for pre-retirement savers as it is managed in line with the investment restrictions that apply to pension funds. If you are not saving within a retirement vehicle, consider Market Plus, the unconstrained version of this mandate.	A concentrated portfolio of 15-20 shares selected from the entire JSE, compared to the average equity fund holding 40-60 shares. The fund requires a longer investment time horizon and is an ideal building block for investors who wish to blend their equity exposure across a number of funds. Investors who prefer to own just one equity fund may consider the more broadly diversified Coronation Equity Fund.
INCOME VS GROWTH ASSETS[1] ● INCOME ● GROWTH	97.1% 2.9%	62.2% 37.8%	50.4% 49.6%	27.6% 72.4%	1.3% 98.7%
LAUNCH DATE	Jul 2001	Feb 2007	Jul 2001	Apr 1996	Oct 2000
ANNUAL RETURN[2] (Since launch)	9.8% 7.7%†	8.3% 5.9%†	10.6% 5.8%†	13.1% 12.1%†	15.5% 11.7%†
QUARTILE RANK (Since launch)	1st	1st	1st	1st	1st
ANNUAL RETURN (Last 10 years)	8.1% 6.2%†	8.0% 5.1%†	6.5% 5.1%†	8.0% 9.1%†	7.8% 7.2%†
STANDARD DEVIATION (Last 10 years)	2.1% 0.2%†	5.0% 1.2%†	6.5% 1.2%†	8.8% 8.2%†	13.7% 13.3%†
FUND HIGHLIGHTS	The fund remains the top performing fund in its category since launch in 2001 and outperformed cash by 2.1% over this period.	Outperformed inflation by 2.4% p.a. (after fees) since launch, while producing positive returns over 12 months more than 99% of the time.	Outperformed inflation by 4.8% p.a. (after fees) since launch, while producing positive returns over 24 months more than 99% of the time.	No. 1 balanced fund in South Africa since launch in 1996, outperforming its average competitor by 1.6% p.a. Outperformed inflation by on average 6.9% p.a. since launch and outperformed the ALSI on average by 1.4% p.a (since launch).	The fund added 3.8% p.a. to the return of the market. This means R100 000 invested in Top 20 at launch in Oct 2000 grew to more than R1.6 million by end March 2020. The fund is a top quartile performer since launch.

[1] *Income versus growth assets as at 31 March 2020. Growth assets defined as equities, listed property and commodities (excluding gold).*

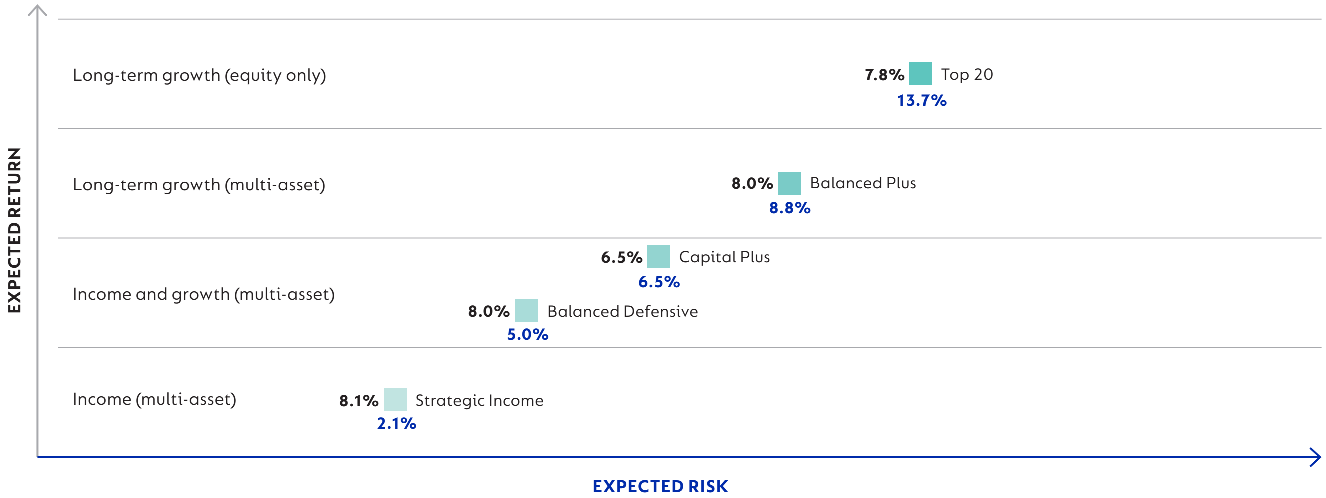
[2] *Highest annual return*
Balanced Defensive: 21.2% (Jun 2012 - May 2013); Balanced Plus: 49.3% (Aug 2004 - Jul 2005); Capital Plus: 33.8% (Aug 2004 - Jul 2005); Strategic Income: 18.7% (Nov 2002 - Oct 2003); Top 20: 68.9% (May 2005 - Apr 2006)

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

Figures are quoted from Morningstar as at 31 March 2020 for a lump sum investment and are calculated on a NAV-NAV basis with income distributions reinvested.

RISK VERSUS RETURN

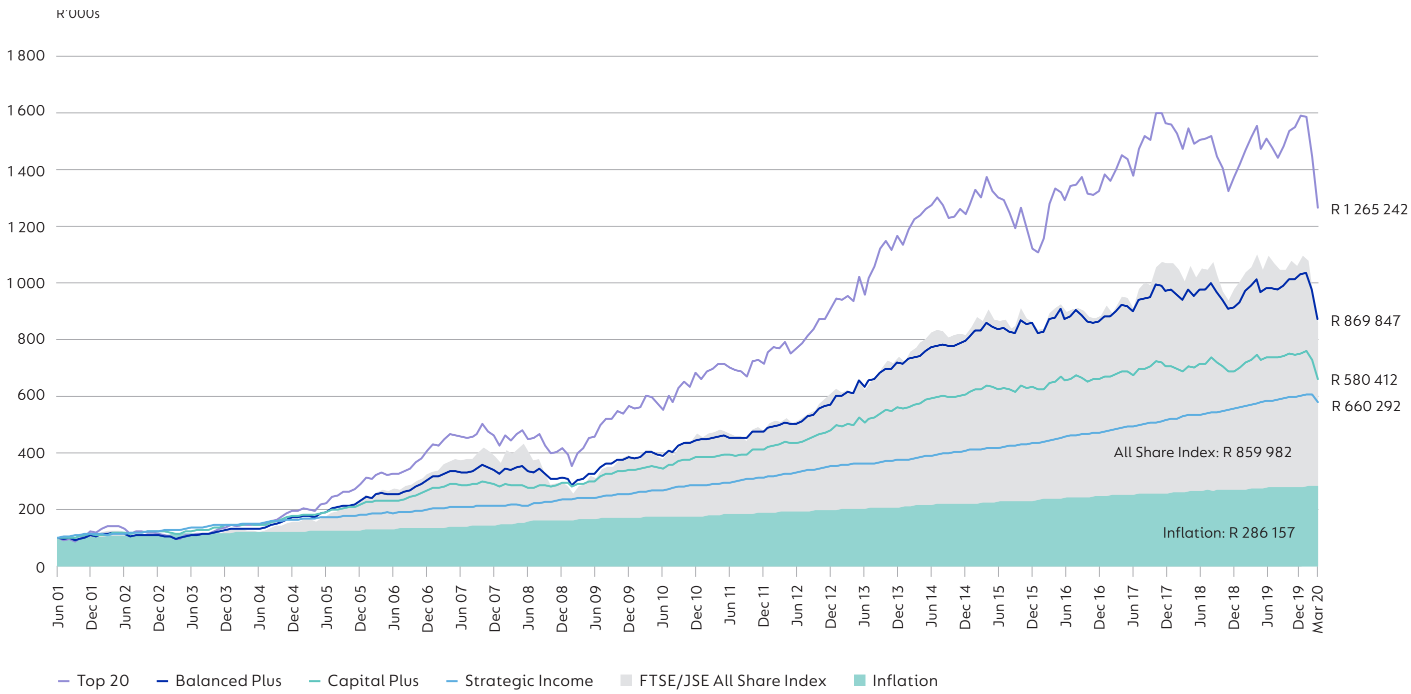
10-year annualised return and risk (standard deviation) quoted as at 31 March 2020.
Figures quoted in ZAR after all income reinvested and all costs deducted.



Source: Morningstar

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

Value of R100 000 invested in Coronation's domestic flagship funds since inception of Capital Plus on 2 July 2001 as at 31 March 2020. All income reinvested for funds; FTSE/JSE All Share Index is on a total return basis. Balanced Defensive is excluded as it was only launched on 1 February 2007.



Source: Morningstar

International flagship fund range

INVESTOR NEED

	DEPOSIT ALTERNATIVE	CAPITAL PRESERVATION	LONG-TERM CAPITAL GROWTH (MULTI-ASSET)	LONG-TERM CAPITAL GROWTH (EQUITY ONLY)	
FUND[1]	**GLOBAL STRATEGIC USD INCOME** US dollar cash (3 Month Libor)†	**GLOBAL CAPITAL PLUS** US dollar cash (3 Month Libor)†	**GLOBAL MANAGED** Composite (equities and bonds)†	**GLOBAL OPPORTUNITIES EQUITY** MSCI ACWI†	**GLOBAL EMERGING MARKETS** MSCI Emerging Markets 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.	A diversified portfolio of the best global equity managers (typically 6-10) who share our investment philosophy. An ideal fund for investors who prefer to own just one global equity fund. Investors who want to blend their international equity exposure may consider Coronation Global Equity Select, which has more concentrated exposure to our best global investment views.	Our top stock picks from companies providing exposure to emerging markets. The US dollar fund remains fully invested in equities at all times, while the rand fund will reduce equity exposure when we struggle to find value.
INCOME VS GROWTH ASSETS[2] ● INCOME ● GROWTH	95.8% 4.2%	61.3% 38.7%	32.7% 67.3%	0.3% 99.7%	4.2% 95.8%
LAUNCH DATE OF OLDEST FUND	Dec 2011	Nov 2008	Oct 2009	Aug 1997	Dec 2007
ANNUAL RETURN[3] (Since launch)	1.9% 1.0%†	4.2% 0.9%†	4.7% 5.3%†	5.1% 5.1%†	1.2% (0.5%)†
QUARTILE RANK (Since launch)	–	1st	1st	–	1st
ANNUAL RETURN[3] (Last 5 years)	0.7% 1.5%	1.1% 1.5%	0.5% 3.2%	(1.7%) 3.1%	(0.3%) (0.3%)
ANNUAL RETURN[3] (Last 10 years)	–	2.4% 0.9%	4.2% 5.1%	3.6% 6.8%	1.5% 0.9%
QUARTILE RANK (Last 5 years)	–	1st	2nd	–	3rd
FUND HIGHLIGHTS	Outperformed US Dollar cash by 0.9% p.a (after fees) since launch in December 2011.	The fund has outperformed US Dollar cash by 3.3% p.a. (after fees) since launch in 2008.	Number one global multi-asset high equity fund in South Africa since launch in October 2009.	The fund seeks to give investors access to some of the best fund managers across the globe.	Both the rand and dollar versions of the fund have outperformed the MSCI Emerging Markets Index by more than 1.9% p.a. since their respective launch dates.

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 March 2020 (for US dollar funds). Growth assets defined as equities, listed property and commodities (excluding gold).*

3 *Returns quoted in US dollar for the oldest fund.*

Highest annual return
Global Strategic USD Income: 7.1% (Jan 2012 - Dec 2012); Global Capital Plus [ZAR] Feeder: 31.4% (Mar 2009 - Feb 2010); Global Managed [ZAR] Feeder: 23.1% (Jul 2010 - Jun 2011); Global Emerging Markets Flexible [ZAR]: 96.0% (Mar 2009 - Feb 2010); Global Opportunities Equity [ZAR] Feeder: 56.9% (Apr 1999 - Mar 2000)

Lowest annual return
Global Strategic USD Income: -2.0% (Apr 2019 -Mar 2020); Global Capital Plus [ZAR] Feeder:-7.0% (Mar 2015 - Feb 2016); Global Managed [ZAR] Feeder: -14.9% (Mar 2015 - Feb 2016); Global Emerging Markets Flexible [ZAR]: -51.9% (Mar 2008 - Feb 2009); Global Opportunities Equity [ZAR] Feeder: -41.3 % (Mar 2008 - Feb 2009)

Figures are quoted from Morningstar as at 31 March 2020 for a lump sum investment and are calculated on a NAV-NAV basis with income distributions reinvested.

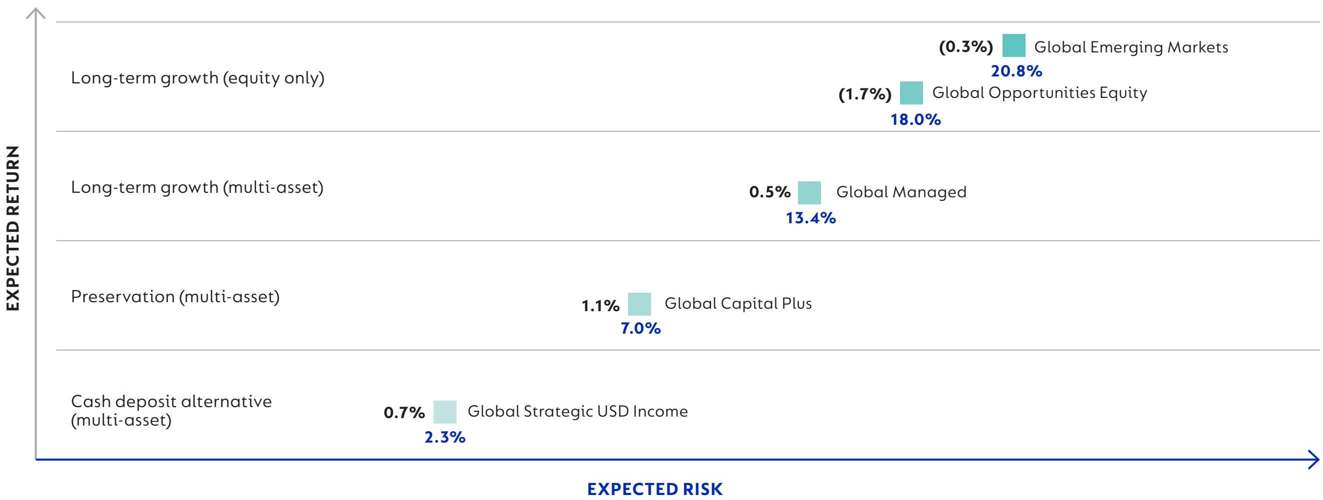
HAVE YOU CONSIDERED EXTERNALISING RANDS? IT IS EASIER THAN YOU MIGHT THINK.

The South African Reserve Bank allows each resident South African taxpayer to externalise funds of up to R11 million per calendar year (a R10 million foreign capital allowance and a R1 million single discretionary allowance) for direct offshore investment in foreign currency denominated assets. If you want to invest more than R1 million, the process is as easy as:

1. Obtain approval from the South African Revenue Service by completing the appropriate form available via eFiling or your local tax office. Approvals are valid for 12 months and relatively easy to obtain if you are a taxpayer in good standing.
2. Pick the mandate that is appropriate to your needs from the range of funds listed here. You may find the 'Choosing a Fund' section or 'Compare Funds' tool on our website helpful, or you may want to consult your financial advisor if you need advice.
3. Complete the relevant application forms and do a swift transfer to our US dollar subscription account. Your banker or a foreign exchange currency provider can assist with the forex transaction, while you can phone us on 0800 86 96 42, or read the FAQ on our website, at any time if you are uncertain.

RISK VERSUS RETURN

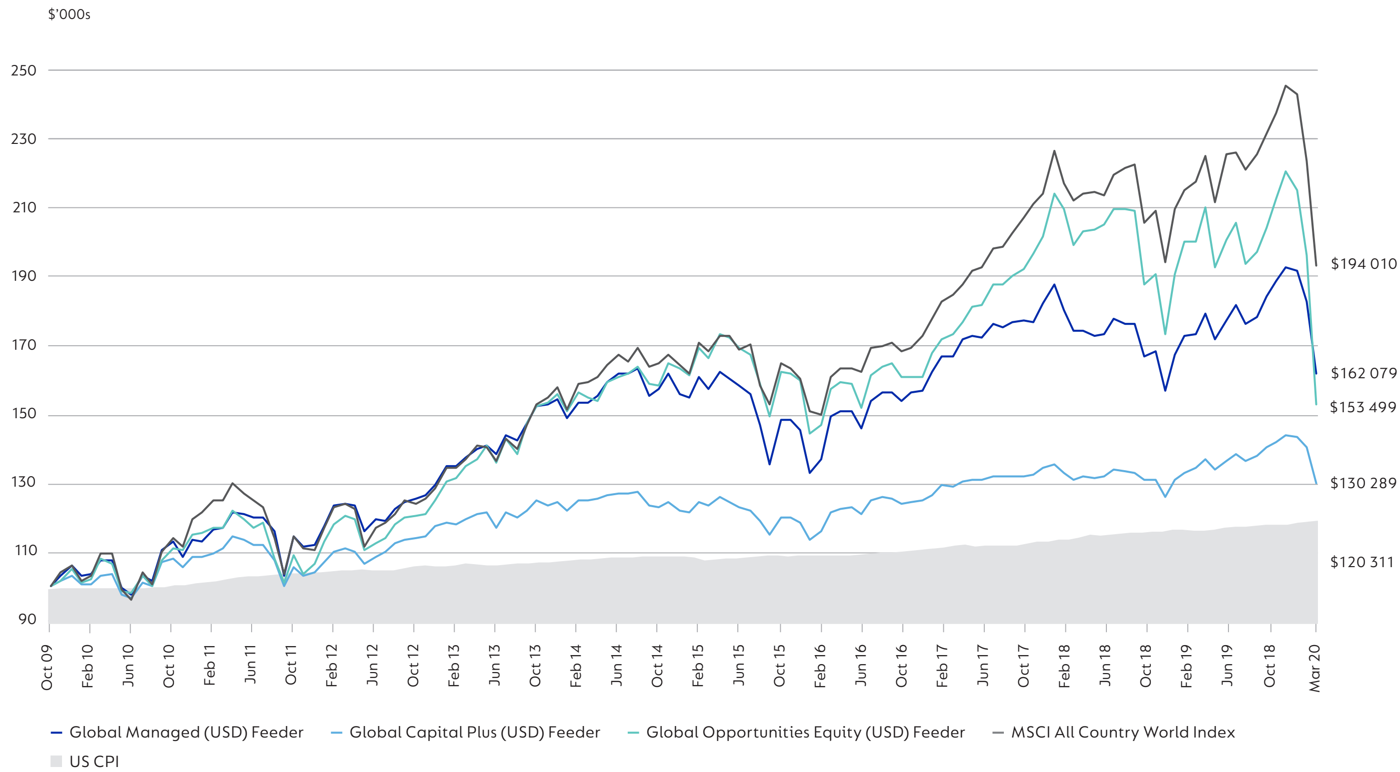
5-year annualised return and risk (standard deviation) quoted as at 31 March 2020. Figures quoted in USD (for the oldest fund) after all income reinvested and all costs deducted.



Source: Morningstar

GROWTH OF $100 000 INVESTED IN OUR GLOBAL MULTI-ASSET FUNDS ON 29 OCTOBER 2009

Value of $100 000 invested in Global Managed [ZAR] Feeder, Global Capital Plus [ZAR] Feeder and Global Opportunities Equity [ZAR] Feeder since inception of Global Managed [ZAR] Feeder on 29 October 2009. All returns quoted in USD. All income reinvested for funds. MSCI World Index is on a total return basis.



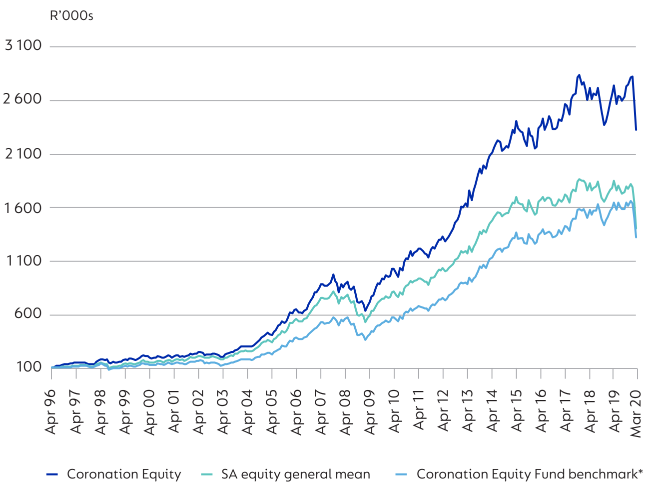
Source: Morningstar

Long-term investment track record

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

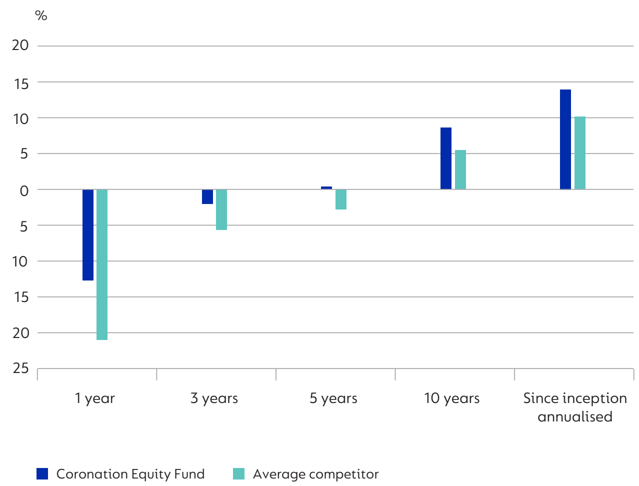
10-YEAR ANNUALISED RETURNS	CORONATION EQUITY	AVERAGE COMPETITOR	OUTPERFORMANCE OF AVERAGE COMPETITOR
2006	19.38%	17.09%	2.30%
2007	21.45%	19.23%	2.22%
2008	17.62%	18.47%	(0.84%)
2009	16.53%	16.68%	(0.15%)
2010	19.59%	19.14%	0.45%
2011	18.03%	16.98%	1.05%
2012	21.12%	18.94%	2.19%
2013	21.60%	18.68%	2.92%
2014	18.44%	16.32%	2.12%
2015	14.86%	12.62%	2.24%
2016	11.95%	9.54%	2.41%
2017	11.99%	8.90%	3.09%
2018	12.77%	10.54%	2.23%
2019	11.35%	8.71%	2.63%
9 Years 3 Months to March 2020	7.53%	4.62%	3.95%
ANNUALISED TO 31 MARCH 2020	**CORONATION EQUITY**	**AVERAGE COMPETITOR**	**ALPHA**
1 year	(12.57%)	(21.06%)	8.49%
3 years	(2.00%)	(5.64%)	3.63%
5 years	0.28%	(2.76%)	3.04%
10 years	8.58%	5.52%	3.05%
Since inception in April 1996 annualised	14.03%	10.13%	3.90%
Average outperformance per 10-year return			1.92%
Number of 10-year periods outperformed			13.00
Number of 10-year periods underperformed			2.00

CUMULATIVE PERFORMANCE



Source: Morningstar

ANNUALISED RETURNS TO 31 MARCH 2020



Source: Morningstar

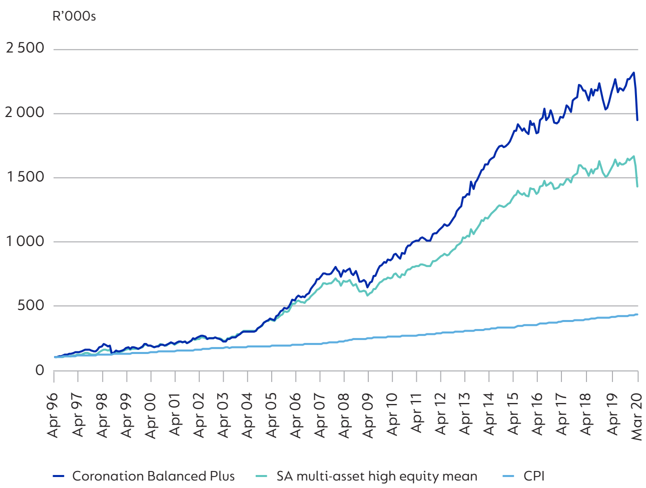
An investment of R100 000 in Coronation Equity on 15 April 1996 would have grown to **R2 309 791** by 31 March 2020. By comparison, the returns generated by the fund's benchmark over the same period would have grown a similar investment to **R1 313 830**, while the South African equity general sector would have grown a similar investment to **R1 389 133**.

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

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

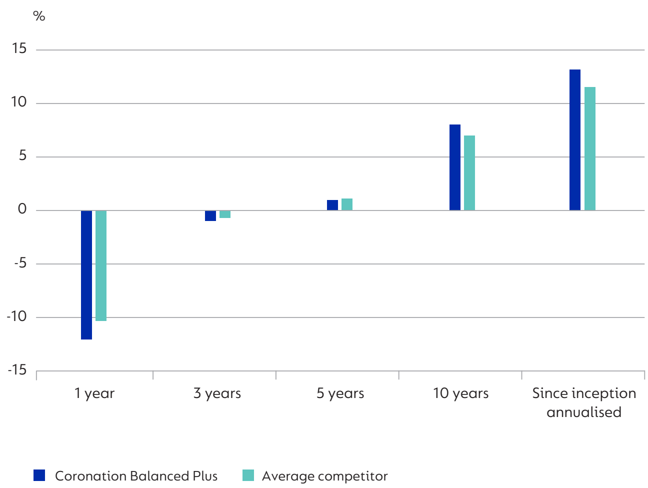
10-YEAR ANNUALISED RETURNS	CORONATION BALANCED PLUS	INFLATION	REAL RETURN
2006	18.33%	6.47%	11.86%
2007	17.81%	6.59%	11.22%
2008	16.96%	6.87%	10.09%
2009	15.69%	6.75%	8.94%
2010	17.20%	6.28%	10.93%
2011	15.78%	6.24%	9.54%
2012	17.85%	5.76%	12.09%
2013	18.63%	5.90%	12.73%
2014	16.58%	6.00%	10.57%
2015	14.01%	6.12%	7.89%
2016	11.08%	6.30%	4.77%
2017	11.04%	5.92%	5.12%
2018	11.26%	5.34%	5.92%
2019	10.30%	5.12%	5.18%
9 Years 3 Months to March 2020	7.51%	5.10%	2.93%
ANNUALISED TO 31 MARCH 2020	**CORONATION BALANCED PLUS**	**AVERAGE COMPETITOR**	**ALPHA**
1 year	(12.03%)	(10.32%)	(1.71%)
3 years	(1.02%)	(0.71%)	(0.31%)
5 years	0.89%	1.11%	(0.21%)
10 years	8.03%	6.97%	1.06%
Since inception in April 1996 annualised	13.13%	11.50%	1.63%
Average 10-year real return			8.65%
Number of 10-year periods where the real return is >10%			7.00
Number of 10-year periods where the real return is 5% - 10%			6.00
Number of 10-year periods where the real return is 0% - 5%			2.00

CUMULATIVE PERFORMANCE



Source: Morningstar

ANNUALISED RETURNS TO 31 MARCH 2020



Source: Morningstar

An investment of R100 000 in Coronation Balanced Plus on 15 April 1996 would have grown to **R1 910 299** by 31 March 2020. By comparison, the South African multi-asset high-equity sector over the same period would have grown a similar investment to **R1 405 811**.

[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.*

OUR CLIENT CHARTER

Our commitment to you

We strive to always put our clients first

We have an unwavering commitment to the long term

We focus on producing top performance over all meaningful periods

We are uncompromising about ethics

CORONATION

TRUST IS EARNED™