CORONATION FUND MANAGERS

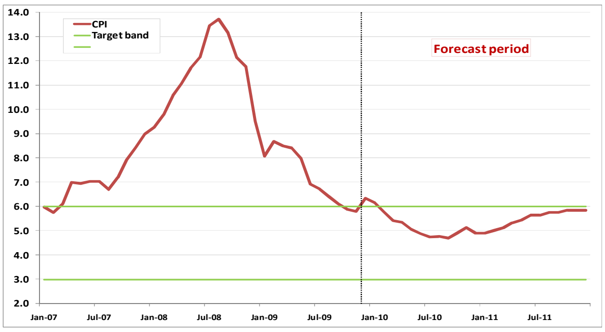
Fixed income update

February 2010

One of the most noteworthy asset allocation changes Coronation made over the past few months was in the Fixed Income portions of our portfolios where we significantly moved out of cash and into corporate and inflation-linked bonds. While bonds returned a very poor -1% for the 2009 calendar year; underperforming cash by close to 10%, the outlook for the year ahead looks decidedly more positive. This improved outlook is largely due to our expectation that the improving trend in inflation will continue in 2010.

The summary below provides our current economic outlook as well as an update about our flagship fixed income product, the Coronation Strategic Income Fund - one of the few funds in the fixed income varied specialist space that has managed to outperform cash in 2009. We'll also touch on the launch of our new low-risk, tax conscious fund, the Coronation Optimal Income Fund.

1. Our current inflation outlook



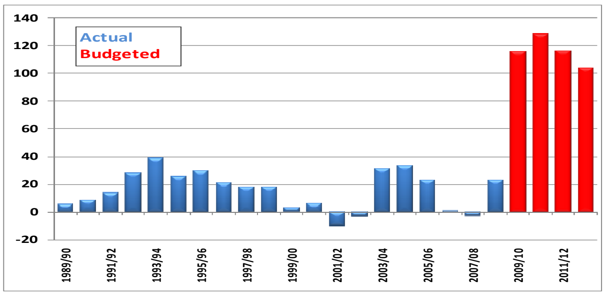
Source: I-Net Bridge

We remain relatively bullish on local inflation (CPI), which ended 2009 with a November release of 5.8%; the second month in which it fell within the 3% - 6% target range. While December and January figures breached the upper limit slightly, continued rand strength (towards the end of 2009) coupled with falling food prices and weak private sector credit extension bode well for inflation into 2010.

The risks to our relatively benign inflation outlook stem from a potential unwinding of the base effects of the lower fuel prices experienced in 2009, uncertainty about electricity prices and the chance of a severe bout of global risk aversion which could trigger a sharp retracement in the rand.

We are of the view that inflation could move within the 4.5% - 5% range towards the latter half of this year. However, over the longer term Coronation is concerned about inflation as significant infrastructural needs, administered prices and structural issues are likely to put upward pressure on inflation.

2. The elephant in the (bond market) room…



Source: National Treasury

The proverbial 'elephant in the room', putting pressure on the bond market and not allowing any compression in yields, remains the weekly supply of new government debt. The 2009 supply is just shy of R120 billion, while this year's budgeted funding requirement is around R140 billion - and we see significant pressure continuing into the future.

What will help alleviate the supply pressure comes predominantly in the form of growth. We are already starting to see the signs of growth turning, with for example a very positive year-on-year rate of car sales growth for January. We are expecting growth to average around 3% in 2010, compared to a contraction of 0.8% in 2009. As the SA economy start expanding again, one would see an increase in tax revenue collections and we are already starting to see an element of VAT collections improving. While corporate tax is likely to lag we expect an improvement towards the latter half of this year. This improved revenue collection should feed through and take some pressure off Government in terms of its funding requirements.

Only once there is a let up in the issuance programme (improving tax revenue/growth) or new buyers of bonds (foreigners or banks as they start extending credit again) can one expect a decent rerating of bond yields to occur. Once this starts to happen, bond yields should trade a lot closer to our fair value range of 8% - 8.5%.

3. Coronation Strategic Income Fund

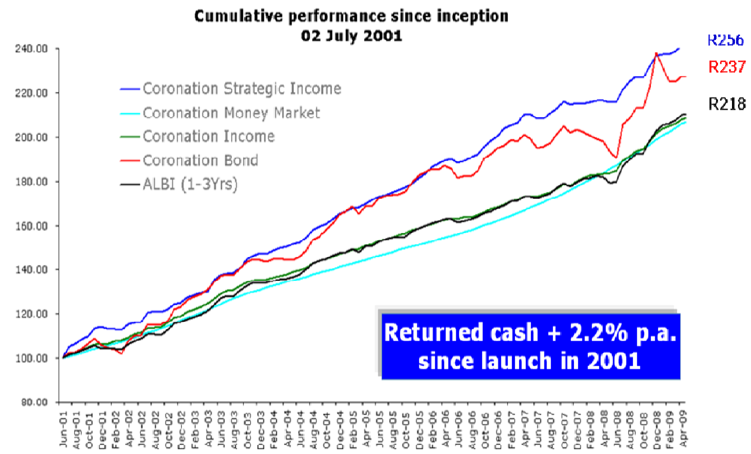
Strategic Income, our flagship fixed income fund, aims to provide a managed solution that performs better than cash (through the cycle) and delivers most of the upside from the bond market over time.

Following a tough first half of 2008, which resulted in the fund underperforming cash, we re-examined the positioning of the fund. As a result, we aligned the fund's benchmark more closely with our clients' objectives, changing it from the Short Bond Index to a cash plus benchmark: 110% of cash (as represented by the Alexander Forbes 3-months STeFI Index).

We also looked at how we deploy the risk budget in the fund. Historically, we deployed up to 20% of the fund to non-traditional assets such as listed property and preference shares. In the second half of 2009, we added more tools by giving the fund the ability to hold up to 10% in international assets, while increasing the overall limit of non-traditional fixed income assets to 25%. This ability is not a strategic holding, but more opportunistic in nature. For example, when one can buy dollar-denominated debt, issued by the same entity which issued rand-denominated debt at a higher yield, one would prefer to own the hard currency debt.

Lastly, given our current outlook for returns from the yielding asset classes, we've also lowered the fund's fees.

Has the strategy delivered over the long term? We believe so - Strategic Income has produced an average return of more than 2% per annum ahead of cash since inception in July 2001.

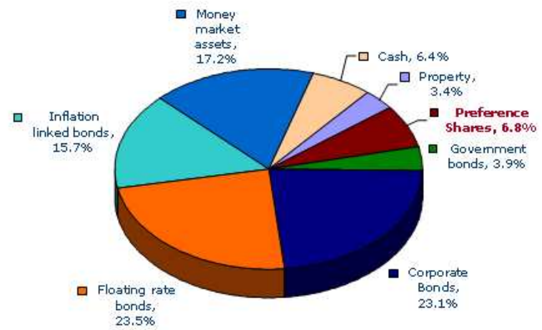


Source: Morningstar as at 30 December 2009

The fund currently yields just above 9%, with a duration of 1.6 and foreign exposure of 5% in predominantly SA companies that have issued dollar-, euro- or pound-denominated debt.

4. Portfolio structure

Current portfolio structure

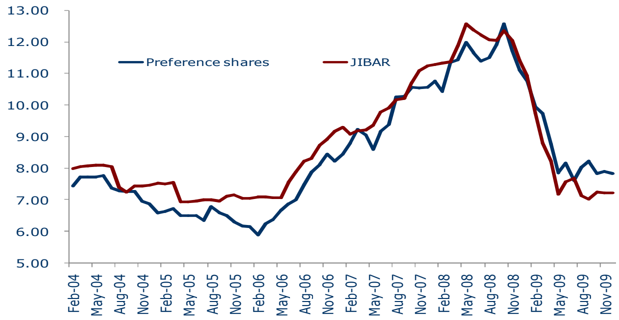


Portfolio structure as at 31 December 2009

One of the biggest differentiators of the Strategic Income Fund is our holding in preference shares, which currently comprises 7% of the total portfolio. We have also made use of exceptional circumstances to lock in above average corporate spreads; exposure to corporate bonds currently lies at just more than 20%. In addition, we have built a core holding in inflation-linked bonds, at 16% of fund, while overall exposure to listed property has been slightly reduced to around 3.5% of the fund.

The case for preference shares

We believe there is a high probability of this asset class re-rating given the current scrutiny of dividend income funds, with a decent probability that one could see a fair amount of cash flowing into preference shares over time. The current yield on listed bank preference shares trade at almost 1% above current yields available on cash investments. To put this into perspective, for the marginal taxpayer, money market yields need to almost double in order to break even with the non-taxable dividend from these listed perpetual bank preference shares.



Source: I-Net Bridge

The case for corporate bonds

The aftermath of the 2008 financial crisis created a sweet spot for investors who were prepared to take on corporate credit risk. For example, we increased our exposure to corporate bonds during the financial crisis last year when one was able to buy 5-year senior bank bonds at levels in excess of prime.

Why we have already bought inflation-linked bonds

While it may theoretically be a little too early to start buying inflation-linked bonds in terms of where we are in the fixed interest investment cycle, supply constrains justified a move into inflation-linked bonds. We have built up a core holding in this asset class at very attractive real yields of between 5% - 6%.

Are there still pockets of value within listed property?

Our broad view is that the asset class is somewhat expensive. However, we continue to hold selective counters such as Growthpoint, which holds a well-diversified portfolio of properties and currently produces a dividend yield of around 9%. While distribution growth one year out is likely to remain anaemic, we expect to see above-sector distribution growth 24 to 36 months out.

5. The Coronation Optimal Income Fund

Given the potential for a re-rating in the listed preference share market, Coronation has launched a low-risk, tax conscious fund that uses sustainable methods and the full skills set of our experienced investment team to outperform its benchmark of after-tax cash. Similar to Strategic Income, the fund invests across the various asset classes, but with a bias towards more tax efficient asset classes such as equities and preference shares. It will however use hedging to reduce the risk normally associated with investing in equities.

The fund is suitable for investors who are:

- tax-conscious, risk averse and have a time horizon of between 6 months and 3 years

- seeking a conservative and sustainable tax-conscious investment solution

- looking for an alternative to managed income funds that are less correlated to the interest rate cycle.

6. Key asset allocation changes in our multi-asset funds

Between March 2009 and January of this year, Coronation made the following changes in respect of our portfolios. We've reduced domestic equity exposure by 10% - 20% into strength. However, we retained our full international weighting with a bias towards equities. As discussed above (in length) we made use of exceptional circumstances to lock in above-average corporate spreads and switched around 10% of our multi-assets funds' assets into inflation-linked bonds.

Our current views can be summarised as follows:

- Equities is still our preferred asset class, especially offshore
- Domestic equities dominated by defensive names with reasonable valuations, strong cash flows and defensive business models
- Still increasing inflation linkers as a hedge against loose monetary policy and administrative price pressures
- Prefer corporate credit exposure over government; starting to acquire bond into weakness again
- Reduced listed property into strength, more expensive than some developed markets
- Preference shares offering an attractive opportunity but liquidity remains an issue

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7. Long-term performance

Our commitment to delivering strong long-term returns is illustrated in the performance of our core domestic range of funds. As at 31 December 2009, all funds rank first quartile over 5 years and since inception.

INVESTOR NEED	FUND	5-YEAR RANKING	SINCE INCEPTION RANKING
Long-term growth (equity only)	Top 20	1st Quartile	1st Quartile
	Coronation Equity	1st Quartile	1st Quartile
Long-term growth (multi-asset)	Balanced Plus	1st Quartile	1st Quartile
	Market Plus	1st Quartile	1st Quartile
Income and growth	Capital Plus	1st Quartile	1st Quartile
	Balanced Defensive	New fund	1st Quartile
Income only	Strategic Income	1st Quartile	1st Quartile

Source: Morningstar as at 31 December 2009