

It has been another profitable year for investors in mid and small cap shares. The Coronation Smaller Companies Fund has now delivered positive returns for the past five years. The fund bottomed out at a unit price of around 900c in April 2001 and ended 2005 some three times that level at 2690c. Faced with this kind of performance, investors are probably wondering whether this good thing must also come to an end. My feeling is that while 2006 might not be as good as 2005 (the fund returned approximately 30%), the fund should continue to deliver real returns. This feeling is premised on a couple of factors:

- The South African economy is expected to remain strong, which means corporate earnings growth should be decent.
- In general, shares are not yet overpriced. The fund trades on a one-year forward PE of 9.5. (An indication of the extent of upside we see in the fund is measured by the price to fair value ratio. At current share prices, the fund has a total value of approximately R135 million. If we value each share held by the fund at our estimate of fair value, the fund would be worth R153 million, 14% higher than the current level. To this, one would need to add the expected forward dividend yield on the fund of about 4% to arrive at an expected total return).
- The lack of more attractive returns from other asset classes. We still believe that equities are more attractive than bonds, cash or property.

During the quarter, our more significant purchases included new positions in Cashbuild, Invicta, Enaleni Pharmaceuticals and Dorbyl.

We regret not having bought Cashbuild shares sooner than we have done. This is a share that has gone from R3 back in 2001, to around R43 today, having peaked at R47 in September 2005. Despite the run that we have missed out on, we still believe that in the long term this company will continue to perform. Cashbuild sells basic building materials for cash (cement, bricks, timber, roofing, etc.) from very low cost, basic stores, located mainly in less affluent areas of the country. The stores are open seven days a week, will deliver for free within a certain radius of the store and are growing their sales volumes significantly. The store base is set to grow from the current 150 stores to around 300 stores in the next six years.

Invicta is a distribution business (Bearing Man is the main business) which we were fortunate to get a line of shares in at R13. Having peaked at R18 in July 2005, the share price responded negatively to a weak set of interim results caused mainly by poor agricultural equipment sales from their agricultural equipment distribution business. This presented longer term investors with an opportunity to invest in a very well managed company at a forward PE of just over 7.

We participated in the share placing which resulted in the previously ALT^x listed Enaleni Pharmaceuticals buying the unlisted generic drug distributor, Cipla Medpro, and then transferring its listing to the main board of the JSE. Cipla Medpro is the third largest distributor of generics in South Africa behind Adcock Ingram and Aspen Pharmacare. Generic drug growth in SA has been and is forecast to remain very strong at the expense of ethical drugs. At the share placing price of R3, Enaleni was priced at a significant discount to Aspen, its listed competitor, and we were happy to participate.

Dorbyl is an interesting situation in that we have effectively bought into a two asset portfolio comprising of an automotive component manufacturing business and cash, at a large discount. Should this cash be distributed to shareholders, this discount becomes bigger. We consider the investment to offer an excellent risk/reward profile.

Our more significant sales during the quarter included Mr Price, Wilson Bayly, Illiad Africa and Dawn.

Mr Price has been one of the largest holdings in the fund for some time now, but after a 50% price move in 2005, we do not like it as much as we did at the start of the year. This sale merely reduces our weighting to reflect the lower expected upside from here on out.

Wilson Bayly has been a remarkably consistent performer in the past 10 years, quite phenomenal considering they are involved in construction which is risky business. Currently there seems to be a state of euphoria surrounding any construction-related stock, so much so that Wilson Bayly now trades at a 20% premium to mid and small cap shares on a PE basis, when traditionally it, and all construction stocks, have traded at significant discounts. Despite good prospects for fixed investment spend in South Africa in the next five years, construction remains a tough and risky business with very little margin for error and, for this reason, we believe construction stocks are discount stocks. As such we have sold our position in Wilson Bayly.

We sold out of our position in Illiad during the quarter, preferring exposure to building material retailers via Cashbuild, mainly because of Cashbuild's much higher exposure to the lower-end residential building market which seems much more buoyant than the top-end.

We also sold out of our position in Dawn, the building materials distribution business which recently bought the bathroom fittings manufacturer Cobra. We did well from this investment but at above R7 the margin of safety no longer exists and it seems that more value accretive acquisitions are now being priced in – not a healthy risk/reward profile in our opinion.

Alistair Lea
Portfolio Manager

Fund category	Domestic Equity Smaller Companies
Launch date	1 April 1997
Portfolio manager	Alistair Lea
Fund size	R131.5 million
NAV	2691.02 cents
Annual management fee	1.00% (ex VAT)

Benchmark	Composite benchmark: FTSE/JSE Africa Mid & Small Cap Indices
Fund description	Invests in small and mid capitalisation companies, developing industries and recovery shares.

ASSET AND SECTOR ALLOCATION

Sector	31 Dec 2005	30 Sep 2005
Domestic Assets	100.00%	100.00%
Equity	94.54%	93.82%
Resources	6.89%	4.41%
Basic Industries	16.44%	16.19%
General Industrials	6.91%	5.71%
Cyclical Consumer Goods	6.20%	6.75%
Non Cyclical Consumer Goods	8.72%	6.45%
Cyclical Services	42.76%	45.47%
Financials	1.40%	3.24%
Information Technology	5.22%	5.60%
Cash	5.46%	6.18%
International Assets	0.00%	0.00%

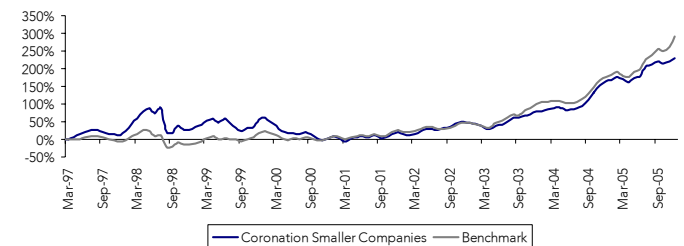
PERFORMANCE & RISK STATISTICS

	Fund	Benchmark
Latest 12 months	25.94%	41.37%
Latest 36 months (annualised)	31.05%	38.77%
Latest 60 months (annualised)	26.47%	30.84%
Since inception (annualised)	14.77%	16.89%
Annual deviation since inception	23.86%	19.91%
Sharpe ratio	0.25	0.35
Maximum gain	67.21%	43.41%
Maximum drawdown	-37.63%	-30.55%
Positive months	61.90%	60.95%

TOP 10 SHARE HOLDINGS

As at 31 December 2005	% of Fund
Mobile Industries Ltd	4.76%
Tiger Wheels Ltd	4.11%
Mr Price Group Ltd	3.89%
Tanzanite One Group Ltd	3.69%
Famous Brands Ltd	3.65%
Massmart Ltd	3.54%
Primedia Ltd – N ordinary shares	3.34%
Datacentrix Holdings Ltd	3.24%
Omnia Holdings Ltd	3.12%
Oceana Group Ltd	3.08%
Total	36.42%

CUMULATIVE PERFORMANCE SINCE INCEPTION



INCOME DISTRIBUTIONS

Declaration	Payment	Amount	Dividend	Interest
30/09/2005	01/10/2005	19.43	17.36	2.07
31/03/2005	01/04/2005	28.63	24.88	3.75
30/09/2004	01/10/2004	25.11	20.85	4.26
31/03/2004	01/04/2004	22.16	18.47	3.69

ANNUAL RETURNS SINCE INCEPTION

	Fund	Benchmark	Active Return
2005	25.94%	41.37%	-15.43%
2004	48.14%	38.62%	9.52%
2003	20.64%	36.35%	-15.71%
2002	24.03%	16.86%	7.17%
2001	15.91%	22.82%	-6.91%
2000	-33.41%	-13.56%	-19.85%
1999	21.50%	36.96%	-15.46%
1998	13.19%	-9.36%	22.55%
1997	12.62%	-4.78%	17.40%

PERFORMANCE RETURNS

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec	YTD
Fund 2005	0.93%	3.79%	-3.05%	-2.85%	4.70%	2.12%	9.28%	1.94%	3.01%	-1.44%	0.97%	4.54%	25.94%
B'mark 2005	1.52%	3.03%	-3.53%	-0.76%	5.34%	2.76%	8.94%	3.06%	5.87%	-1.72%	3.47%	7.92%	41.37%
Fund 2004	1.07%	1.78%	2.19%	0.96%	-3.47%	1.69%	0.70%	3.46%	9.81%	8.68%	8.87%	5.05%	48.14%
B'mark 2004	2.34%	-0.08%	1.72%	-0.23%	-2.58%	0.82%	0.57%	4.83%	6.70%	7.42%	9.07%	3.18%	38.62%