

After recording losses in Q2, bonds rebounded somewhat to show a positive performance in Q3. The 1 – 3 year bond index returned 1.6%, just underperforming cash of 1.9%. The All Bond Index returned 2.1% for the quarter, aided by longer-dated bonds which produced better returns than shorter-dated ones.

Bond market performance was perhaps surprising, given that we entered the quarter just following the first interest rate hike for the cycle in June, and ended it amid a volatile and much weaker rand. Even as expectations cemented around further rate rises – and despite a poor performance by the rand – longer dated bond yields generally moved in a sideways range over the quarter.

It was unusual for the longer-dated bond yields to not have responded more negatively, especially with notable rand depreciation. However, a possible explanation may be that in late June after the first repo rate hike, bond yields broke a lot higher and stayed there – pointedly ignoring the currency appreciation seen in July and August. It thus seems feasible that the reason that longer-dated bonds largely ignored the weakening in the rand during September was that they had effectively already discounted it.

It also appears that central bank credibility was established through the 50 basis point rate hikes in June and September. The bond market appears to have confidence that the SARB will respond appropriately to ensure that any inflationary impact of the rand's weakness will be short-lived. With the depreciation in the rand so far this year (it is currently down around 25% on a trade-weighted basis) together with the interest rate rises that we have seen so far with more to come, it is a matter of time before the worrying current account deficit starts to correct.

The international backdrop remains of critical importance too. The rand's reaction to the news of the current account deficit should be seen in the context of jitters in emerging market currencies – especially those of countries with high current account deficits. Furthermore, the restraint in local bond yields, would probably not have been possible had both US Treasury yields and emerging market bond spreads (as measured by the EMBI) not have remained at relatively low levels during the quarter.

Money market rates on the other hand rose to levels of around 9.5% this quarter, which offers good value versus bonds. Hence we continue to invest in the 1 to 2 year area of the curve, largely using tradeable fixed rate NCD's which pay regular interest and are issued by the top four banks.

The Coronation Income Fund's asset allocation has swung towards holding a higher proportion of lower risk money market assets over bonds. The majority of the bond component is represented by a selection of corporate bonds which provide an attractive yield pick-up over government bonds. The portfolio ended the quarter with a duration of 1.52 years versus that of the benchmark of 1.4 years.

**Tania Miglietta**  
Portfolio Manager

Fund category	Domestic Fixed Interest Income
Launch date	3 April 2000
Portfolio manager	Tania Miglietta
Fund size	R153.3 million
NAV	1107.29 cents
Annual management fee	0.75% (ex VAT)

<b>Benchmark</b>	BEASSA ALBI (1 – 3 year) TR Index
<b>Fund description</b>	Aims to provide a high level of current income with moderate levels of capital growth. Stability of capital invested is of prime focus.

## ASSET ALLOCATION

Maturity Band	30 Sep 2006
0 – 12 months	28.85%
1 – 3 years	56.30%
3 – 7 years	8.79%
7 – 12 years	6.05%
12+ years	0.00%

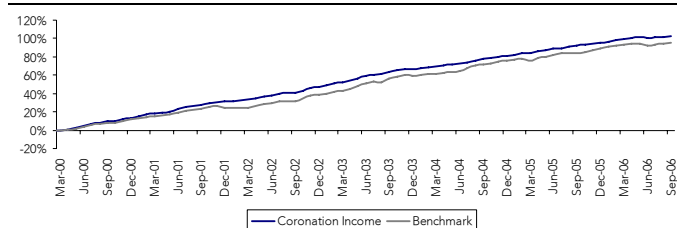
## PERFORMANCE AND RISK STATISTICS

	Fund	Benchmark
Year to date	3.65%	3.23%
Latest 12 months	5.88%	5.97%
Latest 36 months (annualised)	7.54%	7.86%
Latest 60 months (annualised)	9.72%	9.63%
Since inception (annualised)	11.52%	10.86%
Annual deviation since inception	1.96%	2.76%
Sharpe ratio	0.82	0.35
Maximum gain	101.41%	26.14%
Maximum drawdown	-0.25%	-1.54%
Positive months	96.15%	88.46%

## ANNUAL RETURNS SINCE INCEPTION

	Fund	Benchmark	Active Return
2005	8.16%	7.70%	0.46%
2004	8.52%	10.17%	-1.64%
2003	13.64%	15.02%	-1.38%
2002	12.16%	11.50%	0.66%
2001	15.75%	11.56%	4.19%
2000	13.14%	11.54%	1.60%

## CUMULATIVE PERFORMANCE SINCE INCEPTION



## INCOME DISTRIBUTIONS

Declaration	Payment	Amount	Interest
30/09/2006	01/10/2006	17.91	17.91
30/06/2006	01/07/2006	17.67	17.67
31/03/2006	01/04/2006	17.85	17.85
31/12/2005	01/01/2006	24.61	24.61

## MONTHLY PERFORMANCE RETURNS

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec
Fund 2006	0.56%	0.60%	0.53%	0.60%	0.48%	-0.25%	0.60%	-0.13%	0.61%			
B'mark 2006	0.74%	0.74%	0.35%	0.73%	0.09%	-1.09%	0.60%	0.38%	0.66%			
Fund 2005	0.64%	0.67%	0.27%	0.93%	0.68%	0.90%	0.49%	0.57%	0.59%	0.52%	0.91%	0.70%
B'mark 2005	0.34%	0.96%	-1.05%	1.69%	0.41%	1.25%	0.75%	0.31%	0.18%	0.24%	1.40%	0.99%