

Keeping out of trouble

Guided by an unwavering commitment to the long term

By KARL LEINBERGER

The greatest challenge in any investment firm is to build an enduring competitive advantage. In an industry as competitive as fund management, it is not an easy task.

It is tempting to argue that Coronation's competitive advantage lies in its people. We endeavour to hire only the very best and then we put extraordinary effort into training them to become world-class investment professionals. But we have to acknowledge that we have no monopoly over good people. In previous generations, the smart kids all became lawyers, doctors and engineers. These days, they all seem to want to join the financial services industry. The sad truth (for us!) is that we compete in an industry full of smart people.

The defining characteristic of Coronation's investment philosophy is its long time horizon. Any Coronation person will tell you that this is our enduring competitive advantage. In the investment world, time horizons have collapsed as they have converged with reporting periods. In our industry, smart people are placed under massive pressure every day to perform well this month, this quarter and this year. It is axiomatic that in a market where most participants are obsessed with short-term performance, market prices will reflect short-term considerations. This inevitably results in severe dislocations between market prices and long-term business value. It follows that this must then present a compelling opportunity for those investors that have the long time horizon to take advantage of this dislocation.

The last two years have been very successful for Coronation. During a time of extraordinary volatility our portfolios have all performed well. The period kicked off with euphoria in the commodities markets. Halfway through 2008, the local market was hit by the simultaneous collapse of the commodity, construction and small cap cycles. In late 2008, global markets sold off in anticipation of the worst synchronised global recession since the Great Depression and then, to everyone's surprise, recovered strongly in 2009 as the global economy showed signs of recovery. I must stress that we do not believe that our good performance came from any special insights. We had no idea when the commodity, construction or small cap cycles would turn. We certainly had no inkling that global markets would recover by approximately 60% off their March 2009 lows. What has kept us out of trouble, time and time again, has quite simply been an unwavering commitment to the long term.

It all sounds very intuitive: cut out the noise; fish where no-one else is fishing. In practice though, it is much harder than you think. It is tempting to try and time markets. We underestimate how susceptible each one of us is to instant gratification. It is tough when you are under-performing and you know it could be a long time before things turn. But the upside is enormous. We have built our entire business around this commitment to long-term investing. We are fortunate that our clients understand our philosophy and support us, and we have the business structures in place to ensure that our investment team is not distracted from its long-term focus. These are things that sound easy, but are, in reality, very difficult to achieve in an investment business.

We recently did some interesting work on our long-term track record. The following charts

show the alpha of our equity portfolios since Coronation opened for business in 1993 over varying periods (rolling one year and five years).

The analysis is, in our opinion, instructive for the following reasons:

Our long-term track record is compelling. Over just 16 years we have achieved alpha of 3.5% p.a. (or 13% p.a. using the alternative compound annualised alpha* calculation).

The power of compounding is staggering. In 16 short years this has translated into 62% in value (client portfolio 62% higher than the benchmark).

Over meaningful periods (five years, in our opinion): our long-term alpha has been consistent.

Over periods as short as 12 months our short-term alpha has been tremendously volatile with many periods of substantial underperformance (always followed by periods of outperformance as our long-term views were vindicated).

LONG-TERM TRACK RECORD

Per annum	Coronation Equity	Benchmark	Alpha	Cumulative Alpha*
Since inception	18.95%	15.41%	3.54%	13.20%
10 years	18.09%	14.44%	3.65%	9.25%
5 years	22.20%	19.77%	2.43%	4.74%
3 years	9.89%	6.31%	3.58%	4.03%
1 year	35.11%	29.91%	5.19%	5.19%

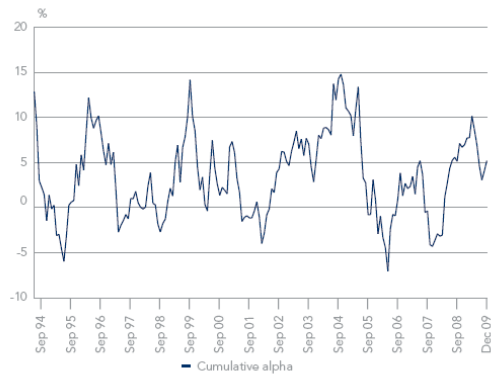
Source: Coronation

CUMULATIVE RETURNS



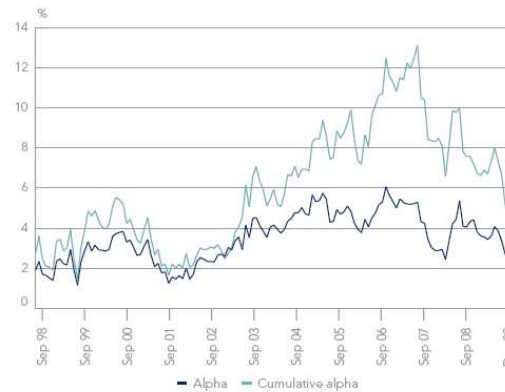
Source: Coronation

1-YEAR ROLLING ALPHA



Source: Coronation

5-YEAR ROLLING ALPHA



Source: Coronation

This analysis demonstrates that a long-term investor with a good track record will have many challenging years. It is important for clients to understand that this comes with the territory and it is often in these periods that the best long-term investments are made. Naturally, in these periods we will be asked hard questions - but this also comes with the territory. We will respond by testing ourselves to ensure that we have the necessary conviction in our underlying views and that our portfolios have been stress-tested for the inescapable uncertainties of the world we live in.

When performance is good, one easily forgets how trying these times are. They will come again and when they do we hope that as an investor you will take comfort from the fact that we have been there before, and that there are no short cuts to wealth creation.

Karl Leinberger

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