

LONG TERM OBJECTIVE

The Coronation Absolute Bond Strategy aims to protect capital regardless of the interest rate cycle. This Strategy therefore offers lower volatility and greater focus on capital preservation when compared to traditional bond portfolios.

INVESTMENT APPROACH

Coronation is a long-term, valuation-driven investment house. Our aim is to identify mispriced assets trading at discounts to their fair value through extensive proprietary research. The fixed income portfolios are positioned on a long term strategic market view, but this is balanced by taking advantage of shorter-term tactical opportunities when the market lags or runs ahead of that strategic view. As active managers, we consider investment decisions across the full spectrum of potential return enhancers. These include duration and yield curve positions, inflation-linked assets as well as yield enhancement through credit enhanced assets. We aim to maximise returns by actively combining both a top-down and a bottom-up approach to portfolio construction.

STRATEGY RETURNS GROSS OF FEES

Period	Strategy	Benchmark	Active Return
Since Inception (cumulative)	848.5%	226.5%	622.0%
Since Inception p.a.	10.2%	5.3%	4.9%
Latest 20 years p.a.	10.1%	5.4%	4.7%
Latest 15 years p.a.	9.6%	4.9%	4.7%
Latest 10 years p.a.	9.8%	4.6%	5.2%
Latest 5 years p.a.	10.1%	4.8%	5.3%
Latest 3 years p.a.	11.1%	3.7%	7.4%
Latest 1 year	12.0%	3.0%	9.0%
Year to date	0.0%	1.0%	(1.0)%
Month	(2.2)%	0.4%	(2.6)%

ASSET ALLOCATION

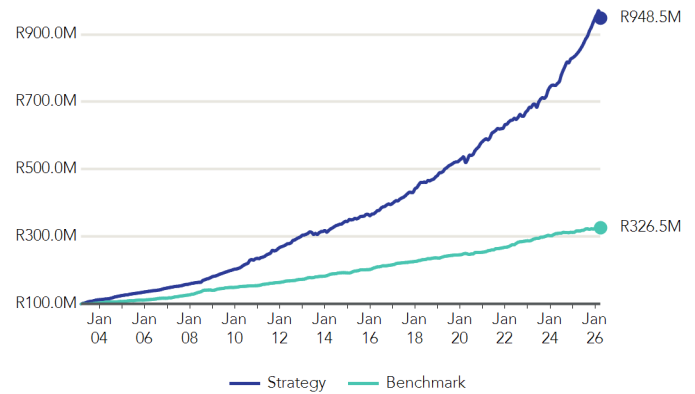
Asset Type	% Strategy
Fixed Rate Government Bonds	29.3%
Corporate ILBs	27.6%
Government ILBs	11.7%
Fixed Rate Corporate Bonds	10.5%
Floating Rate Corporate Bonds	9.3%
Fixed Rate NCDs	3.2%
Cash	2.4%
Other	2.1%
Fixed Rate Other	2.1%
Floating Rate NCDs	1.7%
Floating Rate Other	0.1%

GENERAL INFORMATION

Inception Date	01 March 2003
Strategy Size *	R4.57 billion
Strategy Status	Open
Mandate Benchmark	Consumer Price Index (CPI)
Performance Target	CPI + 2% (gross of fees and taxes) over a rolling 12 month period
Dealing Frequency	Daily
Base Currency	ZAR

*Strategy assets under management as at the most recent quarter end.

GROWTH OF R100M INVESTMENT



Benchmark: Consumer Price Index (CPI)

EFFECTIVE MATURITY PROFILE

Term	% Strategy
0 to 1 year	11.6%
1 to 3 years	30.5%
3 to 7 years	35.8%
7 to 12 years	18.0%
Over 12 years	4.1%

STRATEGY STATISTICS

Modified Duration (incl. inflation-linked bonds)	3.4
Modified Duration (excl. inflation-linked bonds)	1.9

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REVIEW FOR THE QUARTER

The first quarter of 2026 was defined by the dramatic escalation of conflict in the Middle East in late February and early March — a geopolitical shock that transformed the investment landscape in a matter of weeks. The conflict triggered the closure of the Strait of Hormuz, the largest supply disruption in the history of the global oil market. Brent crude surged to nearly US\$120 per barrel, approaching its 2008 peak, as the shock reverberated across asset classes globally. Stock markets declined, a broad bond sell-off ensued, and central banks moved to delay or reconsider easing paths as the prospect of higher inflation and tighter financial conditions took hold. Entering the second quarter, markets remain hostage to the trajectory of the conflict, with the reopening of the Strait of Hormuz being the single most consequential variable for the global macro outlook.

South African (SA) assets, which had been buoyed by improving domestic sentiment, a strong rand, and contained inflation at the start of the year, bore the brunt of the risk-off rotation. The fallout was widespread. By the end of March, the rand had lost over 6% against the US dollar, ending the quarter around R16.94/US\$, while the SA bond market suffered a sharp reversal after its remarkable 2025 rally. The FTSE/JSE All Bond Index returned -3.36% for the quarter (versus 19.2% over the last year), and the 10-year SA government bond (SAGB) yield widened by 112 basis points (bps) to 9.32%, erasing much of the prior year's compression. The long end bore the greatest pain, with bonds of 12 years and above losing 4.09%, while the one- to three-year segment offered modest protection at +0.64%. Inflation-linked bonds (ILBs) also declined, returning -1.13% (versus 13.32% over the last year), though they outperformed nominal bonds on a relative basis as breakeven inflation expectations repriced higher due to the oil shock. Cash returned 1.60% — the only positive-returning domestic fixed income asset class for the quarter.

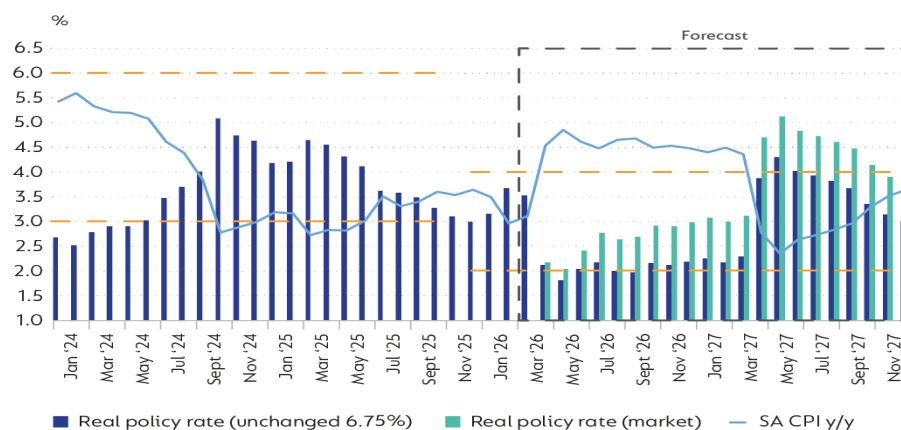
First round pain, second round risk

Significant increases in fuel prices will be the first source of higher inflation, immediately adding 0.5%–1% to headline inflation relative to previous forecasts. However, the longer the oil price stays high (c.US\$90–100/barrel), the greater the likelihood of second-round effects on the rest of the inflation basket. The closure of the Strait of Hormuz also affects approximately 35% of the global fertiliser trade, raising the risk of higher agricultural input costs and, by extension, food prices. Incorporating just the first-round effects of the oil price hike into our inflation forecasts sets the inflation average above 4% in 2026, before easing to an average closer to 3.5% in 2027. There is a risk that inflation in 2027 will be 0.2%–0.4% higher if oil takes longer to normalise, causing second-round inflation effects.

The South African Reserve Bank (SARB) has indicated a willingness to look through first-round effects; however, their base forecasts assume a much quicker normalisation in the oil price to lower levels, while their adverse forecasts are closer to our current baseline. In the SARB's worst-case scenarios, they project the repo rate to around 7%–8.25% (25bps to 150bps of rate hikes). Current market expectations are for 75bps of rate hikes (repo rate at 7.5% by end 2026), which would keep the real policy rate at 3%. This pricing seems quite conservative. The long-term impacts of a sustained oil price spike are unambiguously negative for growth. This is a dynamic the SARB is acutely aware of and which, historically, has tempered its willingness to tighten aggressively into supply-side shocks. If the SARB ultimately hikes less than the 75bps the market has priced, this represents an unrecognised tailwind for bond valuations. (Figure 1).

Figure 1

SA INFLATION AND POLICY RATE



Sources: Coronation, Bloomberg

Fiscal is credible but not shockproof.

The February National Budget presented a credible path for fiscal consolidation as expenditure constraint was maintained without any overtly optimistic revenue expectations. Prudent debt management strategies, including more floating-rate issuance, the introduction of new bonds issued at par, and more flexibility on the maturity profile of issuance, have helped lower borrowing costs. This has allowed a sizeable reduction (R750 million/week) in weekly issuance, which was very well received by markets.

The current inflation spike does not immediately endanger the path to fiscal consolidation, as any increase in expenditure should be offset by increases in revenue. However, two risks bear watching. First, if the spike in the oil price is prolonged beyond three to six months, it could materially dampen the growth outlook, resulting in lower-than-projected tax receipts and a less favourable fiscal outcome. This is precisely the dynamic that derailed consolidation during the 2014–2016 commodity downturn. Government has agreed to provide some offset to higher pump prices by reducing the fuel levy, which should provide consumer relief, with sufficient buffers in the fiscus (contingency reserve and other areas) for it to be funded for approximately three months. Second, if the conflict extends beyond that horizon, government will face a difficult choice between allowing the fuel levy reduction to lapse — adding to consumer inflation at an inopportune time — or finding additional funding sources that could widen the deficit. The issuance reduction that was so encouraging to markets could come under pressure in that scenario. SA's debt load still remains an area of longer-term concern. Until reform results in growth in excess of 2.5% over a sustained period, debt will not consolidate meaningfully, and SA will remain a sub-investment-grade economy.

Stretched to investable

Bond yields are up c.100bps from the start of the year and c.130bps since the lows reached during the course of 2025. Whereas the pre-conflict levels seemed extended and did not reflect a sufficient margin of safety, current levels are starting to encroach on cheap territory.

The ratio of SA bond yields to cash is now back to its long-term average, which provides approximately 40bps–60bps of breathing room before bond yields start to perform in line with cash. A note of context is warranted here: the 'long-term average' for this ratio spans a period that includes the post-Covid blowout of 2020–2022, when SA bonds were genuinely distressed, and the ratio was at extreme levels. Reverting to an average that incorporates those outliers is meaningfully different to reverting to pre-pandemic norms. Relative to the 2015–2019 average, current levels are modestly cheap. As shown in Figures 2a and 2b, the valuation case is, therefore, best characterised as 'reasonably attractive' given improved fundamentals rather than 'outright cheap' in a historical sense.

Figure 2a

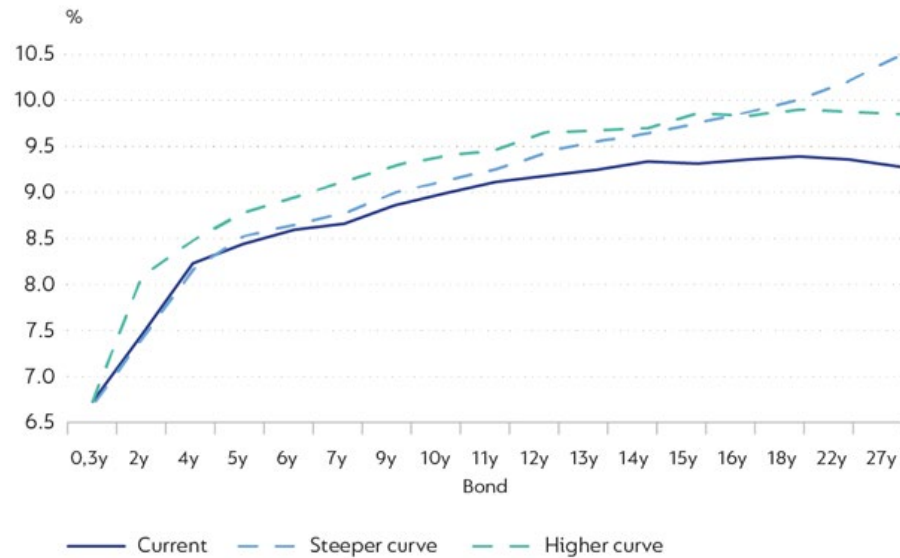
BOND BREAKEVEN STILL TIGHT BUT BACK TO LONG-TERM AVERAGE



Sources: Coronation, Bloomberg

Figure 2b

SOME CUSHION REEMERGED ON THE YIELD CURVE



Source: Coronation, Bloomberg

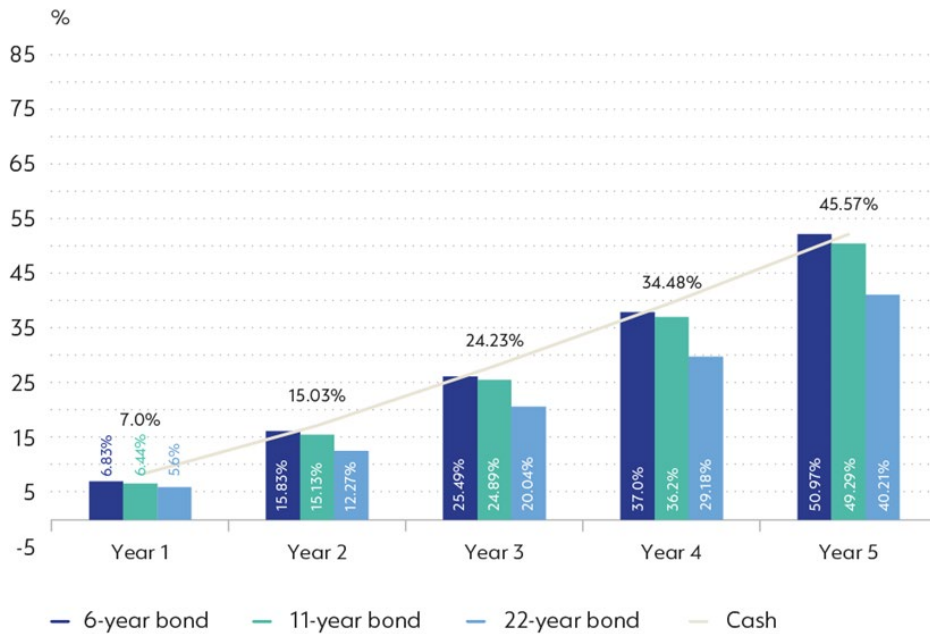
The market is pricing 75bps of rate hikes, but the SARB's historical reluctance to tighten aggressively into supply-side shocks suggests the actual outcome may be more benign. If the SARB delivers only 25bps to 50bps of hikes — or pauses after an initial move — the repricing in bonds would look excessive in hindsight, and current yields would represent a genuine entry point. Conversely, if the oil shock proves persistent and the SARB is forced into the upper end of its adverse scenario (150bps of hikes), the current 40bps–60bps cushion might prove sufficient. The valuation case is therefore conditional on the nature of the shock, not just its initial magnitude.

In addition, the higher yields also provide cushioning for a steeper yield curve (>20-year bonds can steepen by 50bps relative to <10-year bonds) before they start to underperform cash. These levels might not seem as eye-watering as they were in the period during and after Covid; however, given the somewhat improved fundamental outlook (lower inflation, better fiscal positioning), they represent a much better entry point than where we stood at the start of the year.

We resurrect an analysis that we performed quite regularly during Covid, looking at the total return of SAGBs under an adverse scenario (50bps widening in bond yields every year for five years) compared to that of cash. It is clear that yields still provide the investor with a decent amount of protection as long as one remains in the sub-12-year area of the curve. This part of the curve handsomely outperforms cash and longer-dated bonds over a five-year period, primarily because the curve is quite elevated in that region relative to cash rates and encompasses a decent amount of interest rate normalisation already (75bps of rate hikes). In addition, Figure 3 shows that the assumed 50bps of annual widening implies a cumulative 250bps over five years — yet the first quarter alone has already delivered 100bps to 130bps of widening in a matter of weeks.

Figure 3

5-YEAR TOTAL RETURN (CASH & BONDS)



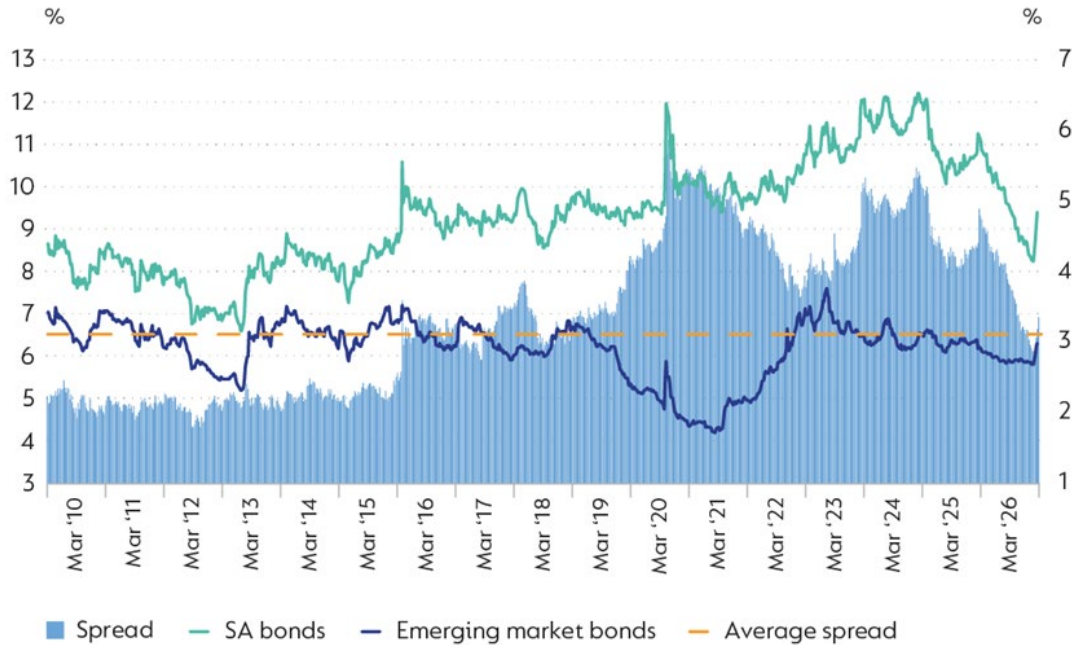
Source: Coronation, Bloomberg

SA had run quite ahead of its emerging market peer group, both from a currency and bond perspective, but the recent reprice has seen spreads retreat back to their long-term average, suggesting more appropriate pricing relative to peers.

If the Iran shock is repricing all emerging market bond markets simultaneously — and it is — then SA reverting to average spreads versus the JP Morgan Emerging Markets Index simply means SA sold off in line with the pack, not that it is independently attractive on a relative basis. The more meaningful question is whether SA's domestic fundamentals (the fiscal consolidation path, the GNU's policy coherence, SARB credibility) justify it trading tighter than its emerging market peer average on the other side of the shock, as it did in the second half of 2025. If so, the current spread levels imply upside. If the oil shock erodes those domestic advantages — through weaker growth, fiscal slippage, or a forced tightening cycle — then 'average' may be fair, or even generous (Figure 4).

Figure 4

SA BONDS IN LINE WITH EMERGING MARKETS



Sources: Coronation, Bloomberg

In a quarter where global risk appetite deteriorated sharply, the behaviour of SA sovereign credit default swap (CDS) spreads offers a useful signal on how the market is decomposing SA-specific versus global risk. SA 5-year CDS widened meaningfully during March but — critically — by less than several emerging market peers with direct oil import exposure, suggesting the market continues to give SA credit for its improved fiscal trajectory and does not view the oil shock as an idiosyncratic SA event. If the sell-off in SA bonds were being driven by a reassessment of SA's creditworthiness rather than a global risk-off event, we would expect CDS to have moved more aggressively. The fact that they have not reinforces our view that the domestic improvement thesis remains intact, even as the near-term is clouded by the geopolitical backdrop.

A real opportunity

ILBs significantly outperformed nominal bonds over the last quarter, but lag over the longer term. However, ILBs have shown their value in a domestic bond Strategy as the only real protection the Strategy can have during times of extreme risk-off due to their inherent inflation protection and lower beta to nominal bond factors. At current real yields, certain portions of the ILB curves still warrant some attention. ILBs out to the seven-year area are still trading above 4% (a guaranteed return of CPI+4%), with the curve past that area trading pretty flat, with no term premium to compensate for the higher risk taken. An important nuance that bears emphasis: while real yields remain elevated, the oil shock has pushed breakeven inflation expectations materially higher. This means that ILBs are now more expensive in breakeven terms, even as their real yields appear attractive in isolation. An investor buying front-end ILBs at a 4%+ real yield is making two implicit bets: first, that real yields will compress as the SARB's eventual easing cycle plays out; and second, that realised inflation will at least match the now-higher breakeven levels baked into the price.

Figure 5 examines the total return of ILBs relative to cash assuming ILB yields sell off 25bps per year over the next five years, and inflation averages 3.8%. The 7-year ILB is the most attractive in this scenario, offering both a superior return to that of cash and longer maturity ILBs.

Figure 5

5-YEAR TOTAL RETURN (CASH & ILBs)

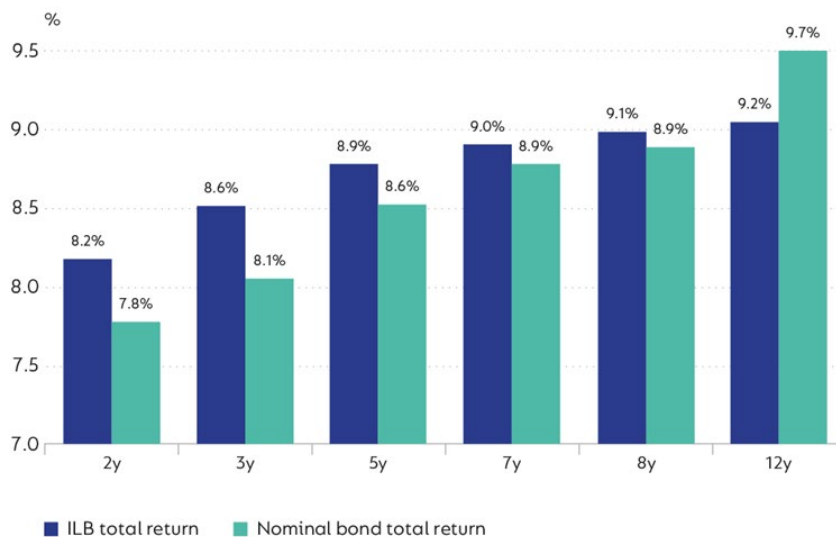


Source: Coronation, Bloomberg

Our current inflation profile has inflation averaging above 4% for most of the next 12 months. What is evident is the total return of the sub-seven-year area of the ILB curve remains more attractive than that of the nominal bonds. Figure 6 illustrates that, given the elevated uncertainty from the geopolitical backdrop, the embedded inflation protection these instruments provide makes them a particularly useful Strategy building block at current levels.

Figure 6

TOTAL RETURN: ILB VERSUS NOMINAL BONDS



Source: Coronation, Bloomberg

As SA exits a turbulent first quarter, the bond market has shifted from a story of stretched valuations and narrow upside to one of renewed opportunity born out of geopolitical disruption. The complex nature of the situation in the Middle East and the closure of the Strait of Hormuz have repriced risk across the curve, but in doing so have restored a more appropriate margin of safety. Crucially, the domestic reform thesis — fiscal consolidation, contained inflation expectations, and SARB credibility — remains fundamentally intact, even as the near-term inflation impulse from the oil shock clouds the path for monetary policy. In this environment, one should favour the belly of the nominal curve where carry and rolldown are most robust, and maintain selective exposure to front-end ILBs where real yields above 4% offer genuine inflation protection and superior risk-adjusted returns. The trajectory of the conflict will ultimately determine whether this repricing proves a compelling entry point or merely a waystation to further volatility, but the quarter's dislocation has provided an opportunity to increase duration to benchmark levels while maintaining a decent allocation to ILBs within bond Strategies.