CORONATION
TRUST IS EARNED™

Please note that the commentary is for the retail class of the fund.

The fund returned 3.2% for the quarter and 17.1% for the full year. The fund has performed well against both its peer group and the quantitative benchmarks over longer periods.

While our large weighting in global stocks added significantly to performance for the year it was a detractor in the fourth quarter as South African assets rallied on the back of the appointment of Cyril Ramaphosa as ANC president in December. Mr Ramaphosa is expected to herald better fiscal discipline, though a divided party leadership will make necessary policy reform challenging.

Over the past year, the fund benefited from holdings in global businesses including JD.Com, 58.Com and Porsche. 58.com is a Chinese online classifieds player operating in a growing marketplace as the business drives penetration into lower tier Chinese cities, expands advertising services to merchants and gains traction in used goods markets. Growing scale and dominance should support margin expansion. JD.Com is a Chinese online retailer similarly benefiting from rapidly growing demand as it expands product ranges and invests in its infrastructure and fulfilment services. The vast domestic market with its large number of high density cities creates longer-term potential for a very profitable business and it continues to gain scale and market share.

Domestic equity markets delivered good returns in 2017, reversing the lacklustre performance of the past few years. The Capped All Share Index (CAPI) returned 18.06% for the year and 6.5% in the fourth quarter. This compares to an annualised 8.9% over three years. The return in US dollar terms is 30.6% over the year as the rand strengthened, reflecting a positive shift in sentiment on the back of the ANC elective conference outcome.

From an earnings perspective domestic shares had a challenging year and had underperformed going into the final quarter of the year. However, the past quarter saw a rally in their share prices with notable performers including banks (+28%) and general retailers (+23%). The large rand hedges such as Naspers (+72%) and Richemont (+25%) had a good year outperforming the market. The fund's Naspers position was consistently trimmed throughout the 12-month period on the back of strong performance particularly in the underlying Tencent investment. Despite this, our absolute position in Naspers remains large, reflecting our continued assessment of the company as an attractive share as it streamlines its investment portfolio and Tencent expands its portfolio of services in large and growing markets. For the full year, resources (+16.8%) lagged the returns delivered by industrials (+22.6%) and financials (+24.4%) (JASIN and FINI 15).

The fund remains overweight offshore stocks, though the buying of domestic shares during the year has reduced the extent of this overweight position. The fund added selectively to better quality domestic industrial names (including Spar, Netcare, Famous Brands, Curro and Pick n Pay) during the year as they underperformed. These positions all contributed to performance during the fourth quarter domestic rally. Notwithstanding this, we believe valuation remains attractive. Offshore names where the fund continues to have meaningful exposure include Naspers, British American Tobacco, MTN and Hammerson.

British American Tobacco in particular looks cheap for a global consumer staple on a one-year forward PE of 15.4x with the opportunity to grow earnings through next generation tobacco products and margin uplift on the back of the recently completed Reynolds take out. The fund added significantly to this position during 2017 and remains convinced of its compelling valuation.

Steinhoff has been a significant detractor from performance over the year exacerbated by the share price collapse on the announcement that the company would delay the release of its 2017 audited financial results, launch an investigation into accounting irregularities and that the CEO had resigned. The fund held Steinhoff for the expanding, cash generative value retailer Pepkor as well as the opportunity to consolidate a rapidly growing but fragmented European furniture market through its vertically integrated European operations. Despite concerns about its acquisitive nature and aggressive tax structuring, the valuation looked compelling on a single digit PE multiple. We did extensive reference checks including meeting many of the high calibre board members and well respected regional managers. To date, limited information has been released to further our understanding of where the accounting irregularities occurred. We continue to monitor events closely and will take action as considered appropriate.

The rally in domestic banks and life insurers is cause for review with higher earnings expectations being priced in. Discovery was one of the biggest contributors to performance in 2017 with particular strength in the past quarter. The position size has been trimmed in line with the reduced margin of safety. Domestic bank valuations are also pricing in a more optimistic outcome. Slow advances growth over the last few years could be accelerated with more accommodative economic growth though a benign credit cycle leaves little room for credit loss improvements. Here too, positions sizes reflect a reduced margin of safety.

Brexit-related market uncertainty continued to undermine the outlook for UK property stocks. Global corporate activity picked up in the property sector in the past quarter with bids such as Unibail for Westfield and Brookfield for GGP highlighting inherent longer term value. In the UK specifically, an all share offer for Intu by Hammerson in early December provided some support to our view that there is long term value in the sector. It is hoped that Hammerson's excellent management team can further unlock the potential in Intu by combining two leading retail portfolios. Valuation remains attractive with the shares trading at significant discounts to NAV. The fund retains a significant holding in UK property via Hammerson PLC, Intu PLC and Capital and Counties.

Calendar 2017 was a relatively robust year for commodity prices with most strengthening as Chinese demand remained resilient. Supply remained constrained as miners persisted with disciplined allocation of capital and Chinese environmental regulation capped domestic supply. While higher commodity prices have reduced the margin of safety in resource valuations, the fund retains a reasonable exposure with contributions to full year performance from Exxaro, Anglo American and Mondi. Exxaro, in particular, performed well with associate Kumba Iron Ore profiting from robust iron ore prices, high coal prices and a recovery in Tronox. A recent pullback in Mondi has meant the valuation again looks attractive and we are adding to our position.

The past quarter's domestic rally has created the opportunity for us to buy some of the more attractively valued offshore shares as the market prices in a very optimistic economic outcome domestically despite lingering challenges. The overall portfolio remains largely unchanged, consistent with our commitment to invest where we see long term opportunity.

Portfolio managers
Karl Leinberger, Sarah-Jane Alexander and Adrian Zetler
as at 31 December 2017