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

The fund returned 0.46% in the second quarter of 2019 (Q2-19). Over longer periods, the fund has performed well against its peer group.

Our large weighting in global equities has added to fund performance over both Q2-19 and the year to end-June 2019. This has been supported by the fund's large holding in Heineken, which has performed strongly. The revenue growth opportunity for Heineken remains exciting, with more than 50% of its revenues derived from high-growth emerging markets. This is a business that has consistently focused on putting investment behind its long-term prospects, building a powerful brand. This approach should deliver a combination of strong revenue growth and margin expansion over time from premiumisation and operating leverage. Heineken's ability to compound earnings over time makes for an attractive investment opportunity in our opinion.

The JSE extended its first-quarter gains, albeit at a slower rate. The JSE Capped Shareholder Weighted All Share Index appreciated by 2.9% during Q2-19. Resources were up (+2.4%) despite signs of slowing global growth, but lagged the stronger quarterly performances from the industrial (+4.0%) and financial (+5.4%) sectors. The outperformance of the resource sector over one- and three-year periods remains considerable.

Despite the conclusion of the much-awaited South African election, domestic sentiment deteriorated during Q2-19. The election result was broadly in line with expectations, with the ANC maintaining its majority rule despite a slight decline in support. The appointment of a new and smaller cabinet was a positive development, reinforcing the message of fiscal discipline. However, the ruling party remains plagued by factional tensions, frustrating the ability of the president to deliver on much-needed reform. Policy uncertainty lingers as reflected in divisive debate on land issues and South African Reserve Bank reform. Eskom's balance sheet problems remain an overhang. Government has signalled its commitment to support Eskom financially, though the underlying state of Eskom's generation and transmission assets remain unclear. These factors combined to weigh on consumer and corporate confidence levels and were reflected in a very weak Q1-19 GDP print of -3.2%, dragged down by manufacturing and mining. Results released during Q2-19 and the accompanying subdued rhetoric of management reinforced how challenging the underlying economic situation is. The weak domestic economy, contained inflation and favourable global interest rate expectations have increased the likelihood of future local rate cuts.

In this environment, domestic stocks reported weak results. Even defensive stocks struggled to defy the pressures of several years of weak domestic economic conditions and high structural cost inflation. We expect these headwinds to persist and remain cautious on businesses heavily exposed to the domestic economy. Our exposure to domestic stocks is mostly through banks and defensive counters, such as food retailers. The fund remains underweight domestic SA stocks. We continue to debate whether these depressed conditions (and earnings bases) provide an opportunity to add meaningfully to domestic holdings, but have made no material changes to the fund to date.

The fund continues to hold high weightings in the JSE-listed global stocks (British American Tobacco, Naspers, Mondi, Quilter, MTN, Bidcorp and AB InBev), all of which have attractive valuations for specific bottom-up reasons.

The British American Tobacco share price declined during the period (-15.7%) as fears related to low nicotine regulation in the US market resurfaced. British American Tobacco has faced a slew of potential regulatory headwinds in its US business, exacerbated by volume declines in traditional tobacco. However, new generation products are gaining traction. We believe the underlying fundamentals of the business remain intact, with strong pricing power, improving cost controls and de-gearing continuing to drive earnings. In addition, we believe that new generation products are lower-risk products and present an opportunity to grow the overall market. British American Tobacco trades on 9.1 times one-year forward earnings and a 7.3% dividend yield. We believe this to be very attractive for a stock of this quality and it remains a large position in the fund.

The resources sector (+2.4%) showed mixed performances, with Sasol's underperformance (-22.2%) offset by a strong performance from gold miners (+29.6%) and platinum (+9.5%). Iron ore (+32.9%) has been particularly strong as supply disruptions have driven up near-term prices, supporting the fund's large holding in Anglo American. This position was trimmed during the quarter. The Sasol share price declined meaningfully when the company announced that its Lake Charles Chemicals Project (LCCP) would a) cost more to deliver and b) produce a lower normalised level of profitability. Disappointments in the delivery of the LCCP have meant a further reduction in the already muted returns offered by the initial projections, which carried significant risk (a fact Coronation highlighted to the board in a letter sent in 2013). The fund has been underweight Sasol, but added to the position on the back of the price weakness. As the project nears completion, execution risk should reduce and the group's earnings base is anticipated to increase by 20% to 30%. However, given the heightened risks (operational and financial), we have limited Sasol's overall position size within the fund.

We remain meaningfully invested in platinum counters. We reduced our Anglo American Platinum position in response to its strong share price rise, reinvesting the proceeds into names that have underperformed on a relative basis. The demand outlook for platinum group metals (PGMs) remains strong, buoyed by increasingly stringent emissions regulations. While we expect electric vehicles to play a role in future mobility solutions, we see a structural deficit in PGM markets over the next decade as supply remains tight after years of underinvestment. Despite the upwards move in the metal's price, PGM producers are not yet earning fair returns on their invested capital. We believe prices need to rise further to incentivise sufficient ounces.

The financial sector (+5.4%) performed strongly during Q2-19, as local banks (+9.7%) have defied domestic market headwinds and are expected to deliver underlying earnings growth. This growth reflects prudent management through the cycle with limited credit extension resulting in low credit loss ratios. The fund has holdings in several of the large banks, including FirstRand, Nedbank and Standard Bank.

Political turmoil continued to reign in the UK with the resignation of Prime Minister Theresa May during the quarter. The Labour Party's indecisiveness on several key issues reduced the strength of the opposition's position. High levels of uncertainty in the UK undermine the economic outlook. Despite this, compelling valuation-driven opportunities exist. Quilter remains the fund's largest single holding in the UK. This is a business with a structural growth opportunity stemming from pension reform in the UK market. The fund has built up its position in food services company Bidcorp, which continues to benefit from consumers' desire for eating out of home and its diverse operations across many markets. While we see exciting investment opportunity in the UK market, the fund continues to tightly manage overall UK exposure, given the uncertainty.

Markets have remained challenging this year, with several companies reporting material earnings disappointments that have put these businesses at risk. A rigorous research process and heightened balance sheet scrutiny have protected the fund from several of these examples. We remain committed to building robust, diversified portfolios with a focus on risk management. We believe these efforts will protect the portfolio against unexpected outcomes and position the fund well to deliver inflation-beating returns over the long run.

Portfolio managers
Karl Leinberger, Sarah-Jane Alexander and Adrian Zetler
as at 30 June 2019