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

The fund returned 1.6% for the second quarter of 2019 (Q2-19). Since inception, it has averaged an annualised return of 16.6% relative to its benchmark's return of 14.1%, while it has moderately underperformed its benchmark over the past five- and 10-year periods.

Despite the conclusion of the much-awaited South African election, investor and consumer sentiment continued to deteriorate during the quarter. The election result was broadly in line with expectations, with the ANC maintaining its majority rule – albeit with slightly reduced support. The appointment of a new, smaller cabinet was a positive development, reinforcing the message of fiscal discipline. However, the ANC remains plagued by factional tensions, frustrating the ability of President Cyril Ramaphosa to deliver on much-needed structural reform. Policy uncertainty lingers, as reflected in the divisive debates around land, the South African Reserve Bank's independence and the restructuring of Eskom. The latter's balance sheet problems remain an enormous overhang for the fiscus and the broader economy. Government has signalled its commitment to support Eskom financially, though the underlying state of the utility'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 first-quarter GDP print of -3.2%, dragged down by manufacturing and mining, in particular. Corporate financial results released during Q2-19, and the accompanying subdued tones of management, reinforce how dire the underlying economic situation actually is. The weak domestic economy, contained inflation and favourable global rate expectations have increased the likelihood of future interest rate cuts.

Performance attributions over the past three years have been boosted by our holdings in Cartrack, Mondi and Spar. Cartrack also contributed positively during the quarter, while our large weighting in British American Tobacco detracted. Richemont, while being the second largest position in the fund, contributed meaningfully to absolute fund performance in Q2-19, but its underweight position contributed to relative underperformance.

The British American Tobacco share price declined by 15.7% in the quarter, as prior concerns around the US regulatory environment, the extent of volume declines in the US market, the company's debt levels and the outlook for its next-generation products all resurfaced. We continue to believe that the regulatory concerns are overblown, and even if increased regulations – such as lower nicotine levels – are introduced, they will take years to implement. During this time, we expect the US to remain a very profitable market for British American Tobacco and will continue to help the company deleverage its balance sheet. Furthermore, we are very encouraged by the progress the company is making in next-generation products and believe its suite of products is particularly well positioned to gain market share and drive future earnings growth. The share is currently trading on c.9 times one-year forward earnings and a 7% dividend yield. We believe this to be extremely cheap for a stock of this quality and it remains a large overweight position in the fund.

Cartrack is the second largest overweight position in the fund and has contributed materially to performance over time. Cartrack is a vehicle tracking and telematics business that is leveraging its leading position in South Africa (SA) and selected African markets. It is also expanding internationally into Europe, the US and some exciting Asian markets. Its low cost, vertically-integrated model provides it with a competitive advantage relative to its peers, which has allowed it to achieve remarkable customer growth while maintaining industry-leading profitability margins. Its management team has some very exciting things planned for the business and we remain optimistic about its prospects.

Notwithstanding SA's economic challenges, we have been finding exceptional value in a number of domestic stocks and have been adding to our positions over the past few quarters. These include names such as Zeder, Pioneer, Rhodes Food Group, the local hospital groups, some of the food retailers and a number of smaller positions in selected small and mid-caps. Collectively, these stocks now comprise a meaningful part of the portfolio and, while the newsflow around these names might not be improving any time soon, we are excited about their return prospects.

During the quarter, trading activity was primarily limited to opportunistically adding to existing positions at attractive prices. Examples include Spar, MultiChoice, Aspen and Famous Brands. We funded these buys by trimming some of our Naspers and Richemont positions after a very strong run in both stocks.

Navigating the domestic equity market is certainly proving challenging at the moment but, given current valuations, we remain very excited about future return opportunities.

Portfolio manager changes

Sarah-Jane Alexander has been a portfolio manager on the fund for the past seven years and has made a significant contribution to its track record. From 1 May 2019 she will be focusing her efforts on managing the Coronation Equity and Balanced Plus funds. Joining Adrian Zetler as co-manager of the fund is Tumisho Motlanthe. Tumisho has been a member of the Coronation Equity team for the past 10 years and has already positively contributed to the fund through his analysis of a number of industrial and retail companies. We look forward to his future contribution.

Portfolio managers
Adrian Zetler and Tumisho Motlanthe
as at 30 June 2019