CORONATION
TRUST IS EARNED™

The fund delivered a year-to-date return of 11.8%, which was marginally behind the benchmark return of 13%. Our aim is to deliver outperformance over longer-term time periods. To this end, the fund's returns since inception are compelling, with alpha of 4.1% per annum, net of fees.

Our platinum-group metal (PGM) holdings, Pan African Resources and Trencor, contributed to performance this quarter, while Exxaro and Sasol detracted.

The third quarter of 2019 saw stock markets come under pressure. The mining sector was no exception. Escalating trade tensions and slowing global growth have been the key headwinds for the sector. These factors have started impacting demand for many commodities, sending commodity prices lower (as always, there were a number of exceptions, such as nickel, PGMs and gold). We regard most commodity markets as reasonably well balanced. Lower demand is somewhat tempered by supply austerity that has been in place since the 2015 commodity market lows. We expect increased Chinese stimulus to have a positive demand impact, although there is typically a 12-month lag from the implementation of stimulus to the breaking ground of infrastructure and property spend.

Anglo American, Glencore and Exxaro remain our preferred diversified miners. We have added to our Exxaro and Anglo American positions during the quarter. Exxaro's share price came under pressure as iron ore and thermal coal prices declined. We have been encouraged by Exxaro's capital allocation since the new management team has been in place. Actions include: the sale of Tronox for a reasonable price and paying out most of the proceeds as a special dividend; changing their dividend policy to pay through the full dividend they receive from Kumba Iron Ore; and purchasing buyback shares to minimise dilution during the replacement black economic empowerment deal. They have also managed their coal operations well. Exxaro is trading cum a R18 dividend. Apart from this, the share trades on six times our assessment of normal earnings.

Our PGM shares continued their strong performance this quarter. Northam Platinum and Impala Platinum (Implats) went up 40% and 37% respectively. Deficits in PGMs have seen the three elements' (platinum, palladium and rhodium) basket price continue to rise. Despite their strong run, we still view PGMs as very attractive. Our holdings in Northam and Implats trade on between 6 times and 8 times our assessment of normal earnings and have meaningful (albeit lower than a few months ago) upside to our fair values. Given the strong run, we have sold some of our shares in Implats. We have introduced a new position into the fund, being Sibanye Stillwater. In the past, we have had a number of concerns around the Sibanye investment case. These centred around their safety track record, leveraged balance sheet and acquisitive strategy.

On safety, we have been encouraged by their reducing their lost time injury frequency rate over time. They have introduced a number of interventions after their unacceptable 2018 fatality record. Encouragingly, they have been fatality-free in 2019 year-to-date in the troubled gold business. On the debt side, with PGM and gold prices where they are (and we consider current PGM prices to approximate "normal" levels), Sibanye could generate up to R17 billion in free cash flow in 2020, which would go a long way to reducing its current R27 billion in gross debt. So far, as acquisitions are concerned, we are confident that the heightened focus on reducing the debt levels will reduce corporate activity in the medium term. Sibanye trades on 4.3 times spot earnings and < 5 times normal, which we think this is very attractive. The assets it possesses (excluding Stillwater) are not on par with Northam and Implats; however, we have sized the position appropriately for its risk-return trade off.

Mondi is a very attractive business. It has a shareholder-friendly management team that balances the investment needs of the business with return-of-capital to shareholders. Over the years, they have invested heavily in their asset base to drive down their cost position and improve their return on invested capital. Their ownership and vertical integration into forestry assets provides them a moat that would be costly and near impossible for peers to replicate. They stand to benefit from the continued trend of offline-to-online shopping (necessitating increased packaging), and the trend of increased use of sustainable packaging and a shift from plastic to paper-based packaging. We do, however, expect a tough environment for Mondi in the short- to medium-term. European containerboard supply is increasing at a time when demand conditions are softening. We have reduced the size of our Mondi position, with the proceeds being applied to the diversified miners, as discussed above.

Sasol has been extremely disappointing for the fund. Further overruns on the Lake Charles Chemical Project (LCCP) cracker (when the project was 98% complete and no further overruns were expected), and the delay of their full-year results to June 2019, put pressure on the already depressed share price. We believe that the results delay is as a result of control weaknesses identified around the LCCP budgeting process and not centred around the financial statements themselves. A number of LCCP units have commenced their ramp up. As a result, we expect the company to shift to a phase of debt reduction and improved free cash flow. Sasol trades on four times 2021 earnings, which are set using what we feel are relatively undemanding rand-oil price assumptions. This is very attractive for a business of its quality.

Trencor announced that it will be unbundling Textainer to shareholders in the coming months. This is something Coronation has been pushing for over the last few years. The share price reacted positively (up 37% for the quarter) and we used the opportunity and reduced margin of safety to reduce our stake.
We are happy with current valuation levels and portfolio positioning. We believe prospective returns from this base will prove attractive.

Portfolio managers
Nicholas Stein and Nicholas Hops
as at 30 September 2019