CORONATION BALANCED PLUS FUND

Quarterly Portfolio Manager Commentary

CORONATION

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

This was a strong period for asset class returns, with the Fund returning 14.9% for the second quarter of the year (Q2-20). The Fund has performed well against its peer group over all meaningful, longer-term periods.

Following on from the record decline in equity markets during the first quarter of 2020, the second quarter saw a rapid recovery. The MSCI All Country World Index recovered 19.2% in US dollars during the quarter, reflecting the huge amounts of fiscal and monetary stimulus being injected into the global economy. The MSCI Emerging Markets Index was up 18.1% in US dollars for the quarter, but still declined (-3.4%) over twelve months. We remain concerned about the ability of lower-income emerging markets to withstand the economic shock, given their limited ability to provide financial support to businesses and households.

The FTSE World Government Bond Index rose (+2%) in US dollars for the quarter as markets remained indifferent to the risk that high and growing levels of government indebtedness present to bondholders. The very low yields offer a poor return for the rising risk and we continue to avoid global developed market sovereign bonds.

Having increased our exposure to global equities to an overweight position towards the end of the first quarter, these sharp upward moves resulted in us bringing back the position to a more neutral level. Our expectations for a faster economic rebound in more robust developed market economies and the risk diversification benefits for South African (SA) investors continue to justify a sizeable holding.

The All Bond Index (ALBI) returned 9.9% for the quarter, bringing the year-to-date number into positive territory. SA's bonds continue to offer attractive yields in a low inflation environment. However, the deteriorating fiscal position will require meaningful issuance to fund in the coming years and increases the risk of a debt trap. While June's supplementary budget acknowledged the challenge, it will take considerable political will to implement the level of structural reform required. We continue to watch this closely. The Covid-19-related demand shock provided the opportunity to add well-priced protection (in the form of Inflation-Linked Bonds) against the longer-term risks of a rise in inflation. The rand strengthened slightly against the US dollar (2.9%) but has still declined meaningfully year to date (-19.3%), reflecting the damage the Covid-19 economic shock has wrought on an already weak economy.

Along with its global counterparts, the JSE Capped Shareholder Weighted Index experienced a significant rebound during the quarter (+21.6%) but remains down (-10.7%) for the year to date. All sectors saw rising returns. Resources (+41.2%), with its high offshore exposure, outperformed industrials (+16.6), financials (+12.9%) and property (+20.4%)

The portfolio remains skewed to rand hedge stocks, which are attractive for stock-specific reasons and should also benefit from exposure to economies that are expected to rebound more rapidly. Early in the quarter we added meaningfully to positions in Bidcorp (+33.3%) and Anheuser-Busch InBev (+9.1%), as both had sold off meaningfully. Buying was largely funded by a reduction in the size of Naspers and British American Tobacco holdings, both of which have performed well and remain considerable holdings for the fund.

Bidcorp is a well-run food services business with a long-term growth opportunity. It has grown through international expansion but also in-country by expanding product ranges and getting closer to customers. Bidcorp's investments in local distribution centres and focus on small, profitable customers enable it to distinguish itself with high levels of service. While the Covid-19 pandemic has restricted out-of-home food consumption we believe the long-term aspiration remains intact. This was evident in the rapid resumption that Bidcorp has witnessed in its Chinese operations. Bidcorp is expected to continue its growth trajectory and trades on 15 times earnings three years out.

In the case of Anheuser-Busch InBev, poor results, growing concerns around Covid-19-related weaker beer consumption and high debt levels saw the share sell off markedly towards the end of the first quarter. We were able to acquire shares at a price of less than 10 times our assessment of normal earnings. Subsequent clearance by Australia's competition authority to dispose of an Australian subsidiary will assist in the de-gearing process. The stock is attractively priced for a global staples business, benefitting from the compelling economics of the brewing industry.

Domestic holdings remain concentrated in the higher-quality South African stocks such as the food retailers (Shoprite, Spar), whose more resilient business models are best placed to weather the very tough South African macroeconomic environment. Having held up well during the first quarter's sell-off, many of these underperformed during the second quarter, with the food and drug retail sector declining -2.0%.

We acknowledge that many of the more cyclical domestic businesses look cheap, but we are concerned that the long-term headwinds they face are considerable and strengthening. Weak revenue prospects due to an already weak economy are now expected to be compounded by rising retrenchments, which will ultimately feed through to consumer demand. An underweight in domestic stocks continued to benefit the Fund.

Resources rebounded strongly during the quarter (+41.2%) as the demand outlook for commodities improved due to a resurgent Chinese economy and the easing of restrictions elsewhere. Covid-19-related supply disruptions also tightened markets. This benefitted the Fund's increased exposure to resources with sizeable positions in Anglo American (+31.9%) and the platinum shares. Platinum miners rose as concerns over weak automotive demand subsided and major markets reaffirmed their commitment to a reduction in emissions. The Fund remains invested in Impala Platinum (+53.2%) and Northam Platinum (+67.4%).

The gold price continued its upward trajectory (+12.9% Q2-20 / +26.3% over twelve months) given investor concerns around building risks in the financial system and monetary debasement. While the Fund benefits from some direct exposure to gold, we do not hold a position in the producers, whose capital intensity and high-cost mines have resulted in lacklustre returns to shareholders over time.

The market correction began at a point when investors were still being bombarded daily with negative news flow on the extent of the pandemic's economic shockwave. The massive sell-off had created a value opportunity. We retain our commitment to look through the short-term noise and use valuation as our anchor point when investing; selecting assets where we believe the market is mispricing the long-term fundamentals.

Portfolio managers
Karl Leinberger, Sarah-Jane Alexander and Adrian Zetler
as at 30 June 2020