CORONATION
TRUST IS EARNED™

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

The Fund returned 1.3% for the quarter, in line with the benchmark. Year to date, the Fund has returned -3.4%, which is ahead of the benchmark return of -3.7%. We always strive to manage the Fund with a long-term time horizon and ask to be judged over meaningful periods of time. To this end, September 2020 is the month in which the Fund celebrates its 20-year anniversary. We are proud of the Fund's long-term track record and the contribution it has made for unitholders over this period and wish to thank unitholders for their support. The Fund is in the top quartile over most meaningful periods, and alpha since inception has been 3.6% per annum, net of fees. We hope to be able to deliver the same level of outperformance for the next 20 years.

Against our rebased view of the world, we have been pleasantly surprised by a number of the company results reported in the last month. When the magnitude and global reach of Covid-19 became apparent, we moved fast to rebase our earnings expectations lower based on the harsh economic conditions we expected. While the results have been better than these lower expectations, they are still obviously significantly weaker than the pre-Covid-19 outlook. Whether we were too conservative on our adjusted forecasts, or there is still worse to come as the economy fully reflects the damage from lockdown, only time will tell.

We think the full extent of the economic pain has yet to be revealed. This is premised on a number of specific factors:

1) Many consumers avoided transport costs during lockdown;
2) Consumers have been receiving Temporary Employer-Employee Relief Scheme payments;
3) Retrenched individuals still have retrenchment sums to tap into in the shorter-term;
4) We expect more companies to proactively rightsize their expense base for a tougher climate.

Our South Africa (SA) exposure remains largely tilted towards defensive businesses with strong economics. A tough economic climate will see strong companies getting stronger and industries with strong economics and pricing power outperforming weaker ones. This was well highlighted by the results reported by Shoprite. Shoprite grew earnings strongly, increasing its market share from an already impressive position. They also took action on underperforming regions (they have announced their intention to exit lossmaking Nigerian operations. Cash flow improved meaningfully as inventory levels were optimised post their SAP implementation. We trimmed our holding, given the strong share price performance and reduced margin of safety.

We have been increasing our exposure to the life insurance sector. Life companies have a number of appealing attributes:

1) A 'sticky'/desirable product set in retirement savings and life insurance. Covid-19 has heightened consumer awareness for life cover;
2) Extensive distribution networks, which are costly and time consuming to replicate;
3) c30-40% earnings exposure to equity markets, which we think offer good value;
4) Large back books continued to generate fees during lockdown;
5) Diversified earnings streams (life insurance, short-term insurance, annuities);
6) Strong capital positions.

Embedded value is often used as a reasonable proxy for life insurance valuations. Life company share prices have derated meaningfully relative to embedded value over the last few years and in the third quarter of 2020 in particular. Momentum Metropolitan has gone from a premium to embedded value in 2015 to a 40% discount today. New management has impressed us through their implementation of a turnaround plan and has placed the business on a firmer footing, improving underlying operational performance and exiting underperforming operations. This was well demonstrated in Metropolitan Life's recent results, which outperformed peers as adviser productivity and digital initiatives bore fruit. We don't think the market gives sufficient credit to the turnaround that is underway. Meaningful earnings pain was taken now in the form of Covid-19 provisions. We believe these will support robust earnings in future periods.

Sanlam is a new position in the Fund. We have long admired the business for its strong growth profile, high-calibre management team and high levels of accounting prudence (a rand of Sanlam earnings is worth more than a rand of earnings at its peers, given the extent to which they raise provisions in downturns). Historically, we haven't owned Sanlam given the lack of margin of safety (for the better part of a decade, we have had little to no upside to our assessment of fair value). The recent sell off has allowed us to pick up a quality compounder at an attractive valuation.

We continue to exhibit a preference for the global businesses that happen to be listed in SA – both industrial and mining. Emerging market economies such as SA are worse-placed than developed market counterparts to withstand the tough economic outlook we expect – both from a financial resources and an institutional capacity perspective. Most of these global shares have attractive growth outlooks, hard currency backing and trade on compelling valuations. Our two largest holdings here are Naspers and British American Tobacco (BTI).

We wrote about Naspers/Prosus last quarter. We have used Prosus as a funding source during the quarter, including switching some of our Prosus shares into Naspers. The Naspers discount to Prosus continued to widen, reaching 30%. While we expect some discount to persist, we think the quantum is too wide and that management will take actions to deal with the discount in due course.

In a world starved of yield, we find BTI's 8% dividend yield to be very compelling. In addition, unlike a government bond, we do not believe BTI is ex-growth and would expect this yield to grow. The market remains concerned around a possible menthol ban in the US (US menthol is c25% of BTI group profits). However, tobacco legislation tends to play itself out over periods of many years in the US. A menthol ban in Canada saw a limited reduction in smoker numbers and 99% remain with their current cigarette brand. BTI is also well placed to be one of the winning companies in next-generation products such as e-vapour and heated tobacco.

We remain constructive on the miners. We believe that the commodity sector has several elements to it that are unprecedented in comparison to historical cycles which, when combined, present a unique investment opportunity. The sector is displaying remarkable supply restraint in the face of healthy margins and incentive prices in several commodities. The decarbonisation of the world over the next few decades is incredibly positive for metal demand (notably copper, nickel, cobalt and PGMs) and stands to produce strong price outcomes when combined with supply, which is yet to respond. On top of this supportive earnings environment, management teams have committed to material capital returns to shareholders, made more attractive by historically cheap starting valuations. We discuss this topic in more detail in our quarterly Corospondent newsletter. We continued adding to our Glencore position during the quarter.

The world remains an uncertain and volatile place. This does unearth good opportunities for stock pickers with long time horizons. We track the upside of the portfolio over time. The current upside remains high relative to history and suggests that future returns from the portfolio should be good.

Portfolio managers
Neville Chester and Nicholas Stein
as at 30 September 2020