CORONATION
TRUST IS EARNED™

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

Following a strong start to the year, the financial sector remained in positive territory for the second quarter (Q2-21), with the Fund delivering 5.2% relative to 8.2% for the benchmark. Over three, five and 10 years, the Fund has returned -4.9%, 0% and 8.1% relative to benchmark returns of -3.0%, 0.7% and 9.2% respectively. Since inception, the Fund delivered 10.5% p.a. against the benchmark return of 9.0%.

Developed market equities continued to rise during the quarter as the benefits of rapid vaccine rollouts in the developed world began to have a positive impact on the pandemic, allowing for an opening up of economic activity. The MSCI World Index returned 7.7% in US dollars versus a 3.6% US dollar return for JSE All Share Index in a quarter during which the rand strengthened 3.5% against the US dollar. In South Africa, Q1-21 GDP was stronger than expected at 4.6% (p/p), seasonally adjusted. While headline inflation accelerated to 5.2% y/y in May from 4.4% y/y in April, core inflation was stable at 3.1% y/y in May vs 3.0% y/y in April. The SARB left interest rates unchanged, but more recent comments from the Monetary Policy Committee members suggest some growing caution about the inflation outlook. In the near term, inflation should be contained as growth picks up, supporting a cyclically improved economic outcome. While the fiscal accounts are problematic given the high levels of debt, the improvement in the economy has provided some breathing room. Growth-enhancing reforms are still needed for a more sustained economic recovery.

The financial sector performance for the quarter was driven by strong returns from the listed property (12.1%) and banking (9.6%) sectors, while the life sector (5.8%) lagged. Fund contributors to quarterly returns included overweight holdings in Investec Plc, Nedbank Group Ltd, RMB Holdings Ltd and Momentum Metropolitan Holdings, as well as an underweight position in the Johannesburg Stock Exchange Ltd. Detractors from quarterly performance included overweight positions in Quilter Plc, Ninety One Plc and Coronation Fund Managers, and underweight positions in Capitec Bank and Growthpoint Properties.

Throughout the Covid-19 pandemic, as measured from the start of the second quarter of 2020, the life sector has underperformed the banking sector. Covid-19 lockdowns presented challenges for both sectors but in different areas. The banks were most concerned about credit default risk on their lending books, given the likely impact that the Covid-19 lockdowns would have on employment and the ability for companies to trade profitably. During 2020, the banks raised significant provisions in anticipation of this risk. Recent bank results and operational updates suggest that the sector was prudent in the level of provisions raised, with defaults proving lower than expected. This has driven a faster recovery in earnings for the sector and supported a re-rating in valuations.

The life sector faced concerns in two areas: a likely increase in mortality claims and a fall in new business volumes and, like the banks, raised reserves to cover the anticipated higher mortality risk. SA has gone through two Covid-19 waves and is currently in the midst of the third. As these waves progress, the life companies utilise the reserves raised and, at each reporting period, review the adequacy of the remaining buffers in light of an evolving Covid-19 picture. While this journey may not yet be complete, we believe the sector is adequately capitalised to weather the pandemic and return to more normalised levels of profitability. The intrinsic value of these businesses remains robust, and therefore valuations within the life sector are attractive. We took the opportunity in the quarter to add to holdings in Sanlam, Old Mutual, Liberty and Discovery. These were funded from the banks, Reinet and Santam.

Domestic and international equity markets have recovered strongly off the lows reached in April 2020 at the start of the Covid-19 lockdowns. This recovery in markets enhances the earnings prospects for businesses generating fees from market-linked assets, such as asset managers and wealth businesses. The life sector also benefits from improving capital ratios to the extent that they are exposed to equities within their shareholder portfolios. Interestingly, we have not seen a recovery in valuations of asset managers and wealth businesses commensurate with our expectation of their improving earnings prospects. Therefore, we are excited about the valuation opportunities in Quilter (UK wealth manager) and Ninety One (fund manager), both significant holdings in the Fund.

We see opportunity amid the challenges SA is navigating, both on the pandemic front and on the fiscal side. The financial sector in SA has some strong and enduring businesses that are well-capitalised and run by experienced management teams. Currently, many of these businesses can be bought at undemanding valuations. We continue to position the Fund to benefit from these opportunities.

Portfolio managers
Neill Young and Godwill Chahwahwa
as at 30 June 2021