CORONATION
TRUST IS EARNED™

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

The Fund has made a good start to 2021, delivering a 15.7% return for the quarter. The Fund remains the best performing small and mid-cap fund over one, three and five years to end-March 2021, delivering a return of 5.7% per annum for the past three years. While one may not get excited about this return from an absolute perspective, the number does include a year during which most companies were severely impacted by the global pandemic – Covid-19.

It is remarkable how well many shares have recovered after the initial Covid-19-induced panic selling. It is not uncommon to see shares that have doubled, or more than doubled, off their April 2020 lows. In fact, the Fund is up 76.8% in the past year, admittedly off a low base. It seems to us that while Covid-19 has hurt some companies, others have used the crisis wisely to strengthen their business. This may have happened in a number of ways:

- Permanently lowering the cost base
- Generating strong cash flows as a result of not having to fund working and fixed capital expenditure and using these cash flows to:
  - Buy back undervalued shares
  - Make acquisitions at distressed valuations
  - Return capital to shareholders.

Our focus, therefore, has been to identify those companies that might come out of this pandemic in better shape than before. Some examples of this are Mpact and Cashbuild.

Mpact generated very strong cash flows in the past year and used these cash flows to buy back 15% of their own shares at very attractive levels. This has been materially value-enhancing to shareholders, and there is now a good chance that the business is worth more today than before the pandemic.

Similarly, Cashbuild has been a beneficiary of the pandemic as a result of the very strong demand we have seen for building materials. In addition, Cashbuild has bought a large competitor, The Building Company, based on the company's pre-pandemic earnings – i.e., before the strong industry sales growth. This acquisition should end up being materially earnings and value-enhancing when it is finally consummated.

Managing a fund is all about rotating out of shares that have limited upside (and have typically performed well) into shares with more upside (and have typically not performed well) while at the same time being mindful of the overall quality of the portfolio holdings (i.e., not rotating out of good quality into poor). Our two largest buys and sells in the quarter to end-March are good examples of this.

JSE Limited and Zeder (the two largest buys)

The JSE is a fantastic business. It is essentially a regulated monopoly (yes, there are other exchanges, but they have <1% market share), generates high returns on capital and strong cash flows. It also has countercyclical features in that it benefits from volatility in markets, which often occurs when other shares perform poorly. As such, it is a good addition to a diversified portfolio.

Zeder has an attractive risk/reward profile, in our opinion. It is no secret that the company is essentially in wind up mode, a process overseen by PSG, whom we consider astute investors. Zeder's underlying assets are worth somewhere around R4 per share, while the share price trades at around R2.60. We acknowledge that a wind up will not be easy or happen quickly, but even if this process takes three years, we believe that our investment in Zeder today will ultimately result in an attractive risk-adjusted return for our investors in the Fund.

Bytes Technology Group and Impala Platinum (our two largest sells)

Bytes (and Altron) have been fantastic holdings for the Fund. Bytes was spun out of Altron and listed on the London Stock Exchange. In the process, a huge amount of shareholder value has been created. The business is well placed as a value-added reseller of software, predominantly in the UK. However, at today's price, it trades on a 28x one-year forward PE multiple on our forecasts, which we consider to be stretched. As such, we sold out of Bytes and are very happy with the returns realised within the Fund from the holding!

Impala is not a dissimilar situation. It has been a fantastic performing holding for the Fund. Right now, platinum-group metals (PGM) shares are in high demand, fuelled by the seemingly insatiable appetite for the underlying PGM metals. This demand has driven the PGM basket price to levels that we consider to be materially above normal and cost curve support levels. These high metal prices mean that Impala still only trades on a mid-single-digit forward multiple, which gives an illusion of value and safety. However, there is nothing safe about owning PGM shares at these levels, in our opinion, and we have therefore elected to take the profits and invest the proceeds in other lower heartbeat opportunities within the Fund.

Portfolio manager
Alistair Lea
as at 31 March 2021