INVESTING FOR LONG-TERM CAPITAL GROWTH

COROLAB

Your guide to investment ideas

10/19

CORONATION

TRUST IS EARNED™

THE CORONATION CLIENT CHARTER

We strive to always put clients first

We have an unwavering commitment to the long term

We focus on producing top performance over all meaningful periods

We are uncompromising about ethics

THE CASE *for being patient*

Investors looking to achieve long-term capital growth have one great advantage – time. When you are investing to fund a long-term objective such as your retirement, your investment time horizon spans decades rather than years. This allows your investment portfolio to benefit from the key drivers of capital growth.

DRIVERS OF LONG-TERM *capital growth*

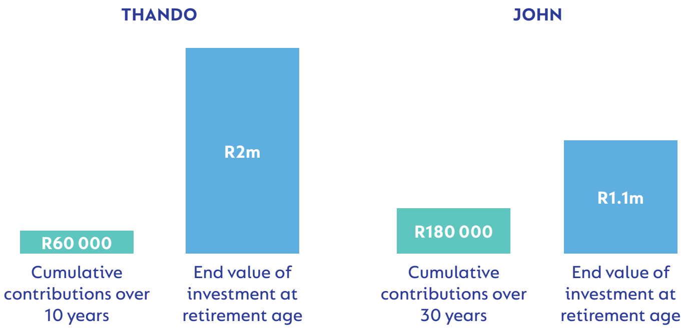
1. The power of compounding

Critical to long-term wealth creation

Compounding is the process of re-investing an asset's returns (from either dividends or interest), which creates a larger base from which you can earn returns in the future. As a result, compounding is an exponential rather than a linear function, so the longer you have to invest, the greater the possibility of dramatically multiplying your purchasing power.

Let's consider compounding's extraordinary power with an example. Thando starts to invest R500 a month at the age of 25. She contributes the same amount monthly for a period of 10 years, with her investment growing at a rate of 10% a year. After 10 years, she stops contributing on a monthly basis and simply allows her investment to grow until her retirement age of 65.

John also invests R500 a month, but only starts 10 years later than Thando (at the point where Thando stops her contributions). He then continues to contribute that same amount diligently until his 65th birthday. His investment also grows at 10% a year.



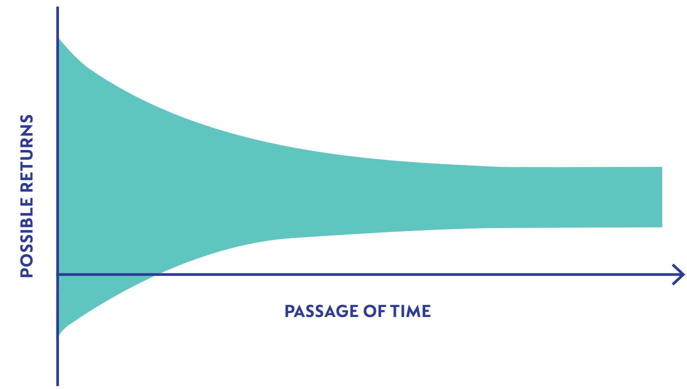
WHAT HAS MADE THE BIG DIFFERENCE FOR THANDO?

The important point to note, as illustrated above, is the significant difference between the end values for Thando and John. At 65, Thando (who only contributed for a period of 10 years and then left the investment to compound over a period of 40 years), had accumulated an amount of more than R2 million. At 65, John (who contributed three times more than Thando) only accumulated half the end value of Thando's investment.

2. *Time diversification of risk*

The benefit of lengthening your time horizon

'After compounding, time diversification of risk is your second-best friend in the market,' writes Franco Busetti in *The Effective Investor* (Pan Macmillan, 2009). Put simply, time diversification means that the longer you hold a growth asset (such as equities), the lower your risk of losing capital becomes.



Consider an investment in equities – the asset class that provides the highest expected return over time, but with higher short-term volatility. The chance of losing capital in any one-year period is much greater than that of an investment in cash or bonds. However, the longer you remain invested in equities, the lower this variability becomes.

R1 committed to *local equities* almost 90 years ago = *R579 today.*

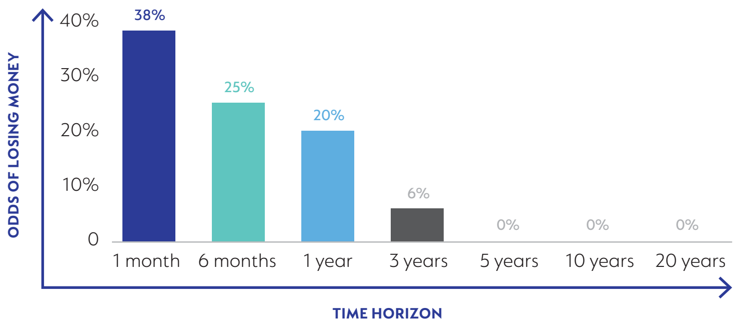
R1 committed to *local bonds and/or cash* over the same period = *R1-3 today.*

Figure 1 shows the odds of losing money on an investment in domestic equities (as measured by the FTSE/JSE All Share Index) over different investment time horizons (rolling 5, 10, 20 years, etc.).

Using returns dating back as far as 1960, it confirms the fact that your likelihood of losing capital on your investment diminishes drastically as your investment horizon increases. Although there has not been a negative return experience from local equities over a 5-year period since 1960, this doesn't imply a future guarantee but rather illustrates the benefit of a longer-term horizon when allocating to growth assets.

Figure 1

YOUR ODDS OF LOSING MONEY REDUCE DRASTICALLY IF YOU GIVE YOUR INVESTMENT TIME



Source: Coronation Fund Managers as at 30 September 2019

3. Asset allocation and diversification

The benefit of making good strategic and tactical decisions

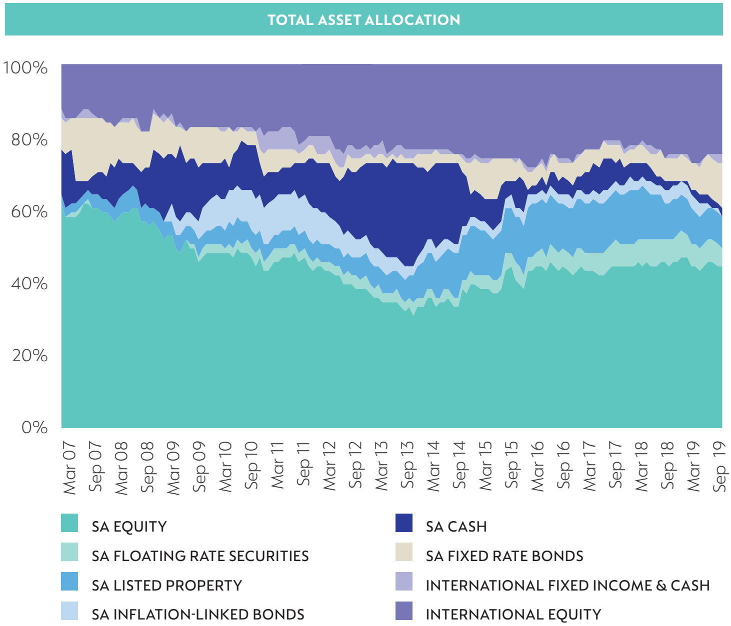
Investors in balanced funds, or those who have the skills to perform the asset allocation themselves, can enhance the eventual outcome of their savings by making good strategic and tactical asset allocation decisions in response to the dynamic market environment, which may include:

- new opportunities arising as companies, industries, countries and asset classes develop and contract;
- changes in relative valuation levels, both within and between asset classes over time;
- a growing investible universe thanks to new asset classes (e.g. inflation-linked bonds);
- the deepening of existing asset classes (e.g. new listings and more activity, as was the case in the domestic listed property market); or
- changes to regulations that restrict or enhance the freedom to invest in foreign markets.

Figure 2 (overleaf) illustrates how we have used the above tools to add value through active allocation in our flagship balanced fund, Coronation Balanced Plus, over more than a decade. The stand-out features are:

1. Our comfort with temporarily holding relatively high levels of cash at times when we believe valuations to be stretched in higher return/higher risk alternatives such as bonds, property and equity; and
2. The increase in offshore equity exposure over time, primarily at the expense of local equities. This trend was partly due to regulatory action, as exchange control limits were gradually relaxed to the current 30% foreign asset limit, but, more importantly, driven by the more attractive relative valuation of global compared to local shares at certain times.

Figure 2



Source: Coronation research

4. The value of active returns

***Alpha**
Industry term for the difference between the return of an actively managed fund and that of the market index. Zero alpha means the earned return = that of the market.

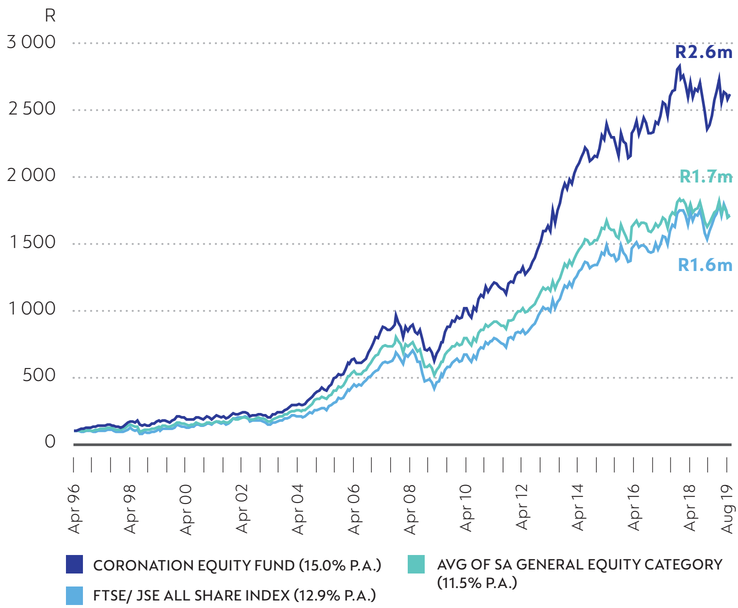
Investing with a skilled fund manager, which actively manages your portfolio, gives you the opportunity to add alpha*, which can add significantly to your investment over time.

Coronation, like all active managers, pursues the outperformance of market indices or benchmarks (net of the fees we charge and costs that our portfolios incur). In **Figure 3** we illustrate the rewards of adding an active return to that of the market by having remained invested with Coronation over the long term. An investment in the local equity market more than 20 years ago would have grown your capital by a little over 15 times (in nominal terms), whereas a similar investment in the Coronation Equity Fund, which has outperformed the market by 2.5% p.a. after fees (a seemingly small number), would have grown your capital by just over 26 times.

Figure 3

GROWTH OF R100 000 INVESTMENT IN CORONATION EQUITY

CUMULATIVE RETURNS SINCE INCEPTION ON 15 APRIL 1996



Source: Coronation Fund Managers as at 30 September 2019
For more detail about the fund, refer to the fund information table at the end of this edition.

The conclusion is as simple as it is compelling. Invest in the equity markets for long periods of time, stick with winning fund managers for the long haul, and the power of compounding will most likely do extraordinary things for you.

A FEW THINGS *to consider today*

EXPECTED RETURNS

Long-term savers are ultimately interested in the real (or after-inflation) rate of return. Earning a positive real return is the 'reward' you get for delaying gratification.

The following table demonstrates the material impact that your expected real return will have on your future purchasing power. The ability to compound returns at a real rate of 5% (as has been achieved by Coronation Balanced Plus over the last decade) increases your purchasing power by 1.6 times over 10 years and by 7 times over 40 years. Being able to add an additional 2% p.a. over the average competitor fund (also achieved by Coronation Balanced Plus since its inception) improves purchasing power by two times after a decade, and by 15 times over 40 years.

INCREASE IN PURCHASING POWER

	REAL RATE OF RETURN		
INVESTMENT PERIOD IN YEARS	**2.5% p.a.**	**5% p.a.**	**7% p.a.**
10	1.3x	1.6x	2.0x
20	1.6x	2.7x	3.9x
30	2.0x	4.3x	7.6x
40	2.1x	7.0x	15.0x

Source: Coronation Fund Managers

SELECTING A PRUDENT REAL RATE OF RETURN

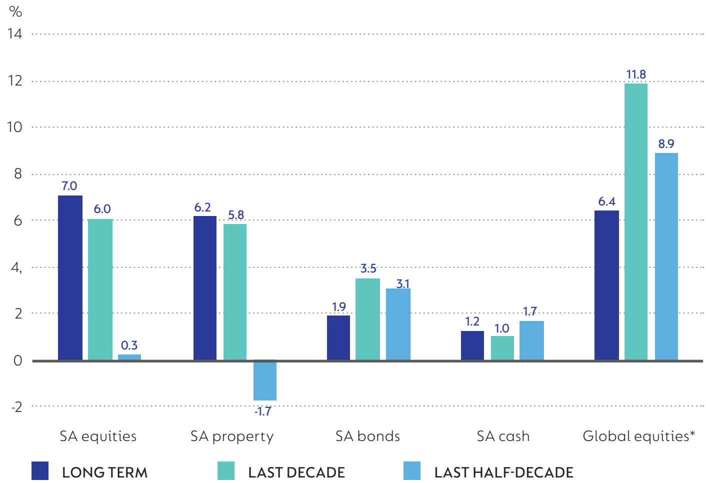
But the future, by its very nature, is uncertain and we have, at best, only partial information to inform our forecasts. A good starting point to selecting prudent rates of return is to look at the very long-run asset class returns. From **Figure 4** it is clear that:

- growth assets (property and equity) produced a real rate of return between 6% and 7%; while
- income assets (cash and bonds) earned between 1% and 2%.

This implies an expected long-run real rate of return of around 5% p.a. for a typical balanced fund (assuming growth asset exposure of between 70% – 75% and income asset exposure between 25% – 30%). Apart from global equities and local bonds, actual real returns achieved over the past decade were more or less in line with the long-term average across most of the major asset classes, which explains why the typical balanced fund achieved a real return of 4.0% p.a., while Coronation Balanced Plus, due to a positive active return contribution, achieved a real return of around 5.3% p.a. over the same period.

Figure 4

ANNUALISED REAL RETURNS PER ASSET CLASS (LAST 119 YEARS VS LAST DECADE AND HALF-DECADE)



**MSCI World Index*
Source: Deutsche Bank, IRESS, Triumph of the Optimists – Dimson, March and Staunten
**Shorter history for foreign equities (49 years) and local property (39 years)*

WHAT ARE OUR EXPECTATIONS FOR THE NEXT DECADE?

The upper band of our 10-year forecast range for local equity (see **Figure 5**) is now slightly above the experience of the last decade as a result of more attractive valuations. The strong performance from global markets has contributed to global equities outperforming local equities over the past decade and warrants caution in future expectations. However, it is reasonable to expect better returns from the average balanced fund over the next decade, based on a more favourable outlook for local growth assets. Considering our forecasted returns for the different asset classes that make up your typical balanced fund, it is reasonable to expect a real return going forward that is more in line with the long-term average return. In other words, after a five-year period of underwhelming returns, there is a higher probability of balanced funds meeting return expectations going forward.

Figure 5

10-YEAR FORECASTS FOR LOCAL AND OFFSHORE ASSET CLASSES (ZAR)

	LAST 10 YEARS*	10-YEAR FORECAST**
Local equity (SWIX)	11.5%	9-12%
Global equity (ACWI)	16.2%	7-9%
Local property (ALPI)	11.2%	9-12%
Local bonds (ALBI)	8.8%	8-9%
Global bonds (BGAB)	9.8%	8-9%
Cash	6.6%	6-7%
Inflation	5.1%	4.5%-6%

*Source: Deutsche Bank as at 30 September 2019 and *Coronation Fund Managers forecasts. While these forecasts are not guaranteed to occur, they are based on our best estimates for possible future returns and represent a more prudent basis for informing planning assumptions than historical results achieved over the past decade.*

INVESTING FOR LONG-TERM CAPITAL GROWTH *with Coronation*

Investors invest for the long term for different reasons. It may be for discretionary purposes, such as your child's education in five to 10 years' time, or for your retirement, which may be multiple decades (30 to 40 years) in the future.

Depending on your specific goal (and investment horizon), we offer a range of funds aimed at meeting the needs of investors who want to achieve long-term capital growth.

INVESTING FOR THE LONG TERM IN A RETIREMENT PRODUCT

INVESTORS NEED TO CHOOSE BETWEEN:

- **investing in a multi-asset (balanced) fund; or**
- **performing the asset allocation themselves by way of building block funds (DIY portfolio)**

Regardless of your chosen investment approach (balanced fund or DIY portfolio), your underlying investment portfolio needs to comply with Regulation 28 of the Pension Funds Act, which allows you to invest up to 75% in equities and a maximum of 30% in international assets.

We do believe that the majority of investors are better off investing in a multi-asset fund with a strong track record, such as Coronation Balanced Plus (see **table on page 12**).

	BALANCED PLUS
Fund description	Our best investment view across asset classes for retirement savers.
Recommended investment period	5 years +
Annualised return* (since inception)	14.1%
Benchmark return (since inception)	12.9%
Peer group average (since inception)	12.2%

** Refer to the fund information table at the end of this document.*

INVESTING FOR THE LONG TERM FOR DISCRETIONARY PURPOSES

INVESTORS NEED TO CHOOSE BETWEEN:

- **investing in a single-asset class; or**
- **a growth-oriented multi-asset portfolio**

SINGLE-ASSET CLASS

We offer two equity (single-asset class) portfolios that pursue market-beating returns over the long term for investors that are able to withstand short-term market turbulence. These funds are not suited to investors who are concerned about short-term capital losses or who want to generate consistent income. The Coronation Top 20 Fund is a concentrated portfolio that consists of no more than 20 of our best SA equity ideas. As a result of its concentrated nature, the fund is not suitable for those who seek an equity investment that tracks the returns of the market. Coronation Equity is less concentrated than Coronation Top 20, making it more suitable for investors holding only one equity fund. The fund may underperform the market in the short term in pursuit of superior long-term gains.

MULTI-ASSET CLASS

We also offer two worldwide multi-asset portfolios for investors looking to build up capital outside of a retirement fund, but who prefer to leave the asset allocation decision-making to the skilled portfolio manager. In the case of Market Plus, investors gain access to our best views across all asset classes limited to a maximum offshore investment of 40%. In the case of Optimum Growth, investors look to access Coronation's best long-term views without any geographical constraints, allowing Coronation the discretion to invest up to 100% of the portfolio offshore.

	TOP 20	EQUITY	MARKET PLUS	OPTIMUM GROWTH
Fund description	A focused portfolio of our top stock picks on the JSE.	A less concentrated equity portfolio than Top 20 that can also invest up to 30% of your money offshore.	A balanced long-term portfolio that will have more of your money invested in South Africa than offshore over time.	An aggressive long-term portfolio that will have more of your money invested offshore than in South Africa over time.
Recommended investment period	10 years +	10 years +	5 years +	10 years +
Annualised return* (since inception)	16.9%	15.0%	15.0%	14.3%
Benchmark return (since inception)	13.3%	12.5%	13.2%	11.4%
Peer group average (since inception)	13.6%	11.5%	10.4%	10.2%

** Refer to the fund information table at the end of this document.*

Investors who wish to invest for long-term capital growth in one of our international funds, can download our Offshore Investing Corolab from coronation.com.

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*Fund information table

FUND	LAUNCH DATE	BENCHMARK	HIGHEST ANNUAL RETURN (SINCE LAUNCH)	LOWEST ANNUAL RETURN (SINCE LAUNCH)
Coronation Balanced Plus	15 April 1996	Composite: 52.5% equity, 22.5% bonds, 20% international, 5% cash	**49.3%** (Aug 2004 - Jul 2005)	**-17.4%** (Sep 1997 - Aug 1998)
Coronation Equity	15 April 1996	Composite: 87.5% SA equity, 12.5% International equity	**62.5%** (Aug 2004 - Jul 2005)	**-28.7%** (Mar 2008 - Feb 2009)
Coronation Top 20	2 October 2000	FTSE/JSE Capped All Share Index (CAPI)	**68.9%** (May 2005 - Apr 2006)	**-31.7%** (May 2002 - Apr 2003)
Coronation Market Plus	02 July 2001	Composite: 52.5% equity, 22.5% bonds, 20% international, 5% cash	**50.0%** (Aug 2004 - Jul 2005)	**-20.1%** (Mar 2008 - Feb 2009)
Coronation Optimum Growth	15 March 1999	Composite: 35% JSE CAPI, 15% ALBI, 35% MSCI ACWI, 15% BGBA	**51.1%** (Jan 2013 - Dec 2013)	**-31.5%** (Mar 2008 - Feb 2009)

Disclaimer

For **enquiries** you can call us on **0800 22 11 77**
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For **more information or to invest online**, visit us on **www.coronation.com**.