EXECUTIVE SUMMARY
CONVERSATIONS WITH CORONATION

JULY 2016

THE CASE FOR INVESTING OFFSHORE

Now, as much as ever, South African investors should have strategic exposure to global investments.

The JSE represents less than 1% of global markets, with the local index consisting of only 160 businesses, compared to the 2 500 businesses included in the MSCI All Country World Index. Global diversification also offers exposure to a whole range of industries not present in SA. For SA investors, global investments also offer a good hedge against exchange rate risk for future liabilities: energy and food prices are set in international markets, and healthcare is heavily dependent on imported content. Research shows that an optimal portfolio has 20% to 30% in global holdings.

The global exposure of Coronation's domestic multi-asset funds remains at the 25% limit, and we believe that clients can benefit from externalising their global investments. While it requires more administration and may be more expensive than investing in rand-denominated funds, having assets outside of the country offers better insurance against sovereign risk. Also, rand-denominated funds are increasingly likely to be impacted by capacity constraints, given that investors in these funds utilise Coronation's foreign investment allowance (currently set at 35% of the household assets invested in our unit trust funds). While Coronation's funds will remain open for the foreseeable future, we are approaching the exchange control limit, and may need to temporarily close our rand-denominated funds to new investments in periods where we exceed the 35% limit.

THE MACRO ENVIRONMENT

Global economic growth has stalled, partly because there is still too much debt in the system. Pockets of deleveraging in the US banking and consumer sectors have been more than overwhelmed by unprecedented credit expansion in Europe, as well as in China and Japan (where debt to GDP has reached an unparalleled 400%). Elevated debt levels sap confidence, which discourages investment and consumption. The end of the commodity supercycle, demographic headwinds in Europe and Japan, and technological disruption are posing economic challenges, while the global elite and emerging market middle classes continue to benefit at the expense of working and middle classes in developed markets.

Against this backdrop, it should not be a surprise that political risk is increasing and that pressure is building against the current consensus that favours globalisation and trade; the rise of Donald Trump and Brexit are prime examples. The latter has created more uncertainty and dented already fragile confidence in the UK and EU. Brexit, however, did not create a Lehman-style contagion. Sterling and UK-focused businesses bore the brunt of the impact. In particular, UK property stocks were hard hit, and we used the opportunity to increase exposure as the immediate sell-off was overdone. The consensus is that Brexit could lower the value of property companies by around 10%, while prices declined by more than 25%. With yields of some 5% (compared to less than 1% for 10-year UK gilts), we are comfortable holding UK property stocks. We prefer Intu, which offers a defensive income stream from properties in areas less likely to be directly impacted by Brexit, to Capco, which has more exposure to residential property serving the City of London, and may see a bigger impact.

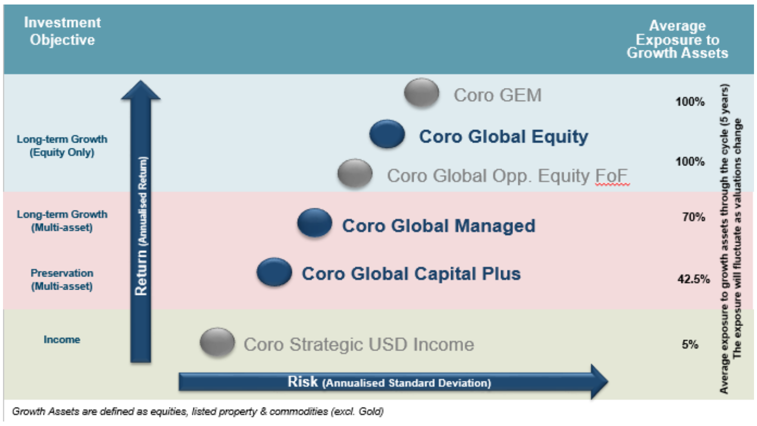
In the short term, we expect lower growth in the UK (perhaps tipping into recession), but the long-term risk is that it is now slightly more likely that the EU may break up completely. Also, Brexit has further fuelled what we think is a massive bubble in government bonds. A third of government bonds worldwide are now trading at negative yields. While other investors may be willing to lock in a loss, we are not: our multi-asset funds do not hold any global government bonds. This has hurt our short-term performance against some fund benchmarks. Over the past 12 months, global bonds returned 12% in US dollar terms, compared to 0% from equities. We do not believe this is sustainable.

US 10-year Treasury yield close to its all-time low following the Brexit result

Source: Bloomberg

UK and European monetary policy will continue to be supportive, while markets currently expect US rates to remain unchanged until 2018. This means half a generation in the US has not seen an interest rate hike, which is distorting behaviour and asset prices, not only for bonds but also for other assets such as safe dividend payers (so-called bond proxy stocks, including consumer staples such as Unilever and Nestlé). Still, these stocks are trading around fair value assuming normal US bond yields, whereas bonds are completely overpriced on a long-term view.

CORONATION'S GLOBAL FUND RANGE



Multi-asset funds

We provide investors with robust risk tailored solutions in the managed fund space, with Global Managed focused primarily on return and Global Capital Plus focused mainly on risk.

Coronation Global Capital Plus is a low-risk fund aiming to deliver returns ahead of inflation without negative 12-month rolling returns. It has outperformed its benchmark by almost 3% per annum since inception. The fund offers diversified exposure to global assets with a focus on capital preservation. Its equity exposure is currently around 34%, compared to a maximum allowed exposure of 50%.

Coronation Global Capital Plus
Performance since inception*

** Since inception – November 2008 (ZAR feeder fund converted to USD)*
*** Benchmark – 3m cash*
Note: Performance net of fees (USD)

Coronation Global Capital Plus
Performance (31 July 2016) vs. local unit trusts (ZAR)

	YTD	1 year	3 years (p.a.)	5 years (p.a.)
Coronation Global Capital Plus Fund	-6.2%	12.6%	13.2%	18.3%
Median – Low equity	-6.2% *(7)	11.8% *(7)	12.6% *(7)	16.7% *(7)

** Number of funds*

Coronation Global Managed is a medium-risk fund, aimed at maximising returns from traditional asset classes. Investors in this fund get exposure to our houseview asset allocation, with our best instrument picks within each asset class.

Equities remain the asset class of choice, but we are finding it harder to find value, and the fund's effective equity exposure of 63% is not far above a neutral weighting. Still, we continue to see plenty of opportunities in emerging market stocks (despite a recent rally). Emerging markets have become attractively valued after an underperformance of 9% p.a. relative to developed markets over the five years to December 2015. We have initiated exposure to gold in Global Managed funds (and Global Capital Plus), capturing some of its recent acceleration. Its large cash position is actively managed, but very conservative in terms of credit and liquidity risk.

Global Managed's short-term performance has lagged due to the fund not holding global bonds, which represent 40% of its benchmark. The fund's long-term performance is in line with the benchmark, but it has added value in all its asset building blocks over time, and performance is in line with, or better than, its average peer over all periods. It has delivered a substantial outperformance compared to the median of its peer funds over meaningful periods.

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Coronation Global Managed
Performance since inception*

** Since inception – November 2009*
*** Benchmark - 60% ACWI & 40% Barclays Global Bond*
Note: performance is net of fees in USD

Coronation Global Managed
Performance (31 July 2016) vs. local unit trusts (ZAR)

	YTD	1 year	3 years (p.a.)	5 years (p.a.)
Coronation Global Managed Fund	-5.9%	8.4%	14.6%	21.7%
Median – High equity	-6.9% *(10)	8.3% *(8)	14.8% *(7)	18.3% *(6)
Median – Flexible	-7.1% *(26)	9.0% *(23)	13.5% *(17)	18.5% *(15)

** Number of funds*

Global Managed continues to hold a reasonable exposure to alternative asset managers, which have seen share price declines in the past few months, despite (in our view) improving fundamentals. The assets under management of these companies have been growing substantially and we expect healthy distributions in coming years when performance fees are realised. The sector is neglected and undervalued amid concerns about adverse tax outcomes as a result of a populist backlash, which we believe are negated by deeply discounted share prices. Current prices ascribe little value to performance fees, which represent more than half of normal earnings. Recent earnings have been better than expected, with Blackstone seeing a sharp upward correction after releasing its results. Four of our holdings have also started buying back their shares, which can add significant value for the remaining shareholders, which will now have larger stakes in the companies.

Long-term investors with Coronation are accustomed to periods of short-term underperformance as we wait for the markets to recognise the value of mispriced assets. Our investment philosophy and process have not changed over the past two decades: We continue to focus on identifying assets that are trading at discount to their long-term value. Our investment decisions are based on our own proprietary research, involving extensive contact with management teams and our financial modelling.

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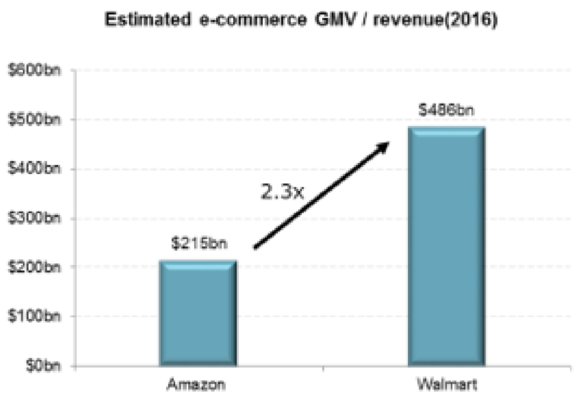
Equity-only funds

Coronation Global Equity Select, which aims to deliver sustainable alpha (outperformance) over long periods of time, was launched 18 months ago in a very difficult market environment. Its performance has gained traction this year, but alpha generation will remain lumpy and unpredictable in a volatile environment. The fund can invest in some 3 500 stocks across global indices, but we are focusing on high-quality businesses in our preferred sectors.

We continued to hold stocks that will benefit from the disruptive power of the internet. While many new digital upstarts are transforming long-established business models, we will only invest in the expected long-term winners who have strong brands and balance sheets.

Alphabet (Google) and the Swedish digital investment group Kinnevik are core holdings, along with Amazon, which we expect will overtake Walmart to become the biggest retailer in the world in the next decade. Amazon's sales are currently growing at a rate of 33% per year, compared to Walmart's 3%. Its revenue is 40% of Walmart's revenue, while its profits only represent a tenth, as Amazon continues to invest heavily in an effort to make its platform unassailable. Accordingly, the company has massive scope to normalise its margins. Due to the impact of heavy investment on its profitability, Amazon currently trades on a price earnings multiple of 96 times (on consensus one-year forward earnings). However, we believe near-term profits are far below what the business will earn in the long run. Also, Amazon has a huge cost-structure advantage due to its scale and lead in rolling out fulfilment infrastructure. We rate Amazon CEO Jeff Bezos, who still owns 18% of the business, as one of the best in the world.

Amazon versus Walmart



A relatively new addition to the portfolio is the global mattress leader Tempur Sealy. As global growth concerns increased, cyclical companies which depend on discretionary income (like Tempur Sealy) have been sold off. This has created an attractive entry point. The company has a new management team, which is focused on cost savings and production improvements following a recent merger. Operating margins have already improved and the share has seen large gains of late.

We have also added to our healthcare exposure. The sector is under pressure as healthcare costs are a contentious election issue in the US. The pharmaceutical and pharmacy sector has been sold off to unwarranted levels, creating buying opportunities. We have bought a stake in the pharmaceutical group Allergan (owner of Botox, which represents 13% of its sales) after its price fell 20% following the cancellation of a deal with Pfizer. The company is trading at a price earnings ratio of 14 times and has a solid balance sheet.

Walgreens Boots Alliance (WBA), owner of the second-largest and largest pharmacy chains in the US and UK respectively, is now one of the fund's top ten holdings. The company has a new management team with an excellent track record in operational execution. We expect the group's margins will be bulked up in coming years, as it continues to benefit from synergies as well as demographic tailwinds (ageing populations with greater medical needs). WBA is hoping to acquire its US rival Rite Aid, which could provide a boost of some 10% to the company's fair value if the transaction is approved.

We believe there is substantial value that can still be unlocked in the Global Equity Select portfolio, which is trading at an effective price earnings ratio of 14 times, primarily due to our holdings in alternative asset managers, which are mostly trading at single-digit multiples.

Coronation Global Equity Select
Top 10 holdings as at 31 July 2016

Top 10 Equity Holdings	% of Portfolio	PE (f)	Dividend Yield (f)
Apollo Global Management	4.3%	12.2x	8.0%
Alphabet	4.3%	21.1x	-
KKR	4.3%	10.3x	4.6%
Fortress Investment Group	3.6%	5.4x	13.1%
Amazon.com	3.5%	-	-
Blackstone Group	3.1%	10.2x	7.3%
American Express	3.0%	11.6x	2.0%
Walgreens	2.8%	15.9x	1.9%
Kinnevik	2.4%	-	3.6%
Charter Communications	2.4%	-	0.1%

Coronation Global Emerging Markets

While gaining developed market exposure remains paramount, we continue to believe that SA investors also need sufficient emerging market holdings. Many emerging markets present a very different set of attractive opportunities compared to SA. Some markets still offer a long runway of growth, with retail penetration of, for example, financial services (banking and insurance) still very low. The per capita consumption of consumer and capital goods continue to be a fraction of that in developed markets. Also, market leaders in attractive industries (for example, retail or banking) often only have a single-digit market share. They have large scope to quickly build additional scale, which will have a large impact on profits. We are very excited by these developments and believe valuations are still compelling.

However, passive investing in an index of emerging market holdings is perilous. An investment in the top 20 holdings of a well-diversified index like the MSCI World or Standard & Poor 500 will include a number of high-quality companies (Amazon and Google, for example) amongst it largest holdings. A similar investment in emerging market indices will result in a bias towards a number of state-owned companies (that may appear superficially cheap, but are unlikely to have shareholder-friendly policies), highly-regulated telecom companies, low-quality tech manufacturers and established conglomerates in Korea or Taiwan. To take advantage of the long-term structural growth in emerging economies, buying the market is generally a bad idea.

We believe active investing is particularly important in emerging markets, where there are big differences in management quality, disclosure, regulatory risk and the opportunity sets. This needs to be captured in the valuation of a company.

Naspers remains the largest holding, and gives the fund access to the Chinese internet and gaming giant Tencent. We continue to be positive about the Chinese internet sector, which has seen a large sell-off (e.g. JD.com halved, and is back at its 2014 IPO price) due to concerns about the local economy. While China is no longer growing at between 8% and 10% per year, growth of 5% to 6% off a larger base is still encouraging – especially compared to stalling developed markets.

The fund also holds the number two Chinese internet gaming company, Netease. China has strict restrictions on foreign gaming consoles, and it is difficult to get hold of an Xbox or PlayStation. Internet gaming is immensely popular. It's part of the Chinese culture and key to social interaction, as most children in China don't have a sibling. A successful game which is constantly innovating has a lifetime of 10 to 15 years, with players becoming very invested over long periods of time.
Baidu, which controls 70% of the Chinese search market, is another key holding. Its shares have been sold off as the market disapproved of the company's spending on speculative new ventures. This is depressing its short-term earnings. Some of its ventures will be successful, which could still add a lot to Baidu's bottom line. Management has also indicated that it may start pulling the plug on activities that are not yielding results. The company has historically maintained margins of 50% on search; currently its margins are between 12% to 15%. If spending is scaled down, these margins could recover quite quickly. The fund is also invested in the travel website C-Trip and the powerful online retailer JD.com.

Some 20% of the Coronation Global Emerging Markets Fund is invested in Brazil, that is still struggling with a recession. A number of reforms have been passed which will sow the seeds of growth in coming years. We continue to believe that holdings in the Brazilian private education operators look particularly attractive and this sector represents 8.5% of the fund. The share prices of our main holdings, Kroton (the biggest player) and Estacio (the no. 2) have seen some movement after a friendly merger was announced in June. The transaction will remove a large number of fixed costs (for example, the cost of developing a curriculum and getting the course approved) and deliver an estimated R$4bn in synergies. This will help to bolster margins. The combined entity will be four times larger than its competitor.

Elsewhere in Latin America, we are seeing pro-market administrations taking power in some countries after years of leftist rule. Significant improvements are seen in Mexico, Argentina, Colombia.

We view India as probably the most attractive emerging market, and 16.5% of the fund is held in that country. India is growing faster than China after years of underperformance. Its recent implementation of a unified tax system (across state lines) will create a single market in India for the first time: A positive for businesses. India has many great companies with years of strong earnings growth (+15%) ahead of them, but valuations are very high in most of these. We view Indian private banks (trading at 12 to 15 times earnings) as a relatively cheap way to get access to earnings growth in the country. The fund has exposure to Yes Bank, India's fifth largest private sector bank, and also to Tata Motors, which owns Land Rover and Jaguar

We are also positive on Russia, which took the pain from the steep oil price decline head on. Its fiscal situation has stabilised, inflation is back into single digits and the country is not facing a debt crisis. Companies cut spending and slashed wages to remain competitive, and are also seeing improved competitiveness thanks to a cheap currency.

We believe that – after a long period of underperformance – emerging market prices can move closer to fair values very quickly when a turning point arrives. There isn't a flood of money waiting to leave emerging markets: Many foreign investors have already exited these markets and should eventually return. The average upside on our GEM coverage list (what we think businesses are worth versus current share prices) is still north of 60%, and justifies continued exposure.

Coronation Global Emerging Markets Flexible

Top 10 Holdings as at 30 June 2016

	Country	% PF
Naspers Limited	South Africa	5.2%
Kroton Educacional Sa	Brazil	4.6%
Baidu Inc	China	4.3%
Axis Bank Limited	India	3.9%
JD.com Inc	China	3.9%
Estacio Participacoes Sa	Brazil	3.8%
Tata Motors Limited	India	3.4%
Heineken Holding	Netherlands	3.3%
Brilliance China Automotive	China	3.2%
Yes Bank Limited	India	2.7%