EXECUTIVE SUMMARY
CONVERSATIONS WITH CORONATION

SEPTEMBER 2013

KEY RISKS TO LIVING ANNUITY INVESTORS

Investors in living annuity products, currently the most popular compulsory post-retirement income option in South Africa, face three key risks: longevity risk (which is a financial planning risk), inflation risk and sequence-of-returns risk (both investment portfolio risks).

Longevity risk: Investors can insure against longevity risk by purchasing a guaranteed annuity from a life office. If however their choice is to invest in a living annuity product, financial advisors have a very important role to play in helping their clients manage this risk by:

- being conservative in their initial income drawdown rate; and
- only increasing their drawdown rates once market returns have been realised.

How conservative should investors be at the point of retirement? We believe that a good reference point is the initial income rate achievable on a guaranteed inflation-linked annuity payable for life, which is currently between 5% and 5.5% if you retire in your early 60s. You may be able to argue for a somewhat higher income if your client is invested in a living annuity product where the underlying assets in the portfolio have a higher expected rate of return (guaranteed annuities only invest income assets).

Inflation risk and sequence-of-returns risk: One of the best ways of ensuring that an investor's future income stream can keep pace with inflation is to have adequate exposure to growth assets. Too much exposure to growth assets, however, can result in short-term losses (sequence-of-returns risk). We, as Coronation, can assist with these risks by offering appropriately constructed portfolios that have the right balance of income and growth assets to achieve the dual objectives of achieving reasonable growth after inflation (over the long-term) and preserving capital (over the short-term).

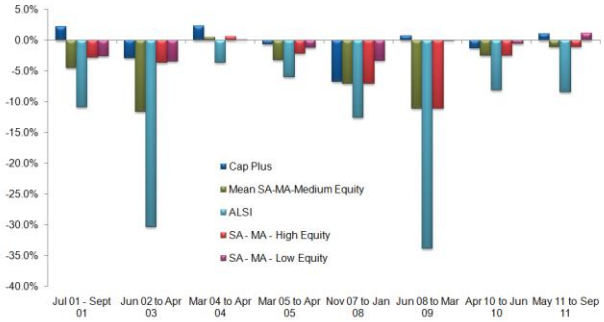
OUR APPROACH TO MANAGING CORONATION CAPITAL PLUS AND BALANCED DEFENSIVE

We offer two funds that are suitable for investors intending to draw an income from a living annuity product over an extended period of time – Capital Plus and Balanced Defensive. Both funds are managed in a measured and risk sensitive manner. We follow a bottom-up approach that assesses every instrument in terms of the upside potential and, very importantly, downside risk.

We do not change our asset allocation aggressively, instead we do so gradually. As an example, we have recently been reducing the equity exposure in both funds; not because we expect a big market correction but because when the price of an asset increases, so does the risk. Investors should therefore expect us to be reducing our equity exposure into market strength and to slowly start adding to those asset classes where the upside potential is greater.

While we cannot make money in a bear market, we aim to protect capital during such periods. We therefore believe that the true test for these funds is a brutal bear market (see graph below) and we are encouraged by the track record of Capital Plus. During the global financial crisis of 2008/9, the fund achieved a slightly positive return, which really speaks to the fact that we manage for downside risk. This however comes at a cost, as the fund will not keep up during bull markets (refer to second graph below).

Coronation Capital Plus: Bear market returns



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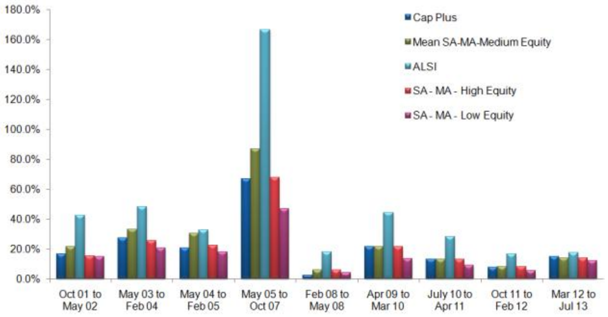
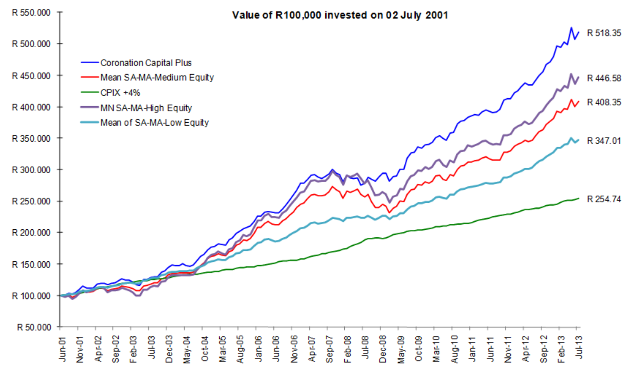
Coronation Capital Plus: Bull market returns



Source: Coronation Fund Managers
Performance quoted from Morningstar as at 31 July 2013 for a lump sum investment with income distributions reinvested.

The impact of having preserved capital during the tough times, along with the power of compounding, however becomes clear when you assess the fund's return on a cumulative basis (see graph below).

Coronation Capital Plus: Performance since launch



Source: Coronation Fund Managers
Performance quoted from Morningstar as at 31 July 2013 for a lump sum investment with income distributions reinvested.

OUR CURRENT VIEWS AND FUND POSITIONING

A year ago we summarised our key points regarding the global economy as follows:

- the world is caught in a low growth, low inflation and low interest rate trap;
- the main investment theme therefore is the search for yield;
- abnormal policies would ultimately lead to abnormal asset prices; and
- a bubble is most likely to take shape in yield-driven investments.

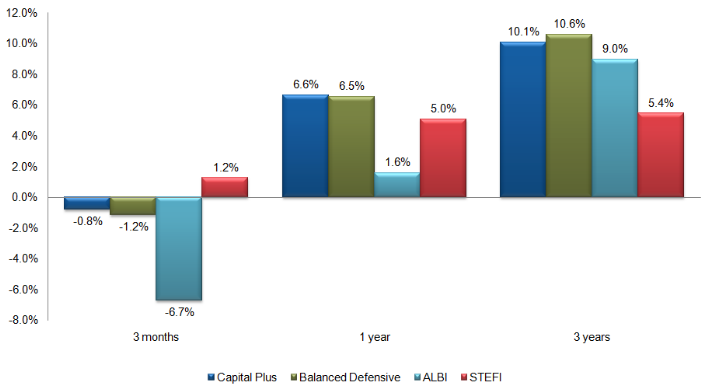
In May of this year, the search for yield theme (that has been driving yields to extreme lows over the past couple of years) came to an abrupt end. The trigger was the announcement by the US Federal Reserve (Fed) chairman Ben Bernanke that the recovery in the US was sound enough for them to consider the tapering of their aggressive quantitative easing programme. US bond yields, in response to this announcement, spiked dramatically; so did bond yields in emerging markets. In addition, the US dollar strengthened, the gold price dropped sharply and most emerging market currencies weakened.

Some investment conclusions

Against this backdrop, our defensive positioning in the income portion of our funds has paid off. We have been mindful of the potential risks in the yielding assets, and as such had no exposure to conventional government bonds. We also took very little interest rate risk as we believe that interest rates will eventually rise, and held a big weighting in inflation-linked bonds (ILBs) as we remain concerned about inflation worldwide. We also held offshore corporate bonds, preference shares and convertible bonds.

Given that the income portion of our funds does not mirror the index (as is the case with our equity and property holdings), it also acts differently during times of stress. We believe that this strategy has delivered. Over the last three months, which includes the significant sell-off in bond markets, the income portion of our funds held up significantly better than the All Bond Index (see graph below). The negative performance we did experience in this area, was largely due to our holding in ILBs, which were also impacted by the sell-off. We remain comfortable with this exposure however, as domestic inflation risks remain skewed to the upside. The more defensive positioning did not come at the cost of lower returns: over the one-year period, where income assets still performed well, our funds did significantly better than the index and better than cash. The same pattern can be seen over the three-year period.

Conservative bond and cash positions reduce downside risk



Performance of the domestic income asset carve-out of the Capital Plus and Balanced Defensive funds relative to domestic All Bond Index and local cash

We continue to believe that equities are more attractively valued than bonds. Combined with the glimmer of improved economic growth in the US, we believe that a rotation out of bond funds into equity funds could provide strong tail winds for this asset class. Within equities, we continue to favour global over domestic.

In the domestic equity market, we have been adding to our resource holdings in a limited manner as the resource sector is currently the cheapest and hence most attractive from a valuation perspective. Given that uncertainties relating to economic growth in China remain, we are not taking on too much risk in this space as yet.

The equity selection within our funds added value. Over the past year, we owned very few of the domestic consumer-facing stocks on valuation grounds. This position has been vindicated so far in 2013 with domestic retailers being among the worst performers on the JSE. The large multinationals held in our funds (British American Tobacco, Naspers, Richemont, MTN and SABMiller) have all performed very well. However, as the market continued to strengthen, we have been trimming a few of these positions, but continue to have exposure to all of them. The one multinational that has hurt our performance is Anglo American. Following a reassessment of the stock, we concluded that it was looking very cheap and have added to our position. Anglo American is now the biggest equity holding in both the Capital Plus and Balanced Defensive funds. (Please refer to our previous summary page for a detailed discussion on our investment case) We have also been adding to our platinum holdings, as we believe that most of the bad news has been priced in. Again, we have been adding to this position slowly.

HOW DID CAPITAL PLUS AND BALANCED DEFENSIVE PERFORM?

Both funds performed well relative to benchmarks and peers over the past year and longer-term periods. This has been driven by strong returns across most asset classes. If we look at the indices, domestic equities and listed property produced annualised returns of 20% and 24% respectively over the past ten years. We do not believe that this trend can continue and again caution investors to lower their future return expectations for the domestic asset classes. The one-year returns of listed property (9.4%) and bonds (1.6%) already reflect this view. Over the last couple of years, we have also been communicating our view that investors should be having sufficient exposure to offshore assets, and as is clear from the table below, the MSCI World Index expressed in rand is now running ahead of all other asset classes over the one- and three-year periods.

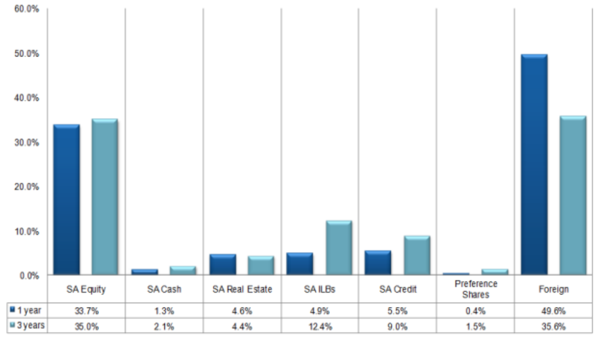
Asset class returns

	1 year	3 years	5 years	10 years
SA Equity	23.0%	16.8%	11.5%	20.1%
Bonds	1.6%	9.0%	10.2%	9.3%
Property	9.4%	19.2%	20.8%	24.2%
Cash	5.3%	5.7%	7.1%	8.1%
MSCI (ZAR)	47.9%	25.3%	11.3%	11.4%
Global Bonds (ZAR)	14.4%	12.7%	9.6%	8.3%
Capital Plus	17.4%	13.1%	13.3%	15.0%
CPI + 4%	10.4%	9.5%	9.2%	9.9%
Balanced Defensive	16.5%	13.8%	12.8%	-
STeFI + 3%	8.1%	8.4%	9.8%	-

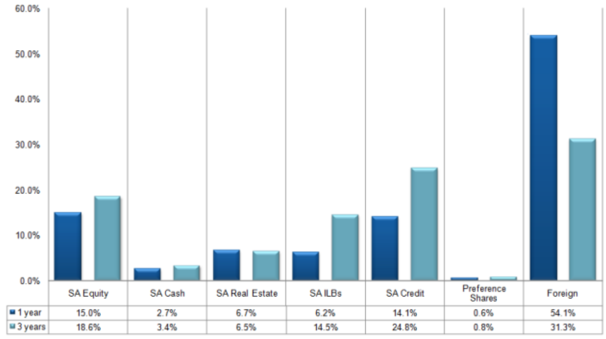
Periods ending 31 July 2013

The asset class contribution over the one and three-year periods also clearly illustrates the strong contribution to fund performance by the offshore components in both funds.

Coronation Capital Plus: Contribution to total return



Coronation Balanced Defensive: Contribution to total return



Periods ending 31 July 2013

For a more detailed discussion on the positioning of Capital Plus and Balanced Defensive, please click here to view the webcast of the full presentation.

PORTFOLIO MANAGER CHANGES

Earlier this year, we announced that Louis Stassen, head of Coronation's absolute return unit and co-manager of Capital Plus, will be relinquishing his responsibility for the local absolute funds at the end of 2013. With effect from 2014, he will assume responsibility for developing our capacity to manage developed market equities directly from Cape Town. Charles De Kock, who has achieved an excellent track record with the Coronation Balanced Defensive fund by producing high levels of outperformance with low levels of risk, will assume responsibility for both Capital Plus and Balanced Defensive together with Henk Groenewald (who has been co-managing Capital Plus with Louis for the past three years).

RETIREMENT REFORM UPDATE

During 2012, National Treasury (NT) released four technical discussion papers. The consultation process has now been concluded and the legislative process to implement the changes has commenced.

The key changes from the four papers include:

- a new tax incentive contribution programme, which will essentially move some of the tax benefits from the high net worth end of the market to the middle income market;
- the ability to access accumulated retirement savings as a lump sum for provident fund members will be phased out;
- the ability to access your pension benefits early when changing jobs or getting divorced will be removed; and
- trustees will be required to offer a default post-retirement income option to retiring fund members.

In July of this year, NT released its fifth technical discussion paper on charges in the retirement system. This paper is currently subject to public consultation. A key point to note is that this paper deals primarily with the accumulation phase of the retirement funding market.

At the heart of this paper is the question of whether the retirement provision industry is simply providing a commodity service or adding value. While NT believes that the market is too complex, too intermediated and that active management is overused, our view is that:

- the industry is healthier than what NT believes it to be;
- the debate should be around value and not just cost;
- advice adds more value than what NT perceives; and that
- some time should be allowed to pass to prevent any unintended consequences from implementing too many changes too quickly.

For a more detailed discussion on retirement reform, kindly click here to view the webcast.