Total returns

At 28 February 2018	1 mth %	3 mths %	6 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	10 yrs % p.a.	Inception % p.a. (Feb 2008)
Ralton Smaller Companies	0.74	1.95	9.82	14.55	12.26	13.43	12.02	9.01	8.74
Income return	*0.34*	*0.54*	*1.33*	*2.86*	*3.01*	*3.22*	*3.52*	3.64	*3.73*
Growth return	*0.40*	*1.42*	*8.49*	*11.70*	*9.26*	*10.20*	*8.50*	5.37	*5.01*
S&P/ASX Small Ord Accum. Index	0.03	2.67	14.58	20.81	10.81	6.22	2.65	1.10	1.47
Difference	**0.71**	**-0.72**	**-4.76**	**-6.26**	**1.46**	**7.21**	**9.37**	7.91	**7.27**

Performance review

- The S&P/ASX Small Ordinaries Accumulation Index returned 0.03% for February, with Health Care and Consumer Discretionary adding value to the index.
- The Ralton Smaller Companies portfolio returned 0.74% for the month, outperforming the benchmark by 0.71%.
- The portfolio's underweight to Consumer Discretionary was a key detractor from portfolio returns, offset by the portfolio's underweight to Information Technology and overweight to Health Care and Financials.

Performance attribution

Key contributors

Key contributors	Positioning
Nextdc Ltd	Overweight
Inghams Group	Overweight
Worley Parsons Ltd	Overweight

Nextdc Ltd (NXT, +17.02%) – delivered a very strong result well ahead of both the market and our expectations, which led to a sharp bounce in the share price. NXT is benefiting from the secular demand for data centre space as core technology processing and storage moves into the cloud. This secular shift is only in its early stages and NXT is in a prime position to be one of the key players in the domestic market. NXT has a pipeline of new centres in the early stages of opening or in the final stages of development. These centres will drive the next stage of earnings growth.

Inghams Group (ING, +10.12%) – delivered a solid result for 1H18, which then saw a positive share price reaction. Management continues to improve the operations of this previously family-run business. The industry structure is favourable with chicken being the most attractively priced form of protein and the two major domestic players continuing to win share. ING continues to find productivity enhancements through either genetics or automation at its facilities. The one area of risk relates to its small exposure to the NZ market where one of its main competitors faces an overhang of inventory which it must clear.

Worley Parsons Ltd (WOR, +6.13%) – continued its recovery after its restructuring necessitated by the collapse in the oil price a few years ago. WOR delivered a result above both the market and our expectations. Further, we saw a reinstatement of its dividend during the half, reflecting a much-improved balance sheet position. We are starting to see a turn in the capital expenditure cycle in the oil and gas industry. While it takes time to gain momentum, once it is underway it should provide WOR with a tailwind. As the industry's capacity gets absorbed, we expect to see margins continue to improve. The one overhang for the stock is the $150m of outstanding receivables with state-owned enterprises in the Middle East. We would want to see some progress on this front in 2H18.

Key detractors

Key detractors	Positioning
Cooper Energy Ltd	Overweight
Fletcher Building Ltd	Overweight
Blackmores Ltd	Overweight

Fletcher Building Ltd (FBU, -15.05%) – has had a number of issues with its construction business and was suspended from trading during the month as it sought to renegotiate its loans as one of the loan covenants was in breach. While the banks gave a waiver for the breach, the US private placement holders were still in negotiations when we decided to exit the position. It is an extraordinary situation for the company to find itself in when such a small contributor to the overall business can jeopardise the organisation. The core of the business is still in good shape, although we are late in the cycle, so there may be an opportunity to revisit the stock again once the debt position is resolved.

Cooper Energy Ltd (COE, -10.96%) – is an emerging gas producer with its key asset, Sole, currently in the development phase. The group still has wells to drill, but it is in shallow water and it has a good cash buffer. So

the only reason we can see for the pull-back is that the market had moved ahead of itself. COE still retains some uncontracted gas from this project which it will be able to sell into a very strong market. It also has another project in its development pipeline which would further enhance its earnings capability.

Blackmores Ltd (BKL, -17.31%) – delivered a rise in profit of 20% on the pcp and broadly in-line with our expectations. However, the outlook provided by management was softer than we had expected and there were some other negatives around constraints on the supply of ingredients for its vitamins and weak cash flow. The market took the negatives and sold off the stock, with the share price looking to be of very reasonable value at the current level, in our view. The longer-term demand outlook for BKL's range of products and the positioning of the company's brands remains very strong.

Portfolio changes

Key additions and material adjustments

After the market ructions in the early part of the month, we elected to deploy some of the surplus cash we have been sitting on for some time into some new opportunities for the portfolio. These positions were as follows.

Bought
Link Administration Services (LNK)
ALS Limited (ALQ)
Coca-Cola Amatil (CCL)
Super Retail (SUL)

We added a position in **Link Administration Services (LNK)** to the portfolio in February. LNK is a financial data administrator organised into three core divisions, namely Fund Administration, Corporate Markets and Information, Data and Digital Services (IDDS). LNK dominates the market for Fund Administration in the superannuation space in Australia with 42% of the total market and 70% of the outsourced market. This division has been a key driver of profit growth, fuelled by synergies from Super Partners. LNK recently completed the acquisition of Capita Asset Services (CAS) which gives it exposure to similar types of businesses in Europe and the UK and expands its offering. The CAS business (now renamed Link Asset Services) has underinvested in technology to improve its operations, so this will be an area where LNK can make improvements. Also, with the benefit of a UK and European base, LNK can start to make bolt-on acquisitions which should be accretive once the base business has been bedded down.

During the month, we acquired a position in **ALS Limited (ALQ)**, which has been benefiting from the recovery in mining exploration and from its various acquisitions in the Life Sciences area. ALS provides professional technical services in the areas of testing, measurement and inspection, supporting environmental monitoring, food and pharmaceutical quality assurance; mining and minerals exploration; commodity certification, equipment maintenance and asset care operations. We expect ALS will continue to benefit from the recovery in greenfields and brownfields mining exploration, an improvement in margins in its Life Sciences business and the deployment of part of its undergeared balance sheet on further acquisitions.

We added a position in **Coca-Cola Amatil (CCL)** during the month, and it has performed well after its inclusion in the portfolio. This was driven by the delivery of a solid result in the face of tough market conditions, resulting in the continued re-rating of the stock. CEO Alison Watkins and her team have been on a journey to transform the business after she was left with a portfolio of mispositioned products – both in terms of price and as an overall suite of products. The core Australian business had too much exposure to overpriced carbonated soft drinks (CSDs) as consumers became more health conscious. A lot of the repositioning has been done in conjunction with the Coca Cola Company (the US brand owner) to improve the product offering in Stills (i.e. water, dairy, energy drinks) and the pricing and marketing for the CSD products. While the Australian business has not yet based, much has been invested into the business which should eventually deliver a turn. The Indonesian business has also been reshaped and has improved in the face of a very tough local environment. It is likely positioned now to see the benefits of an improving macroeconomic environment for its customers.

We acquired a position in **Super Retail (SUL)** late in the month after it had fallen considerably. The fall was driven by a relatively soft 1H18 result and the acquisition of MacPac (an outdoor goods provider). While there appears to be a strategic rationale to the acquisition, the market was likely concerned about it given the fact the group has still not dealt effectively with its Rays Outdoor business. We viewed the decline in share price as providing us with a degree of downside relative to the valuation. The group has taken a number of the steps we would have expected to see to deal with the threat from Amazon as it builds its presence in Australia. As background, the group operates a number of retail brands including Super Retail (Auto), BCF (outdoor) and Rebel (sporting goods).

Key disposals and material adjustments

Sold
Fletcher Building (FBU)
Qube Logistics (QUB)

During the month we disposed of two holding from the portfolio. The first, **Fletcher Building (FBU)** is discussed above and, the second, **Qube Logistics (QUB)** was disposed of as we saw better opportunities elsewhere in the market.

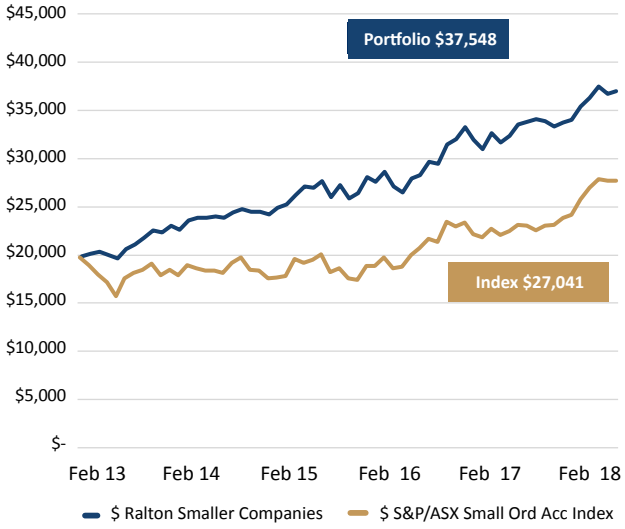
Sector allocation

GICS sector	Ralton	Index	+/-
Health Care	16.4%	7.1%	9.2%
Consumer Staples	12.5%	8.5%	4.0%
Telecommunication Services	5.2%	1.7%	3.4%
Financials	10.2%	7.9%	2.3%
Utilities	2.4%	0.5%	1.9%
Energy	8.7%	7.6%	1.1%
Information Technology	7.4%	8.7%	-1.4%
Real Estate	9.1%	10.9%	-1.8%
Industrials	5.5%	10.0%	-4.5%
Consumer Discretionary	12.4%	18.2%	-5.8%
Materials	10.4%	18.8%	-8.5%
Total	**100.0%**	**100.0%**	**0.0%**

Top 10 holdings#

Company name	ASX code
Worleyparsons Limited	WOR
Speedcast International Ltd	SDA
Tassal Group Limited	TGR
Nextdc Limited	NXT
Nufarm Limited	NUF
OFX Group Ltd	OFX
Pact Group Holdings	PGH
Steadfast Group Ltd	SDF
Tox Free Solutions	TOX
Skycity Entertainment Group Limited	SKC

Performance comparison of $20,000*



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Performance of the Ralton Wholesale Smaller Companies Model Portfolio is based on a model portfolio and is gross of investment management and administration fees, but net of transaction costs. The total return performance figures quoted are historical and do not allow the effects of income tax or inflation. Total returns assume the reinvestment of all portfolio income. Past performance is not a reliable indicator of future performance.

*The performance comparison of $20,000 over 5 years is for illustrative purposes only. Performance is calculated on a gross basis. Actual performance will vary depending on the amount of fees charged by the relevant platform that a client uses to implement the portfolio. The comparison with the S&P/ASX Small Ordinaries Accumulation Index is for comparative purposes only. Index returns do not allow for transaction, management, operational or tax costs. An index is not managed and investors cannot invest directly an in index. There is no guarantee these objectives will be met.

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