Quarterly Report
June 2014

Ralton Leaders

Winner of the 2010 Standard & Poors' Fund Awards
- Separately Managed Accounts Category

Investment Profile

A Professionally Managed Portfolio of Australian Shares

The Ralton Leaders model portfolio is a separately managed account, or SMA, actively managed by Ralton Asset Management (Ralton). SMAs are professionally managed portfolios of direct shares whereby the investor receives beneficial ownership of the underlying securities.

Investment Objective

The objective of the Leaders SMA is to provide investors with long-term capital growth and tax effective income from a portfolio of blue-chip Australian shares. The portfolio aims to deliver returns that are consistently above the S&P/ASX 100 Accumulation Index over a three to five year period.

Key Portfolio Features	
Inception	1 February 2008
Benchmark	S&P/ASX 100 Accumulation Index
Authorised Investments	Companies in the S&P/ASX 100 Index or those amongst the top 100 by size.
Number of Stocks	25-40
Cash Allocation	0% to 10%
Tracking Error	1.5% to 3.5%
Investment Horizon	At least 3 to 5 years
Ratings	

Performance

Return %	1m	3m	1yr	3yrs	5yrs	Incept*
Ralton Leaders	-1.04	2.04	17.33	11.75	12.01	5.75
Income Return	0.12	0.64	4.07	4.70	4.48	4.52
Growth Return	-1.15	1.40	13.26	7.04	7.53	1.23
S&P/ASX 100 Index	-1.47	1.13	17.65	11.14	11.63	4.43
Difference	**0.43**	**0.91**	**-0.32**	**0.60**	**0.37**	**1.32**

**Since Inception p.a., Feb 2008*

The Portfolio is designed for investors who...

- Seek long term capital growth & tax-effective income
- Expect consistent above market returns
- Have a long term investment horizon of at least 3-5 years and accept the risk of equity markets.

Portfolio Structure

No.	Company Name	ASX Code
1	Commonwealth Bank of Australia	CBA
2	ANZ Banking Group	ANZ
3	BHP Billiton Limited	BHP
4	Telstra Corporation Limited	TLS
5	Westpac Banking Corporation	WBC
6	Oil Search Limited	OSH
7	QBE Insurance Group	QBE
8	Amcor Limited	AMC
9	Aristocrat Leisure Limited	ALL
10	Brambles Limited	BXB

GICS Sector	Ralton	Index	+/-
Industrials	10.6%	6.3%	4.3%
Consumer Discretionary	5.9%	2.5%	3.4%
Health Care	7.9%	4.6%	3.3%
Energy	8.8%	6.3%	2.5%
Telecommunication Services	7.4%	5.2%	2.2%
Information Technology	1.8%	0.7%	1.1%
Materials	16.7%	16.7%	0.0%
Utilities	0.0%	1.7%	-1.7%
Property	2.7%	6.8%	-4.1%
Consumer Staples	3.4%	8.3%	-4.9%
Financials (ex-Property)	34.8%	40.9%	-6.1%
Total	100.0%	100.0%	

Quarter in Review

Performance Summary

- The S&P/ASX 300 accumulation index added 1.13% for the quarter, with Energy and Utilities the top performing sectors.
- The Ralton Leaders Model Portfolio recorded a solid gain of 2.04% for the quarter, outperforming the benchmark index by 0.91%.
- At a sector level, the portfolio's overweight exposure to both the Energy and Healthcare sectors added value, offset by our underweight exposure to Financials.

Portfolio Commentary

Quarterly Performance Attribution

Top Contributors	Positioning	Key Detractors	Positioning
ResMed Inc	Overweight	QBE Insurance Group	Overweight
Echo Entertainment	Overweight	Coca-Cola Amatil	Overweight
Oil Search Ltd	Overweight	Newcrest Mining	Not Owned

Positive Contribution

ResMed Inc. (RMD, +15.9%) was a strong contributor to the portfolio in the June quarter. The company's third quarter profit result delivered 8% growth in earnings per share (EPS) and was well received by the market. Critically, the US region, which accounts for about 55% of company sales, demonstrated an improving sales trend for both masks and breathing devices compared to recent quarters and, perhaps, the market's overall expectations. The result and management commentary strongly suggest that recent disruptions caused by changes in pricing and consolidation of service providers (known as DME's) in the US were abating and that 'business as usual' was returning. Reimbursement pressures are a constant in healthcare as government and private payors seek ways to offset the rising cost of providing services. Despite this, RMD is well placed to grow its service offering, through ongoing penetration of the patient population for sleep apnea and expanding services. RMD is expanding its clinical offering, with full launch of the Astral 150 in Europe later this year, targeting the market for invasive and non-invasive life support ventilation for both adult and paediatric patients. This launch together with new product initiatives and a likely whole new platform offering in their sleep apnea segment should, in our opinion, drive solid revenue growth and support our investment in ResMed.

Echo Entertainment (EGP, +27.6%) was also a strong contributor to portfolio performance, driven by two key factors. Firstly, the company's profit guidance for FY14, provided in June, was above market expectations. Underpinning the profit upgrade was strong revenue growth at EGP's QLD and NSW casino operations across the current half year, supported further by retention of recent cost saving initiatives. In particular, investors were reassured that EGP's main asset, Star Casino in Sydney, has finally begun to deliver consistent returns following the recent major capital refurbishment and operational initiatives. Secondly, EGP have partnered with Chow Thai Fook Enterprises (CTF) and Far East Consortium (FEC) to form the 'Destination Brisbane Consortium'. This group will tender for rights to build an integrated resort, including a casino, at the Queen's Wharf site in Brisbane. EGP are the incumbent casino operator in Brisbane, operating a fairly modest size casino in the former QLD State Treasury buildings. This partnership with two foreign companies provides EGP with both a tourism link to Asia and development experience, placing the consortium in a highly competitive position to succeed in the government controlled tender. Submissions are due by late 2014 with the QLD government targeting a decision early in 2015.

Oil Search (OSH, +15.7%) was boosted by the shipment of first gas to customers in Japan from the company's flagship PNG LNG gas plant, train 1, during May. OSH and plant operator Exxon Mobil have since confirmed that ramp up of first gas from the second LNG train is running ahead of schedule and should commence mid-year. Early commissioning means an earlier path to cash flows for all of PNG LNG's owners. For OSH the dollar amounts will be transformational, allowing scope for the company to increase dividends to shareholders and likely invest in further LNG gas trains in PNG (up to another three by 2020 are possible). OSH recently acquired a material interest in another PNG gas field, named Elk/ Antelope (or PRL15). This field, co-owned by Total and InterOil, will likely be used to support some of the additional LNG trains. The size and nature of any future LNG trains will be determined by further field (exploration) works, together with negotiations between the joint owners of Elk/Antelope and the PNG government. We expect clarification on this front across the balance of 2014.

Negative Contribution

QBE Insurance Group (QBE, -15.2%) was the largest detractor from portfolio performance. Contributing to the weakness was the ongoing strength of the Australian dollar, which of course impacts translation of US dollar profits, together with some weakening in key government bond yields, which impacts QBE's investment returns and value of its liabilities. In the short term it appears that bond investors are tempering their view of the US growth outlook following a severe winter that has weakened economic activity in the US. QBE also announced a 'strategic review'' of its US middle market business at its AGM in April. This will likely see the company sell and exit some aspects of the business in the US, and overall was not a material surprise in our view. In June, the company announced the merger of its Asia Pacific and Latin American businesses to form an emerging markets division, effective August 2014. We view this development positively, given the positive growth outlook for these regions in years to come and the need for QBE to ensure a dedicated focus.

Coca-Cola (CCL, -14.2%) also detracted from portfolio performance during the quarter, although most of the stock price fall came after we had significantly reduced the weight in the portfolio in early April. CCL has been facing substantial headwinds over the past couple of years. These related to increased competition from a Japanese controlled competitor (lacking profit discipline), de-stocking by the major supermarkets, a soft consumer environment and cost headwinds in Indonesia arising from a decline in the value of the rupiah and a rise in the minimum wage. In addition, there are rising health concerns about the level of sugar consumption (i.e. is this the next tobacco?). At the time we acquired the initial holding we were of the view a number of these headwinds would ease in CY14, and that it will be a long time before health concerns significantly dent consumption. We reduced our holding in early April after re-visiting our thesis around the timing of a recovery in a number of these areas. Later in the month, new CEO Alison Watkins surprised us with a dramatic downgrade in current year earnings expectations. We are of the view some of this is a re-basing of earnings to give the new CEO room to manoeuvre in making some structural changes in the company. At another level, there is a recognition that the competition from Schweppes, the soft domestic consumer environment and the Indonesian pressures will persist in the short-term. We are still a fan of the products CCL produces, the financial returns it has generated over a long period of time, and the growth options presented by Indonesia, and expect it will get back on the path of profit growth in coming periods. So we will continue to monitor the progress of Alison Watkins as she conducts a restructure of the operations with a view to adjusting the portfolio position further at an appropriate time.

Finally, having no holding in Newcrest Mining (NCM) detracted from relative performance across the quarter. Gold, which gained 3.3% in US dollar terms across the quarter, was the beneficiary of increased geopolitical risk, with flashpoints in both the Ukraine and Iraq. European Central Bank (ECB) easing measures also likely supported the price and the share price of gold miners in turn.

Portfolio Adjustments

During the Quarter we...

SOLD: ASX Ltd (ASX), Toll Holdings (TOL)

BOUGHT: Transpacific Industries Group (TPI)

Purchases

We added a position in Transpacific Industries (TPI) during the quarter. The stock's progress in recent times has seen the company enter the Top 100 index of Australian companies. As well as coming into the investment universe for this portfolio, the move into the top 100 was a trigger for short term share price weakness as 'Small Cap' managers were forced sellers of the stock. We are attracted to the waste industry and TPI because of the GDP type growth profile that waste streams provide. In recent years, the company has expended considerable efforts to reduce its debt and bring its balance sheet under control. Post GFC the business had required a series of equity raisings. With this process now complete and the sale of the NZ Waste business now finalized, new CEO Robert Boucher has taken the reins of a debt free business. As such TPI management can finally focus all its energies on running the business more efficiently and seeking avenues through which to grow. We expect to see revived sales strategies to acquire new customers, improving route density across their waste collection network. The new CEO has also flagged his intention to acquire, either outright or in partnership with others, ownership in landfills. By owning the landfill, TPI will be able to capture the profits across a greater portion of the waste value chain. Although the Australian east coast economy continues to face headwinds, we believe that over the long term, waste production and therefore services should grow at rates at or above GDP, and hence be supportive of our investment in TPI.

We also increased our holding in Recall Holdings (REC), noting the strong start the company has made in terms of acquisitions since the demerger from Brambles at the end of 2013. The company recently acquired US-based CitiStorage for $47.2m. Given their clean balance sheet and a quite fragmented industry, REC are well placed to grow by acquisition, building on the current storage footprint and the high degree of recurring revenue and free cash flow that the business delivers. We also recently attended a meeting with management where they provided far more insight about the moat which exists around the storage business (it is a very sticky business). As counter-intuitive as it might seem in this digital age, the demand for long-term hard storage is growing due to regulatory requirements and litigation risks.

Disposals

There were two outright stock sales for the quarter, with both ASX Ltd (ASX) and Toll Holdings (TOL) sold from the portfolio. Although Toll continues to deliver on a series of cost out initiatives, our analysis indicates that headwinds across a number of Toll's service offerings remain. In particular, domestic customers continue to seek lower cost service offerings for their transport requirements as part of their own cost saving initiatives. In addition, Toll's operations in both the Asian region and resource segment continue to face margin pressures and risk from contract renewals. On balance, we have elected to sell our position in Toll, with the proceeds invested in TPI.

The other stock sale for the quarter was ASX Ltd (ASX), with most of the proceeds used to increase the investment in Macquarie Group Limited (MQG). Whilst we still like the ASX business model, the company does face some headwinds given that volume growth for equities and derivatives continue to be subdued.

RALTON ASSET MANAGEMENT

Investment Approach

A Three Stage Investment Process

Intensive bottom-up research is the cornerstone of the entire process, supplemented by top-down economic and thematic views. The process is disciplined and consistently applied, using a number of proprietary qualitative and quantitative techniques to ensure that targeted companies have been thoroughly scrutinised. The aim is to uncover undervalued businesses. The companies that Ralton typically invests in are those with strong and reliable management, good profit and dividend growth expectations, reasonably predictable future profits and cash flows, and a very clear business model.

Stage 1: Defining the Investment Universe (Screening)

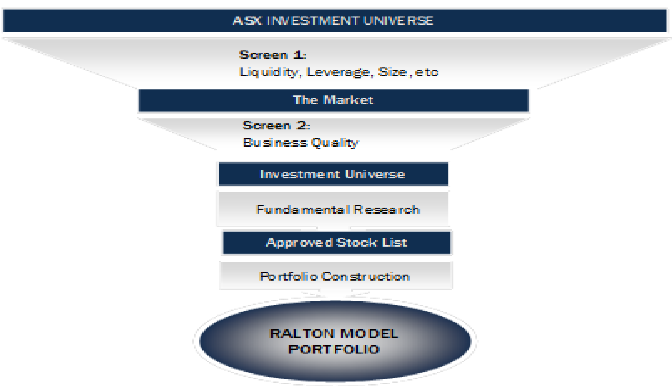
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

Stage 2: Bottom-up Fundamental Company Research

Ralton's research programme is focused on understanding the key drivers of business performance and returns, namely people, operations, products and services, and market dynamics. For companies remaining in the Investment Universe, a detailed assessment is made of executive management, interviews competitors and suppliers, reviews financials, and forms a clear view on the outlook for the company's industry.

Stage 3: Portfolio Construction

Risk management and capital preservation are key themes underlying the portfolio construction framework. With a focus on actively managing down-side portfolio risk for investors, Ralton constructs an efficiently diversified portfolio of high quality, undervalued companies, and invests for the long term (typically 3 to 5 years) in an effort to maximise after tax-returns.



About the Manager

Ralton Asset Management is part of the OC Group, a boutique investment specialist majority owned by members of its investment team and key executives.

Ralton is a Value manager with a fundamental investment approach designed to identify quality businesses trading at a considerable discount to valuation. The process is guided by three fundamental beliefs:

- Markets are not perfectly efficient and the true value of a business is not always reflected in its share price;
- Undervalued companies can be identified through detailed and intensive research; and
- Capital preservation is critical to wealth creation.

The Investment Team

Andrew Stanley *BEc, LLB, ACA, FFin, MA AppFin*
Portfolio Manager, Ralton Model Portfolios

Andrew Stanley is the lead portfolio manager for the Ralton portfolios. He is supported by a dedicated and highly experienced team of investment professionals each with an average 18 years investment experience. Andrew has been working in financial markets for more than 19 years, including the past 5 years managing the Ralton portfolios. Prior to Ralton, he was an Executive Director at UBS in Hong Kong, and over the course of his career has held senior positions with major investment institutions in Melbourne, Hong Kong, Tokyo and New York. Andrew started his career at Arthur Andersen in Melbourne.

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