Quarterly Report September 2014

RALTON ASSET MANAGEMENT

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	MORNINGSTAR ★★★★

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	BHP Billiton Limited	BHP
3	Telstra Corporation Limited	TLS
4	ANZ Banking Group	ANZ
5	National Australia Bank Limited	NAB
6	Westpac Banking Corporation	WBC
7	Amcor Limited	AMC
8	QBE Insurance Group	QBE
9	Oil Search Limited	OSH
10	Aristocrat Leisure Limited	ALL

GICS Sector	Ralton	Index	+/-
Industrials	13.6%	6.5%	7.1%
Health Care	9.3%	5.4%	4.0%
Consumer Discretionary	7.1%	3.4%	3.7%
Telecommunication Services	7.3%	5.1%	2.2%
Materials	17.4%	16.3%	1.1%
Energy	7.6%	7.0%	0.6%
Information Technology	0.0%	0.7%	-0.7%
Utilities	0.0%	2.0%	-2.0%
Property	3.1%	7.0%	-3.9%
Consumer Staples	2.9%	8.2%	-5.2%
Financials (ex-Property)	31.7%	38.4%	-6.7%
Total	100.0%	100.0%	

Performance

Return %	1m	3m	1yr	3yrs	5yrs	Incept*
Ralton Leaders	-2.67	1.26	9.23	16.90	7.86	5.72
Income Return	0.53	1.33	4.10	4.49	4.47	4.55
Growth Return	-3.20	-0.07	5.12	12.41	3.40	1.17
S&P/ASX 100 Index	-5.36	-0.72	6.25	15.54	7.19	4.14
Difference	**2.69**	**1.98**	**2.98**	**1.36**	**0.67**	**1.58**

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

Quarter in Review

Performance Summary

- The S&P/ASX 100 Accumulation Index fell heavily in September to finish the quarter down 0.72%, with Healthcare the top performing sector and Materials the weakest.

- The Ralton Leaders Model Portfolio gained 1.26% for the quarter, outperforming the benchmark index by 1.98%.

- This outperformance was driven by our overweight exposure to the Consumer Discretionary and Industrials sectors and our underweight to resource stocks within the Materials sector.

Portfolio Commentary

Quarterly Performance Attribution

Top Contributors	Positioning	Key Detractors	Positioning
Recall Holdings	Overweight	Transpacific Industries	Overweight
Aristocrat Leisure	Overweight	Oil Search	Overweight
Amcor Limited	Overweight	Macquarie Group	Overweight

Positive Contributors

Recall Holdings (REC, +17.2%) was the portfolio's top contributor for the quarter, buoyed by speculation that they may be a takeover target for US peer Iron Mountain (IRM). IRM is the number one player in the global document storage market and their acquisition of REC, the number two player, would make sense from a synergistic perspective. REC however denied that they had fielded any approach from IRM. Earlier in the quarter, REC shares were boosted by the announcement of productivity improvements across their global storage facilities. The productivity program is consistent with our view that since the demerger from Brambles, REC management has considerable scope for 'self-help' initiatives that will deliver value to shareholders.

Aristocrat Leisure (ALL, +11.0%) received a positive market response to their acquisition of US based Video Gaming Technologies (VGT) for US$1.28bn, funded by a capital raising from shareholders and an increase in debt. We believe that the acquisition makes sense and was done at a reasonably attractive price, with VGT a strong cash-producing asset. We are happy with the progress being made by the company under CEO Jamie Odell's 5-year turnaround plan. ALL have invested heavily in resources to improve the quality of their gaming offering, both in the traditional slot machine setting, and also online software. To this end, despite modest backdrop in demand growth for slot machines, the company has been gaining share in key markets.

Amcor Limited (AMC, +8.6%) added to portfolio returns following strong financial results. Cash flow was strong, margins in the key Flexibles division rose strongly year-on-year, and the dividend was higher than market estimates. The company is well positioned for solid revenue growth, having an exposure to global emerging economies and their demand for packaged goods across food, healthcare and hygiene products. Amcor highlighted a $3bn pipeline of acquisition opportunities.

Underperformers

Transpacific Industries (TPI, -19.7%) weighed on portfolio performance after the company announced that they had increased their landfill remediation provision by $189m (after tax), noting the need to spend more cash than previously planned over the next 5 years ($25-35mpa). TPI also grounded their entire waste management fleet nationally during August, following a fatal accident involving one of their vehicles in South Australia. All vehicles were required to pass a roadworthy certificate and all vehicles have subsequently returned to the road.

A weakening oil price as the US dollar strengthened contributed to weakness in PNG-focused energy company, Oil Search (OSH, - 7.8%), and detracted from portfolio performance. As discussed last quarter, the company recently shipped their 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).

Macquarie Group (MQG, -3.4%) impacted portfolio performance for the quarter, although it still outperformed many of its peers as weakness across the banking sector was significant. Whilst we like the medium term outlook for the stock, given its current valuation we are concerned about how it will perform as the US Federal Reserve ends quantitative easing. For this reason we sold the stock from the portfolio during August. This was the last of the diversified financial holdings in the portfolio.

Portfolio Adjustments

During the Quarter we...

SOLD: Computershare (CPU), Macquarie Group (MQG), Suncorp Group (SUN), Woodside Petroleum (WPL)

BOUGHT: Transurban Group (TCL)

Portfolio Additions & Material Adjustments

Transurban Group (TCL) was the only stock addition to the portfolio in the quarter. TCL own a portfolio of high quality toll roads, concentrated across the eastern seaboard of Australia. The assets are high quality, largely intra-urban roads with strong volume growth from demographic changes and essentially mandated annual fee rises for road users across the life of the asset or concession period. The combination of GDP driven volume increase in traffic load plus annual price hikes gives strong ongoing growth in free cash flow for TCL, and hence, growth in dividends to its investors. The recent acquisition of the Queensland-based QML road network appears to be a solid, long-term investment. The capital raising associated with the QML acquisition provided a depressed price at which we acquired the position.

Portfolio Disposals & Material Adjustments

We disposed of three stocks from the portfolio during the quarter after deciding to reduce our exposure to the financial sector. Firstly we disposed of our final stake in Suncorp Group (SUN), a stock we had acquired in the early stages of its turnaround. The company delivered solid FY14 results across all divisions. However, the insurance pricing cycle has started to peak and it is not clear how much of the planned costs savings will need to be reinvested to protect market share in this environment. Also the market had, in our opinion, started to price in the special dividends as permanent.

The position in Computershare (CPU) was also sold after a review of our investment thesis post the company reporting its financial year 2014 results. We also disposed of our holding in Macquarie Group (MQG), as noted above.

Outside of financial stocks, we also sold our position in Woodside Petroleum (WPL). Australia's largest oil and gas company has been a pioneer in the Australian LNG market and now boasts two large cash flow producing assets in the Pluto LNG asset and NW Shelf asset. Despite these achievements and being cash rich - supporting current dividend yield payouts - WPL is lacking in growth projects. As such, we currently prefer our other holdings in the Energy sector, being Oil Search (OSH) and Origin Energy (ORG).

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)

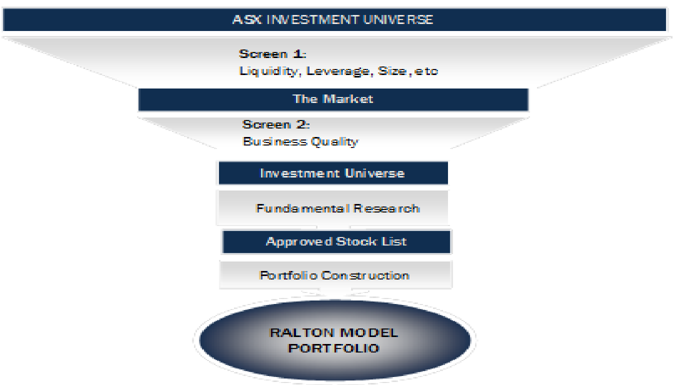
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

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.

Roger Walling *BOptom, MBB* Portfolio Manager, Ralton Model Portfolios

Stephen Evans *B Com, ACA*, Portfolio Manager

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For Further Information

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