Monthly Report August 2014

Ralton Australian Shares

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

Investment Profile

A Professionally Managed Portfolio of Australian Shares

The Ralton Australian Shares 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 Ralton Australian Shares SMA is to to provide investors with long-term capital growth and some tax effective income from a concentrated portfolio of Australian shares. The Portfolio aims to deliver a return superior to that of the market over periods of five years or longer while at the same time seeking to minimise the risk of investment capital loss.

Key Portfolio Features	
Inception	1 February 2008
Benchmark	S&P/ASX 300 Accumulation Index
Authorised Investments	Companies in the S&P/ASX 300 Index or those amongst the top 300 by size.
Number of Stocks	20-35
Cash Allocation	0% to 10%
Tracking Error	3% to 6%
Investment Horizon	At least 5 years
Ratings	MORNINGSTAR ★★★★; LONSEC Investment Grade SMA; van Eyk

Performance

Return %	1m	3m	1yr	3yrs	5yrs	Incept*
Ralton Aust Shares	1.18	3.12	14.86	16.20	10.58	6.65
Income Return	0.73	0.91	4.02	4.56	4.46	4.49
Growth Return	0.45	2.20	10.84	11.64	6.12	2.16
S&P/ASX 300 Accum. Index	0.64	3.56	14.15	14.00	9.07	4.39
Difference	**0.54**	**-0.44**	**0.71**	**2.20**	**1.51**	**2.26**

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

The Portfolio is designed for investors who

- Seek long term capital growth & some tax-effective income
- Expect consistent above market returns
- Have a long term investment horizon of at least five 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	National Australia Bank	NAB
6	Oil Search Limited	OSH
7	Westpac Banking Corporation	WBC
8	Origin Energy Limited	ORG
9	Amcor Limited	AMC
10	QBE Insurance Group Limited	QBE

GICS Sector	Ralton	Index	+/-
Industrials	14.4%	7.6%	6.8%
Consumer Discretionary	8.2%	5.5%	2.7%
Energy	8.7%	6.8%	1.9%
Health Care	6.6%	5.1%	1.5%
Telecommunication Services	6.2%	5.5%	0.7%
Materials	16.8%	16.6%	0.2%
Information Technology	0.0%	0.9%	-0.9%
Utilities	0.0%	1.9%	-1.9%
Property	4.6%	7.1%	-2.5%
Consumer Staples	4.7%	7.4%	-2.8%
Financials (ex-Property)	29.9%	35.6%	-5.7%
Total	100.0%	100.0%	

Month in Review

Performance Summary

- The S&P/ASX 300 accumulation index gained 0.64% in August, with Energy and Healthcare the top performing sectors.
- The Ralton Australian Shares Model Portfolio gained 1.18%, outperforming the benchmark index by 0.54%.
- The portfolio's outperformance was driven by our overweight exposure to the Energy sector together with our underweight to resource stocks within the Materials sector. These positives were somewhat tempered by stock specific losses within the Industrial sector.

Portfolio Commentary

Monthly Performance Attribution

Top Contributors	Positioning	Key Detractors	Positioning
Amcor Limited	Overweight	Recall Holdings	Overweight
Orora Limited	Overweight	Transpacific Industries	Overweight
Origin Energy	Overweight	Aristocrat Leisure	Overweight

Positive Contributors

Company reporting season for the end of Financial Year 2014 was a key driver of share performance in August. Amcor Limited (AMC, +9.5%) added to portfolio returns following strong financial results, headlined by a 25% increase in net profits. Cash flow was strong, margins in the key Flexibles division rose strongly year-on-year, and the dividend was commensurately higher than market estimates. Going forward the company is well positioned for solid revenue growth, with 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. We expect that acquisitions will continue to be a key part of AMC's growth strategy and make incremental contributions to shareholder returns.

Amcor spin-off Orora Limited (ORA, +12.2%) was the portfolio's next best contributor. The company's maiden profit result was well received as key financial targets were achieved. ORA is benefitting from various cost savings following a multi-year capital investment program and operational improvement initiatives started by its former parent. The new B9 pulp mill in Botany continues to 'ramp-up' production and management confirmed that B9's multi-year commissioning is proceeding broadly in line with expectations. Successful ramp-up to full production is key to ORA achieving the cost savings targets that are baked into the market's profit expectations. ORA's US packaging operations also reported strong results, with the company highlighting the acquisition of a small operation in Texas.

Origin Energy (ORG, +10.2%) gained ground in August, with three factors driving the share price gains. Firstly, Origin elected to cancel a proposed equity raising to fund the recent Karoon Gas (Poseidon field) acquisition, and raise the capital for this transaction via the European Hybrid markets instead. Secondly, ORG's reported results for FY14 exceeded market expectations, with strong free cash flow, the key division reporting stabilised market conditions, and an improved outlook for the coming year. Finally, construction of the QLD LNG plant (APLNG) is proceeding to plan. Recent developments include the plant (both upstream and downstream) reaching 75% completion and contractor Bechtel signing a new EBA with local unions, alleviating concerns that industrial action could derail the project's budget and schedule. Once the plant is producing gas, the cash flow impact on ORG will be transformational. CEO Grant King was at pains to highlight that ORG intends using the APLNG cash flows to substantially increase dividends to shareholders.

Underperformers

Transpacific Industries (TPI, -15.6%) 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 $125-175m 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 before returning to the road. We believe this decision was the correct one. All vehicles have subsequently returned to the road. We continue to have confidence the relatively new CEO, Bob Boucher, will be able to deliver improved results over the next few years.

Recall Holdings (REC, -7.4%) detracted from returns after announcing the company's profit guidance for the coming year would not match market expectations. The key issue was management's statement that costs would remain elevated in the coming financial year, whereas after REC's June announcement of a Facility Optimisation Program, i.e. productivity improvements across their global storage facilities, the market had built up high expectations of near term cost savings. We note that since the demerger from Brambles in late 2013 management have been very clear that costs, particularly on the sales side, needed to grow, to continue to drive revenue growth. This is being done after an extended period where costs were cut across this business by BXB, to "dress" Recall up for sale to private equity. Our view is that the cost savings REC have targeted are achievable and will be delivered in the medium term. We have confidence that management initiatives, including selective M&A, new contract wins (eg HSBC), and the Facility Optimization Program, will deliver stable profit growth for investors.

Aristocrat Leisure (ALL, -3.0%) also gave up some of their recent gains and as a result weighed on portfolio returns. After announcing the acquisition of US-based Video Gaming Technologies (VGT) for US$1.28bn in July, news flow in August was relatively light, although they did announce an agreement to divest the European-focused Lotteries business to Playtech for AUD$15mn. The business is small and non-core within Aristocrat. The main game for investors remains market share gains in the key Australian and US markets for ALL's machines. Recent merger activity in this sector may help ALL in this regard, as competitors are distracted by the internal machinations that usually follow mergers.

Portfolio Adjustments

During the Month we...

SOLD: Macquarie Group (MQG), Suncorp Group (SUN)

BOUGHT:

Portfolio Additions & Material Adjustments

There were no new stock additions to the portfolio in August

Portfolio Disposals & Material Adjustments

We disposed of two stocks from the portfolio during August as part of a process of reducing our exposure to the financial sector. Firstly we disposed of our final stake in Suncorp which 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.

We also disposed of our holding in Macquarie Group (MQG). Whilst we like the medium term stay with the stock, we are concerned about how it will perform as the US Federal Reserve ends qualitative easing, given its current valuation. This was the last of our diversified financial holdings in the portfolio.

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)

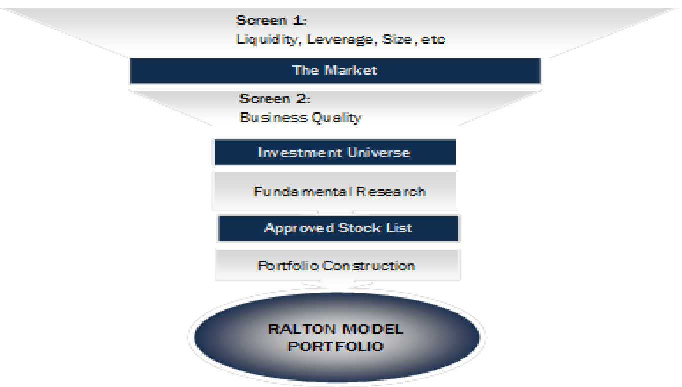
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

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.

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

Stephen Evans *B Com, ACA*, Portfolio Manager

Stephen Sedgman Chairman OC Funds Risk Mgt Committee

Robert Frost *B Com, LLB*, Portfolio Manager

Robert Calnon *B Com, ACA*, Portfolio Manager, Equities Dealer

For Further Information

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