Monthly Report October 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	4.23	2.70	8.80	16.69	9.80	6.72
Income Return	0.00	1.28	4.02	4.27	4.33	4.46
Growth Return	4.23	1.42	4.78	12.42	5.47	2.26
S&P/ASX 300 Accum. Index	4.27	-0.70	5.97	13.30	7.91	4.07
Difference	**-0.04**	**3.40**	**2.83**	**3.39**	**1.88**	**2.65**

**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	Telstra Corporation Limited	TLS
4	BHP Billiton Limited	BHP
5	National Australia Bank	NAB
6	Westpac Banking Corporation	WBC
7	Amcor Limited	AMC
8	Incitec Pivot Limited	IPL
9	Oil Search Limited	OSH
10	Origin Energy Limited	ORG

GICS Sector	Ralton	Index	+/-
Industrials	13.3%	7.5%	5.8%
Consumer Discretionary	9.8%	5.6%	4.2%
Health Care	8.3%	5.4%	2.9%
Materials	17.6%	15.5%	2.1%
Energy	7.4%	6.4%	1.0%
Telecommunication Services	5.9%	5.6%	0.3%
Utilities	1.2%	1.8%	-0.7%
Information Technology	0.0%	1.0%	-1.0%
Consumer Staples	4.3%	7.7%	-3.3%
Property	3.2%	7.4%	-4.2%
Financials (ex-Property)	29.0%	36.0%	-6.9%
Total	100.0%	100.0%	

Month in Review

Performance Summary

- The S&P/ASX 300 Accumulation Index recorded a strong gain of 4.27% for October, with Financials and Telecommunications the top performing sectors
- The Ralton Australian Shares Model Portfolio also posted strong gains, adding 4.23% for the month, performing essentially in line with the benchmark
- On a sector basis, the portfolio's overweight position in the Consumer Discretionary sector was offset by our overweight position in the Energy sector

Portfolio Commentary

Monthly Performance Attribution

Top Contributors	Positioning	Key Detractors	Positioning
Aristocrat Leisure	Overweight	Oil Search	Overweight
Transpacific Industries	Overweight	Origin Energy	Overweight
Lend Lease	Overweight	iSelect	Overweight

Positive Contributors

Aristocrat Leisure (ALL, +9.8%) continued its recent strong run and was a positive contributor to portfolio performance for the month. Industry feedback and sales data has confirmed that ALL is gaining share with their products in key markets. This confirms for us that the heavy investment in talent and content over recent years is bearing fruit. In addition, ALL's online or 'app' based software is gaining users, recording good growth in 'MAU' or monthly average users, lead by 'Product Madness' and 'Heart of Madness.' Also, Aristocrat confirmed the early settlement of their acquisition of US based Video Gaming Technologies (VGT), having completed all necessary regulatory requirements nearly six months earlier than expected.

Transpacific Industries (TPI, +10.4%) performed strongly, rebounding from recent share price weakness. At the company's AGM, CEO Robert Boucher confirmed that trading conditions in their key markets remain challenging which was not unexpected. On a positive note, TPI noted that their entire waste management fleet has returned to the road following the voluntary grounding for safety checks in August. Equally positive was the progress being made with the new sales program introduced by the CEO which is key to why we believe TPI can continue to grow earnings despite challenging economic conditions. This program is in pilot stages in various markets but shortly will be rolled out across the Cleanaway network. We consider this a key cultural change initiative, which will, in turn, drive future company profitability.

Lend Lease Group (LLC, +9.2%) was boosted in October by contract wins and the positive outlook presented at their investor day. LLC, together with their partners, confirmed that they had reached financial close on the $5.3billion Public Private Partnership (PPP) for construction of the East West Link in Melbourne. Our view is that LLC will be a strong beneficiary of what appears to be an impending infrastructure investment phase (perhaps not a boom!) in Australia, particularly along the East Coast. Illustrative of this theme, LLC's engineering backlog stands at $5.3bn, up from $2.1bn in June this year. At the investor day, LLC were also keen to highlight the opportunities that lie ahead in the United States, particularly in the areas of healthcare and urban regeneration where LLC has significant expertise.

Underperformers

Our overweight position in Energy stocks detracted from portfolio returns in October. The oil price has fallen some 25% since mid-year, triggered by increased supplies (mainly from the US) and negligible demand growth from the global economy. Oil demand growth rates are falling in key emerging market oil consumers such as China, as economic growth slows. Typically when the oil price stages a significant decline in a short space of time, OPEC responds by cutting production (often mainly by key producer Saudi Arabia). However this has not yet happened, suggesting that the Saudis are comfortable with the lower oil price.

The weakening oil price was a contributor to the share price softness in Oil Search (OSH, -3.3%). OSH performed slightly better than the energy sector as a whole, which declined by 3.6% over the month. OSH held a strategy day in October where they highlighted the outlook for future LNG plants in Papua New Guinea and the proposed use of free cash flow. This confirmed our understanding of the approach management is planning to adopt.

Shares in Origin Energy (ORG, -4.7%) were also impacted by the falling oil price this month. ORG also held an investor day, at Gladstone where they showed the progress at the APLNG site. Construction of the project's upstream (gas production and pipelines) and downstream (LNG manufacturing) facilities is now more than 80% complete. ORG have maintained their target for first LNG production by mid 2015 with both of the LNG 'trains' operational by the end of financial year 2016.

iSelect Limited (ISU, -3.2%) also underperformed the strong market and detracted from portfolio returns.

During the month ISU's co-founder and Executive Chairman, Damien Waller, announced his intention to resign as Executive Chairman of ISU, effective December 2014. Waller intends to remain on the ISU Board, however a new independent Chairman will be sought. CEO Alex Stevens will also be appointed to the Board of Directors as part of these changes. We believe that this change is positive and continues efforts by ISU to rebuild investor confidence in the company's governance structure following a poorly received IPO in 2013.

Portfolio Adjustments

During the Month we...

SOLD:

BOUGHT: Echo Entertainment Group (EGP), Energy Developments (ENE)

Portfolio Additions & Material Adjustments

Two new stocks were added to the portfolio during the month, namely Echo Entertainment (EGP) and Energy Developments (ENE).

EGP's new management, namely CEO Matt Bekier and his team, have begun to deliver on key targets. The improved return on the massive investment in the Star Casino in Sydney has been achieved by improvements in marketing, the loyalty program and service offerings. We believe that this turnaround is yet to mature, and hence, our decision to build a position in EGP. A recent trading update at the company's AGM confirmed strong revenue trends for the main gaming floor and VIP customers at the Star and at EGP's smaller Queensland operations.

We also purchased a small position in Energy Developments (ENE) which provides internationally low greenhouse gas emissions energy and remote energy. ENE was subject to an attempted privitisation by a private equity investor. It only ended up with partial control. Since then ENE has been transformed with the older problematic projects cleaned out and new growth options introduced. The attraction today is the reasonably predictable cash flows that will be delivered from a series of long-life, contracted energy assets. The company will likely have opportunities to add to its asset base. In time, we expect the private equity investor, who remains a significant shareholder, to sell down further and this will improve liquidity further.

Portfolio Disposals & Material Adjustments

There were no outright sales for the portfolio in October, however we did take some profits in Recall Holdings (REC) following the stock's recent share price performance. The share price has re-rated significantly since the Brambles demerger, buoyed in our opinion by investors' better understanding of the business, together with a series of operational improvements by management. Recently, the share price rose on speculation that REC 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.

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)

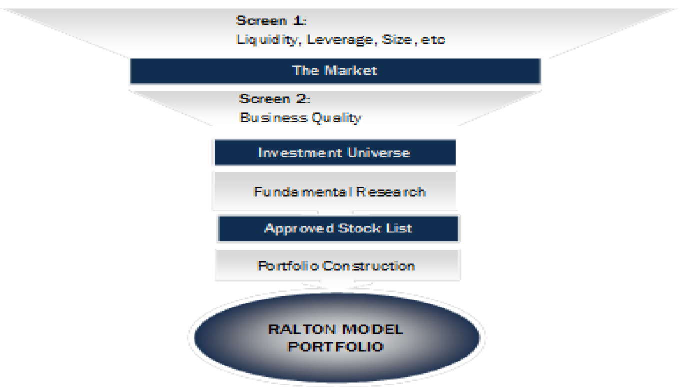
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

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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