Ralton Smaller Companies

Monthly Report
July 2015

Investment Profile

A Professionally Managed Portfolio of Australian Shares

The Ralton Smaller Companies 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 Smaller Companies SMA is to provide investors with long-term capital growth and some tax effective income from a concentrated portfolio of smaller capitalisation ASX listed 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 Small Ordinaries Accumulation Index
Authorised Investments	ASX listed companies that are not included in the S&P/ASX 50 Index
Number of Stocks	25-40
Cash Allocation	0% to 15%
Tracking Error	5% to 9% per annum
Investment Horizon	At least 5 years
Ratings	MORNINGSTAR ★★★★ / Approved Lonsec Research

Performance

Return %	1m	3m	1yr	3yrs	5yrs	Incept*
Ralton Smaller Companies	4.93	0.97	11.65	19.09	14.25	7.41
Income Return	*0.00*	*0.25*	*3.09*	*3.56*	*3.71*	*3.76*
Growth Return	*4.93*	*0.72*	*8.55*	*15.53*	*10.54*	*3.66*
S&P/ASX Small Ords Acc Index	1.56	-4.13	-2.77	3.05	0.63	-2.71
Difference	**3.37**	**5.10**	**14.42**	**16.03**	**13.61**	**10.13**

*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	Super Retail Group Limited	SUL
2	Ardent Leisure Group	AAD
3	Sky Network Television Limited	SKT
4	Aristocrat Leisure Limited	ALL
5	Macquarie Atlas Roads Limited	MQA
6	Pact Group Holdings Limited	PGH
7	iSelect Limited	ISU
8	Fisher & Paykel Healthcare Corporation	FPH
9	Energy Developments Limited	ENE
10	Tassal Group Limited	TGR

GICS Sector	Ralton	Index	+/-
Consumer Discretionary	38.7%	22.4%	16.3%
Consumer Staples	8.3%	3.4%	4.9%
Utilities	3.6%	0.7%	2.9%
Health Care	11.9%	9.1%	2.9%
Materials	14.3%	12.9%	1.4%
Energy	6.3%	5.5%	0.7%
Information Technology	2.0%	5.5%	-3.5%
Industrials	12.0%	15.7%	-3.7%
Financials (ex-Property)	3.0%	7.5%	-4.5%
Telecommunication Services	0.0%	4.9%	-4.9%
Property	0.0%	12.5%	-12.5%
Total	100.0%	100.0%	

Month in Review

Performance Summary

- The S&P/ASX Small Ordinaries Accumulation Index added 1.56% for July, with Healthcare and Financials the top performing sectors.
- The Ralton Smaller Companies Portfolio added 4.93%, outperforming the benchmark by 3.37% for the month.
- Our overweight position in Consumer Staples and Consumer Discretionary stocks added value to the portfolio, as did our underweight exposure to the Materials sector, principally resource stocks.

Portfolio Commentary

Monthly Performance Attribution

Top Contributors	Positioning	Key Detractors	Positioning
Energy Developments	Overweight	Transpacific Industries	Overweight
iSelect Limited	Overweight	Independence Group	Overweight
Blackmores Limited	Overweight	Pact Group	Overweight

Positive Contributors

Energy Developments (ENE, +8.2%) was boosted by the agreed takeover by the DUET Group (DUE) for $1.67b, equivalent to $8.00 per share in cash. Like most takeovers, as investors we have mixed feelings in this regard. The short-term benefit is clear, however, we felt ENE's assets were attractive and hence the loss of this investment option is a negative over the medium term. The small- and mid-cap segment of the market has, in recent times, seen multiple new stocks come to market as IPOs and hence, at least we are seeing some quality names join the small-cap index.

iSelect (ISU, +22%) rose strongly after it announced the repayment of a loan from NIA (owner of health.com.au). This loan has been a cause for concern to the market for some time. In a three-way deal, Geelong-based private health insurance company, GMHBA acquired the health.com.au business, essentially paying a little over $40m for the insurance clients of NIA. NIA in turn, used these monies toward repayment of the loan from ISU. For ISU, even though the $42m fell slightly short of the value of the loan, it removed a key overhang from the stock. Importantly, GMHBA, will continue to market health.com.au product via ISU and will also add their main brand to the iSelect product offering. In this sense, it's a double win for ISU as they've been repaid and have expanded their current health insurance offering. ISU will soon hold approximately $100m in net cash and we expect will use these monies toward a share buyback. We expect to hear more about capital management and dividends at the full-year result.

Blackmores Limited (BKL, +17.6%) rose again during July, although with the valuation pushing higher we have continued to trim the stock. The strength of BKL's brands and growth options in Asia continue to underpin the long-term outlook.

Underperformers

Waste services company, Transpacific Industries (TPI, -7.8%), underperformed the market and weighed on portfolio returns. Recent years have been quite disruptive for TPI, with the business undergoing management change, asset sales and substantial organizational change. We remain optimistic on the outlook for the transformation of the business over the next few years. In particular, a revamped sales model should drive improved asset utilisation, and therefore drive profit growth. In July, TPI appointed Vik Bansal to the position of CEO. Mr Bansal has most recently headed Valmont Industries in the US, however he has considerable experience in corporate Australia. We expect to hear more about his plans for the company with the full-year results in August.

Base metals mining company, Independence Group (IGO, -9.5%), also weighed on portfolio returns. IGO is in the process of merging with Sirius Resources (SIR) (a nickel-focused mining company) whose key asset is the 'Nova-Bollinger' nickel discovery in Western Australia. We have a positive view on SIR and believe the acquisition by IGO to be positive. In the meantime, weakness in base metal prices, in particular for gold, is weighing on the IGO share price.

Packaging and manufacturing specialist, Pact Group (PGH, -3.4%), gave up some of its recent gains in July, although in the absence of any material news flow. The company is set to report full-year profits in August. As the last financial update was somewhat marred by reduced profit due to the large movement in the Australian dollar and commodity prices late in 2014, we will be looking for a more stable report this period. The group will benefit from the acquisition of SULO this half.

Portfolio Adjustments

During the Month we...

SOLD: iiNet Limited (IIN)

BOUGHT: *Nil*

Portfolio Additions & Material Adjustments

There were no new stock additions to the portfolio in July.

Portfolio Disposals & Material Adjustments

There was only one outright sale as we exited the last of our position in Telco, iiNet (IIN), one of the portfolio's long-held positions. Although the acquisition of iiNet by TPG Telecom (TPM) is still subject to ACCC approval, the deal has been approved by shareholders and hence we sold the stock on market, effectively accepting the TPG offer, though not wanting to receive TPM shares.

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)

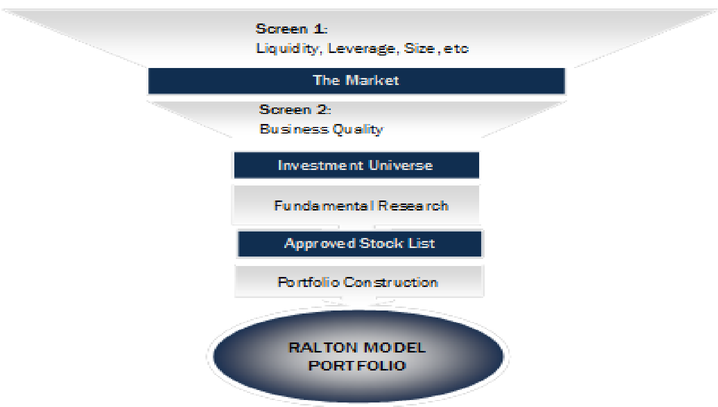
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

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 partnered with Copia Investment Partners, an administration and distribution specialist providing a range of tailored services to each of our leading boutique investment partners.

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*
Head of Australian Equities, 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 24 years, including the past 7 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

Roger Walling is responsible for stock coverage of several industry sectors and assists with the portfolio management process. He has over 12 years of direct funds management experience, including the past 7 years managing the Ralton portfolios. Previous to Ralton, Roger was a shareholder and employee of Cinnabar Equities, a Global Healthcare Fund. In his role as a Senior Analyst, he had sub-sector and stock investment decision responsibility. Prior to his career in financial markets, Roger practiced as an Optometrist.

For Further Information

Financial advisers seeking additional information can contact Ralton Adviser Services at:

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