# Ralton High Yield Australian Shares

## Monthly Report
## August 2015

RALTON
ASSET MANAGEMENT

## Investment profile

*A professionally managed portfolio of Australian shares*

The Ralton High Yield 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 High Yield Australian Shares SMA is to provide investors with consistent, tax-efficient and growing cash dividend yield, and long-term capital growth. The portfolio aims to deliver a return superior to that of the market over periods of five years or longer and an above-market yield.

| 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 among the top 300 by size |
| **Number of stocks** | 20-35 |
| **Cash allocation** | 0% to 10% |
| **Tracking Error** | 2% to 5% |
| **Investment horizon** | At least 5 years |
| **Ratings** | MORNINGSTAR ★★★★ Approved Lonsec Research |

## Performance

| Return % | 1m | 3m | 1yr | 3yrs | 5yrs | Incept* |
|---|---|---|---|---|---|---|
| **Ralton High Yield** | -6.36 | -6.35 | 7.37 | 16.75 | 12.68 | 7.38 |
| *Income return* | *0.68* | *0.83* | *4.21* | *4.83* | *4.99* | *4.98* |
| *Growth return* | *-7.04* | *-7.18* | *3.16* | *11.92* | *7.69* | *2.40* |
| S&P/ASX 300 Acc. Index | -7.70 | -8.83 | -3.23 | 10.95 | 7.91 | 3.35 |
| **Difference** | **1.34** | **2.48** | **10.60** | **5.80** | **4.76** | **4.03** |

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

**The portfolio is designed for investors who...**

- Seek an above-market, tax-efficient cash dividend yield and long-term capital growth.
- 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 | National Australia Bank Limited | NAB |
| 2 | Commonwealth Bank of Australia | CBA |
| 3 | Westpac Banking Corporation | WBC |
| 4 | Woodside Petroleum Limited | WPL |
| 5 | ANZ Banking Group Limited | ANZ |
| 6 | Incitec Pivot Limited | IPL |
| 7 | Woolworths Limited | WOW |
| 8 | BHP Billiton Limited | BHP |
| 9 | QBE Insurance Group Limited | QBE |
| 10 | CSL Limited | CSL |

| GICS sector | Ralton | Index | +/- |
|---|---|---|---|
| Consumer Discretionary | 15.3% | 4.6% | 10.8% |
| Health Care | 9.0% | 6.5% | 2.6% |
| Materials | 16.3% | 14.4% | 1.9% |
| Energy | 6.1% | 4.5% | 1.6% |
| Industrials | 8.7% | 7.6% | 1.1% |
| Consumer Staples | 7.0% | 6.9% | 0.1% |
| Utilities | 2.1% | 2.3% | -0.2% |
| Information Technology | 0.0% | 1.0% | -1.0% |
| Financials (ex-Property) | 33.7% | 38.5% | -4.8% |
| Telecommunication Services | 0.0% | 5.7% | -5.7% |
| Property | 1.7% | 8.2% | -6.5% |
| Total | 100% | 100% | |

## Monthly in review

### Performance summary

- The S&P/ASX 300 Accumulation Index fell 7.70% for the month of August. All sectors recorded a negative return with Energy and Information Technology recording the largest percentage falls.
- The Ralton High Yield Model Portfolio fell 6.36% for the month, outperforming the benchmark by 1.34%.
- Our overweight position in Industrials and Consumer Discretionary stocks added value, offset to some degree by stock selection within the Consumer Staples sector.

### Portfolio commentary

## Monthly performance attribution

| Top contributors | Positioning | Key detractors | Positioning |
|---|---|---|---|
| Asciano Limited | Overweight | Sky Network Television | Overweight |
| Ardent Leisure Group | Overweight | Sky City Entertainment | Overweight |
| Macquarie Atlas Roads | Overweight | Coca-Cola Amatil | Overweight |

**Positive contributors**

August was one of the most tumultuous periods we have seen in the Australian market for many years. The market had fallen back to the level it last saw in December 2014. Ralton had been concerned about the level the market was trading at for some time and had cash / cash equivalents (i.e. takeovers pending) equivalent to levels comfortably greater than 10% in each of its portfolios.

Confirmation of a takeover bid from Brookfield Infrastructure Partners (BIP) saw Asciano Limited (AIO, +4.4%) gain ground in a weak market. The final bid of $9.15 has been recommended by the AIO board and comprises cash of $6.94, together with shares or scrip in the US listed BIP, equivalent to A$2.21 per share at the time of the offer. Ahead of deal closure, AIO is aiming to pay a special dividend of up to $0.90, fully franked. The cash offer will be reduced by the value of the special dividend, whose attraction, of course, is the additional franking credit that will be provided to investors.

Ardent Leisure (AAD, +1.2%) rose following solid, 5% profit growth for the FY15 year. Ongoing progress from the US-based Main Event big box entertainment rollout saw profits rise 85% for this division. Perhaps more pleasing was the improved results from the Australian gyms (or healthcare division) in the second half of the year (poor results from this division in February this year had been our catalyst to enter the stock, following the share price fall). Although profits for the full year ended up down 17%, management has been able to improve key operating trends for net membership growth and profit trends for those gyms that have been rapidly converted to the 24/7 model.

Shares in Macquarie Atlas Roads (MQA, 0.0%) were flat in a negative market and hence outperformed. MQA's key asset, the French toll road continues to deliver modest profit growth driven by traffic growth, price increases and cost savings. At a group level, MQA continues to simplify its debt structure and amortise its debt, and therein interest paid, which overall should allow for growth in dividend payments going forward.

**Underperformers**

Two of our mid-cap New Zealand focused stocks weighed on portfolio returns for the period. Firstly, pay TV operator Sky Network Television (SKT, -18.6%) was sold down on concerns of a flat profit outlook in coming years. SKT is the dominant pay TV provider in NZ and is a strong and stable business. Despite this, we recognise the competition for consumers' entertainment dollar is intensifying. Although noting the recent negative trends in eyeballs and marketing dollars in the largest pay TV market, the US, we tend to believe the industry will endure, although in NZ we note the outlook for profit growth in the short term is muted as competition continues to nip at SKT's heels.

Despite growing profits at near 9%, casino operator, Sky City Entertainment (SKC, -12.8%), also detracted from portfolio returns. The healthy profit growth of the group masked a poor result for the Adelaide casino, including visitor numbers for the partially refurbished Adelaide casino being down year on year and below market expectations. Given the ongoing disruption to the casino and surrounds, such an outcome is not altogether surprising, although expectations of better results for this period had been building. SKC continues to progress its development opportunities in both Adelaide, where additional shopping and car park facilities will be built, and also the flagship Auckland casino, where SKC is commencing a major expansion project.

Coca-Cola Amatil (CCL, -9.5%) also underperformed for the period and detracted from portfolio performance for August. CCL's half-year profit results were in line with our expectations. Although year-on-year profit growth was largely flat, the results demonstrated stability in profits and volumes of key products – a critical juncture given recent downward trends have been reversed. CCL is part way through a multi-year transformation and we expect there will be ups and downs along the way. We are attracted to the solid and sustainable dividend (given the strong free cash flow, near-term decline in capex and the recapitalisation of its Indonesian operations) and the turnaround of the business being put in place by Alison Watkins (Managing Director).

## Portfolio adjustments

### During the month we...

**SOLD:** *Nil*

**BOUGHT:** Sonic Healthcare Limited (SHL) *increased*

**Portfolio additions**

Share price weakness saw us increase our holding in Sonic Healthcare (SHL). FY15 profit results were reasonable, although Australian pathology operations had a weak result, following government cuts to the funding of Vitamin D tests last year. The company, however, appears upbeat on the outlook for FY16, where acquisitions, the ramp-up in tender wins from the UK and improving US market for pathology testing, has seen the company provide earnings guidance for 20% growth in EBITDA in FY16. We like the overall stability of SHL's global business and were happy to add it back to the portfolio.

**Portfolio disposals**

There were no stock sales from the portfolio during the month.

# 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)

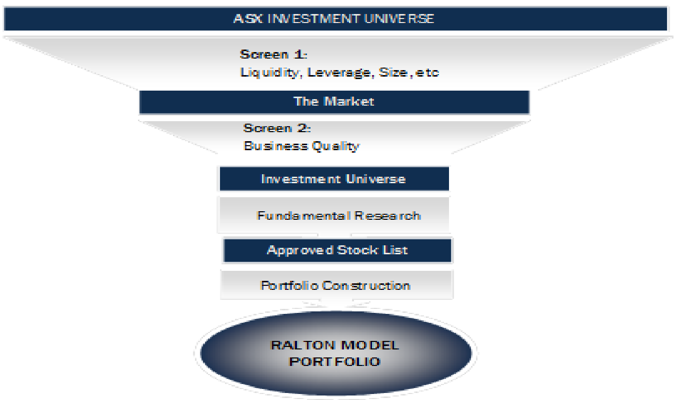
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

### 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 seven 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 seven 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.

## More information

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