Total returns

At 30 June 2017	1 mth %	3 mths %	6 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	Inception % p.a. (Feb 2008)
Ralton Australian Shares	-0.78	0.16	5.68	18.92	11.40	15.92	11.78	7.80
Income return	*0.06*	*0.45*	*1.77*	*3.66*	*3.64*	*3.91*	*4.14*	*4.29*
Growth return	*-0.84*	*-0.28*	*3.91*	*15.25*	*7.77*	*12.01*	*7.63*	*3.51*
S&P/ASX 300 Accum. Index	0.22	-1.57	3.07	13.82	6.64	11.63	8.79	4.63
Difference	**-1.00**	**1.73**	**2.61**	**5.10**	**4.77**	**4.29**	**2.99**	**3.17**

Performance review

- The S&P/ASX 300 Accumulation Index lost ground in the June quarter, falling 1.57%. Strength in Industrials and Healthcare was not enough to offset weakness in other sectors, principally Financials and Telecommunications.
- For the quarter, the Ralton Australian Shares portfolio returned 0.16%, outperforming the benchmark by 1.73%.
- During the period, the portfolio benefited from being overweight Consumer Discretionary and stock selection within Materials, offset to some degree by our underweight to Health Care.

Performance attribution

Key contributors

Key contributors	Positioning
Aristocrat Leisure Limited	Overweight
Boral Limited	Overweight
Evolution Mining	Overweight

Aristocrat Leisure (ALL, +25.5%) – continued its strong rise, gaining a further 25% for the June quarter. ALL's half-year profit results were warmly received by investors. Highlights came from nearly every business segment, with North America, Digital and International Class III gaming results all above expectations. Market share gains were consistent with industry feedback that ALL's current product suite is being well received by both venue owners and end users alike. For Digital, ALL continues to add users and grow daily user revenue, with market analysts now expecting earnings of $160m for the full year from a business which was only established a few years ago after the acquisition of a fledging player in the space for approximately US$20m. The new CEO, Trevor Croker, has continued the group's commitment to strong product investment. This R&D spend continues to support ALL's core business and also supports a movement into adjacent categories such as the new Class II and Class III Stepper games scheduled for release in the US in 2H17.

Boral Limited (BLD, +19.0%) – shares in BLD added value in the June quarter as investors continued to focus on the fundamentals of the US-based Headwaters acquisition. Boral received US regulatory approval for the transaction and formally closed the deal in early May. As we emphasised at the time of the announcement in November last year, the acquisition of Headwaters is consistent with the group's strategy of expanding its presence in the US to gain more exposure to the US housing cycle. With the transaction now having passed all regulatory hurdles, Headwaters' and BLD's existing US operations will account for 45% of BLD's profits. The housing cycle has recovered slowly post GFC but sits well below previous mid-cycle levels, creating potential for significant improvement in demand for Boral's services. This should prove favourable to Boral, combined with its exposure to infrastructure via its FlyAsh business, a key input in concrete products. Cyclical strength could well see US profits account for greater than 50% of total company profits in the near term.

Evolution Mining (EVN, +14.8%) – shares in gold miner, EVN, added value to the portfolio, despite the gold price remaining largely flat across the quarter. A recent site tour of EVN's Ernest Henry asset highlighted the quality of the asset and the opportunity for extensions to its mine life. The mine output contains material copper levels, which means after adjusting for copper credits, the 'all-in sustaining cost' per ounce of gold produced is negative US$114. EVN has a strong capital position and has low cost mines within the first and second quartile of global production costs. The falling Australian dollar has been beneficial to Australian gold miners as gold is sold in US dollars while the bulk of costs are Australian-dollar denominated. We expect EVN to participate in further industry consolidation as it arises.

Key detractors

Key detractors	Positioning
Coca-Cola Amatil	Overweight
QBE Insurance Group	Overweight
Vicinity Centres	Overweight

Coca-Cola Amatil (CCL, -14.7%) – a profit downgrade at CCL's AGM driven by weakness in its core Australian beverage division saw CCL's shares underperform for the period. CCL management called out short-term challenges in its branded water products from private label competition, together with increased price competition in the soft drink (CSD) segment. Pressure from Pepsi has limited the ability of CCL to increase prices to compensate for modest cost increases in inputs such as sugar and aluminum, placing pressure on CCL's margins. Given the progress to date with CCL's turnaround under CEO Watkins, these developments were somewhat frustrating. While we continue to monitor the competitive environment, we expect CCL can offset the broader structural pressures within the CSD segment via cost savings and growth in new branded products (stills/non-CSD) and a recovery in Indonesia. Outside of Australian beverages, CCL's other divisions remain largely in line with expectations. CCL is part way through a share buyback and remains in a strong phase of cash generation, factors we feel will continue to support the stock.

QBE Insurance Group (QBE, -8.4%) – issued a profit warning in June, citing significantly higher claims activity in its Emerging Markets division. QBE experienced a higher frequency of medium-sized claims in Asia, together with the impact of both weather and legacy portfolios in Latin America. Our QBE investment has proved a frustrating turnaround over the years with a number of false starts. The latest update continues this pattern as it follows a clean FY16 result in February that we felt had been a material step toward rebuilding investor confidence. QBE's main divisions, namely America, Europe and Australia, continue to perform in line with expectations. Investment returns are expected to deliver toward the top of the previously guided range. These positive factors support our thesis that QBE's efforts to streamline and simplify its operations have delivered benefits. QBE has made major strides in improving the quality of its capital position and reducing the risk associated with its insurance book. Going forward we expect an upturn in the insurance rate cycle to be a key driver for the stock, noting early signs of improvements in the important US market. Rising premiums should provide a buffer against events that QBE recently experienced in its Emerging Markets segment.

Vicinity Centres (VCX) – we added a position in the retail REIT, VCX, during the quarter. Vicinity owns multiple retail properties across Australia, although is perhaps best known for its ownership of Chadstone – a retail mega world with an emphasis on high-end fashion, located in Melbourne's south east. Shares in many of the retail-exposed REITs have been weaker since late last year, with global bond yields rising and heightened concerns about the impact of Amazon's Australian entry on an already muted retail sector. These concerns provided an opportunity to acquire the shares below their current book value. With the shares drifting lower subsequent to our purchase, VCX was a net detractor from overall performance for the quarter. While there may be downside to rental levels in the future, we believe the share price weakness has been overdone. Tenant leases are typically long dated and will allow for a change in tenant mix across time as Amazon and others force traditional retailers to adapt and change. We expect the quality of VCX's overall portfolio and focus on rental growth to support the shares and maintain its strong dividend yield. There is also an opportunity for a new CEO to divest the lower quality centres which may become more challenged in a world of growing online sales.

Portfolio changes

Key additions and material adjustments

We added several new stocks to the portfolio in the June quarter.

Bought
Lend Lease (LLC)
Pact Group (PGH)
Viva Energy REIT (VVR)
IOOF Holdings (IFL)
Tassal Group (TGR)
Vicinity Centres (VCX)

Lend Lease (LLC) – we bought an initial position in LLC during May, increasing the portfolio's exposure to the Australian east coast infrastructure theme. As was evident in the recent Federal Budget, governments are intent on boosting infrastructure as a means of simultaneously driving economic growth, productivity and voter services. Lend Lease recently restructured its infrastructure team and aims to deliver $4-5bn in annual revenues from this division. This would nearly double current revenues, with LLC seeking a commensurate improvement in margins. We retain a positive outlook toward LLC's other divisions, including US and UK construction and property funds management. LLC's domestic apartment division has likely peaked for this cycle. Pleasingly, LLC's mid to high-end apartment product has served the company well, with strong demand and no material evidence to date of defaults on settlement.

Pact Group (PGH) – we added PGH back into the portfolio following a pull-back in the share price. Pact is a packaging and manufacturing company with multiple manufacturing plants across Australia, New Zealand and Asia, producing a broad range of simple and specialised packaging products for clients that are largely in the food and consumer industries. PGH has dominant market share in its industry segments, where typically there are few competitors of scale. If you look in your fridge, you are highly likely to find a milk, yoghurt or orange juice package manufactured by PGH. Under CEO, Malcolm Bundey, PGH has been expanding its product offering, winning contracts and continuing to make bolt-on acquisitions. Bundey brings considerable international experience to PGH and is overseeing a productivity drive across its manufacturing footprint. PGH reported volume softness in April reflecting a weak economy and some impact from the timing of Easter holidays, triggering a share price pull-back and an opportunity for the portfolio to re-enter this name.

Viva Energy REIT (VVR) – we further increased our exposure to the A-REIT segment with the purchase of VVR for the portfolio. VVR is a long WALE business with exposure to Shell service stations. The REIT owns 400-plus petrol stations across Australia, predominantly branded Coles Express or Shell. The combination of its long-term stable leases with built-in annual growth, plus the capacity to make accretive acquisitions, provides a vehicle with an attractive growing yield and moderate earnings growth.

We added diversified wealth manager **IOOF Holdings (IFL)** to the portfolio during the quarter. IFL generates organic growth through the flow of investor funds into the various phases of the investment cycle. IFL has been very successful as a major consolidator in the wealth management space, where its integration skills allow it to retain the core value of its acquired businesses while stamping out unnecessary costs. Having consolidated multiple platforms, IFL is now targeting an improved service offering to financial advisers and clients. IOOF is particularly focused on the flexibility, or 'open architecture', of its investment platforms which allows advisers to personalise investment services rather than being restricted to in-house product offers. We like IOOF's focus on the customer which differentiates it from the big banks and other large financial institutions. IFL's recent investor day sought to highlight this focus together with the evolution of technology and client communication that underpin its offering.

Tassal Group (TGR) – we bought a position in salmon producer, Tassal Group, a major player in an industry with high barriers to entry. Key drivers for Tassal are volume growth, pricing and cost reductions through operational scale. Salmon demand growth in Australia is solid and has been for many years, driven by healthy eating trends and premium food consumption. TGR shares have been weighed down by a recent capital raise. TGR raised $100m via a capital raise from investors in March, and will use the proceeds to buy more equipment, increase its inventory of fish and stake out future lease opportunities. This bodes well for future growth in salmon sales and suggests a positive industry outlook. TGR has realised it was pulling fish out of the water to satisfy retail supply contracts and fill the shelves of the supermarkets, however the economics of fish farming suggest if the fish were left in the water, TGR would be able to farm bigger fish and yields would improve. Although TGR has had issues with a lease in Macquarie Harbour, it follows good environmental and fish husbandry practices and is well credentialed with third party accreditation, certification and sustainability ranking. TGR has behaved appropriately and, critically, maintained its social licence to operate. Statements by Tasmania's EPA and the recent approval of TGR's waste capture system in Macquarie Harbour support this view. We continue to monitor these developments as ESG considerations are critical to our investment thesis.

Key disposals and material adjustments

Outright stock sales for the quarter are highlighted below.

Sold
AGL Energy Limited (AGL)
Speedcast International (SDA)
Steadfast Group (SDF)
Independence Group (IGO)

Shares in **AGL Energy Limited (AGL)** re-rated considerably in recent months as our thesis around rising electricity prices and the cash-flow benefits that follow to AGL have unfolded. However, we are cognisant this theme may have run its course. The 'forward curve' for electricity prices rose considerably in recent months based on expectations of a tight market for electricity and may well have peaked. The sharp rise in power prices over the past couple of years has benefited AGL and other power generators whose cost of production is somewhat fixed. On top of regulatory risks from politicians keen to shield voters from rising power bills, we have seen a myriad of supply responses over recent months across the spectrum of solar, gas, pipelines, wind farms, battery storage and more. With a peak in pricing likely and AGL trading around fair value, we elected to take profits on this name.

Speedcast International (SDA) – following an eventful 2016 for SDA, including a large-scale merger and headwinds in end markets such as the energy segment, the recent share price recovery gave us an opportunity to exit our position. We harbour some concerns in relation to SDA's integration capability, particularly regarding its accounting and other back-office systems. The acquired businesses and operations are spread across the globe given the business operates remote telecommunication services, adding further complexity to the task. We will look to revisit the investment if such concerns can be overcome.

We also exited our successful investment in **Steadfast Group (SDF)** during May. SDF shares rallied strongly in recent periods, reflecting expectations of rising premiums in the Australian SME insurance market. Our research indicates the cycle for SME pricing is now turning, driven by a lack of profitability in a number of key lines for insurers. The market has now factored in a substantial amount of recovery in insurance premiums. With the stock trading around fair value, we elected to sell our holding.

Finally, we reduced our mining exposure with the sale of base metals producer **Independence Group (IGO).** IGO's most valuable mine is the Nova-Bollinger nickel mine in WA. Nova-Bollinger is a first-class nickel asset and production costs are expected to be in the bottom quartile of global producers. Despite recent teething issues as the mine heads toward full commercial production, we expect management is largely on top of the issues and that FY18 should be a positive year for mine operation and production. Despite progress at the mine, nickel supply concerns and excess inventories in the nickel market continue to weigh heavily on the stock. Our expectations had been that various production shutdowns, including mine closures in the Philippines and export bans in Indonesia would ease the global inventory glut and prices should begin to rise. Recent weakening of these measures in both countries, including allowable selective exports from Indonesia, have suggested nickel pricing softness may continue in the coming periods. On this basis, we elected to exit our holding in IGO, however the quality of Nova's core assets remains and should our confidence around the fundamentals of the nickel market improve, we would look to revisit the name.

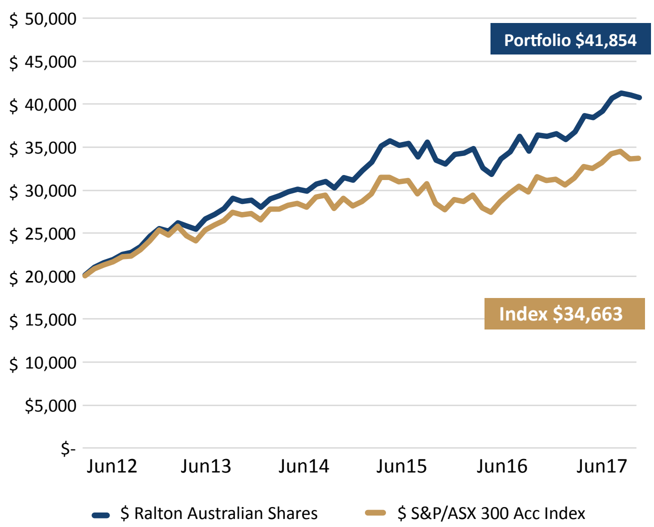
Sector allocation

GICS sector	Ralton	Index	+/-
Consumer Discretionary	10.7%	5.2%	5.5%
Energy	7.2%	4.1%	3.1%
Information Technology	3.8%	1.5%	2.3%
Materials	18.3%	16.0%	2.3%
Consumer Staples	9.0%	7.1%	1.9%
Telecommunication Services	3.4%	3.8%	-0.3%
Health Care	5.8%	7.5%	-1.6%
Utilities	0.0%	2.3%	-2.3%
Industrials	4.4%	7.4%	-3.1%
Real Estate	4.6%	8.3%	-3.7%
Financials	32.8%	36.9%	-4.1%
Total	**100.0%**	**100.0%**	**0.0%**

Top 10 holdings#

Company name	ASX code
Commonwealth Bank of Australia	CBA
ANZ Banking Group Limited	ANZ
BHP Billiton Limited	BHP
Westpac Banking Corp	WBC
Aristocrat Leisure Limited	ALL
Woolworths Limited	WOW
QBE Insurance Group Limited	QBE
Computershare Ltd	CPU
Boral Limited	BLD
Telstra Corporation	TLS

Performance comparison of $20,000*



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*The performance comparison of $20,000 over 5 years is for illustrative purposes only. Performance is calculated on a gross basis. Actual performance will vary depending on the amount of fees charged by the relevant platform that a client uses to implement the portfolio. The comparison with the S&P/ASX 300 Accumulation Index is for comparative purposes only. Index returns do not allow for transaction, management, operational or tax costs. An index is not managed and investors cannot invest directly an in index. There is no guarantee these objectives will be met.

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