

## 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 Leaders	-0.18	-0.46	5.49	16.01	9.71	14.35	10.76	6.99
Income return	0.12	0.57	1.97	3.85	3.93	4.09	4.31	4.51
Growth return	-0.30	-1.03	3.51	12.17	5.79	10.26	6.46	2.48
S&P/ASX 100 Accum. Index	0.03	-1.70	3.28	14.62	6.60	12.15	9.23	5.11
Difference	-0.21	1.24	2.21	1.39	3.11	2.19	1.54	1.88

## Performance review

- The S&P/ASX 100 Accumulation Index was down 1.70% for the quarter. Losses in Financials and Telecommunications were the key negatives, offset to some degree by positive contributions from Industrials and Health Care.
- The Ralton Leaders portfolio returned -0.46% for the period, outperforming the benchmark by 1.24%.
- For the quarter the portfolio benefitted from stock selection within Materials, our overweight position in Consumer Discretionary, and our underweight to Financials (principally banks).

## Performance attribution

### Key contributors

Key contributors	Positioning
Aristocrat Leisure	Overweight
Boral Limited	Overweight
IOOF Holdings	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 fledgling 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.

**IOOF Holdings (IFL, +14.9%)** – diversified wealth manager IOOF was buoyed by the prospect of material fund inflows into its investment platforms ahead of the government's regulatory superannuation cap. IFL generates organic growth through the flow of investor funds into the various phases of the investment cycle where it now has extensive representation. 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.

### Key detractors

Key detractors	Positioning
Coca-Cola Amatil	Overweight
CSL Limited	Underweight
QBE Insurance Group	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.

**CSL Ltd (CSL, +10.1%)** had a noteworthy June quarter for two reasons. Firstly, CSL acquired a majority stake in Chinese plasma fractionator, Wuhan Zhong Yuan Rui De Biological Products. The US\$352m acquisition is modest in terms of CSL's market cap, but marks the first move by a Western plasma producer into China's direct blood fractionation market. CSL has a good exposure to China already, with approximately one third of its Albumin already sold in China. The growth opportunity is huge, although we expect CSL to proceed slowly, cognisant of the regulatory nuances and other considerations that come from operating in China. Secondly, we saw CSL's Haegarda, a new treatment option for Hereditary AngioEdema (HAE) approved by the US FDA. HAE is a rare condition, meaning CSL's product will receive a very high sales price on a per person basis. This was an important and expected approval for CSL, though we note that Shire's competing product, with a superior dose profile, is likely to be approved and on market in the next year or so. Although CSL's share price move was positive for investor returns, our portfolio holding was below the benchmark and as such, CSL was a net detractor in terms of portfolio attribution.

**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.

## Portfolio changes

### Key additions and material adjustments

Bought
Evolution Mining (EVN)
Macquarie Atlas Roads (MQA)
Healthscope Limited (HSO)
Lend Lease (LLC)
Vicinity Centres (VCX)

We added **Evolution Mining (EVN)** to the portfolio as a gold exposure, replacing **Newcrest Mining (NCM)** post the recent mine damage at its Cadia operations in NSW (discussed below). EVN has a strong capital position and a portfolio of low-cost mines in the first and second quartile of global production costs. Australian gold miners have benefited in recent times from the falling Australian dollar which increases the value of gold sales. With costs across the whole mining sector falling as miners seek large productivity improvements, higher gold prices have been highly favourable to the gold names. We expect EVN to participate in further industry consolidation as it arises.

We added a position in **Macquarie Atlas Roads (MQA)** to the portfolio, with the stock having recently entered the top 100 index. MQA is a fund manager whose two key assets are ownership stakes in major toll road networks. MQA's French Toll Road, APRR, is more integral to the French economy than the Transurban (TCL) assets in Australia. MQA recently moved to 100% ownership in the Dulles Greenway (DG) in Washington, Virginia. MQA's corporate structure and assets have been steadily cleaned up in recent years, driving greater investor transparency and steady growth in distributions. The debt structure is understandable and the level of gearing is steadily decreasing. Steady growth in traffic volumes and tolls drives modest top line growth across the APRR toll road network. Combined with progressive debt reduction and a shift toward lower interest rates, this has driven very solid growth in earnings and distribution growth

for shareholders. The Dulles Greenway structure is also simplifying and is expected to begin cash distributions in 2019. As a result, solid growth in investor dividends is expected for several years.

**Healthscope Limited (HSO)** – We added Australia’s number two hospital operator to the portfolio in June. The stock was relisted via IPO in mid 2014. The share price rallied circa 50% at its peak before recently reverting toward the IPO price, and we now view the valuation as more interesting. Recent concerns included the exit of long standing CEO Rob Cooke and a slow-down in hospital admissions during calendar year 2016 which coincided with HSO bringing more bed capacity onto the market. Broader economic driven affordability concerns for private health insurance (PHI) also weighed on the stock. We expect this to cap PHI participation in years to come, although expect that the core of HSO’s patients, the 50 plus demographic, will attempt to maintain PHI to ensure access to preferred hospitals and surgeons. On this basis, and assuming that HSO can grow admissions around 2-3% per annum, we see HSO as reasonable value over the medium term.

**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.

**Vicinity Centres (VCX)** – we added a position in the retail REIT, VCX, during the period. Vicinity owns multiple retail properties or shopping centres 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 concerns about the impact of Amazon’s Australian entry on what has been a muted retail sector. These concerns provided an opportunity to acquire the shares below their current asset value. While there is likely 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 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.

#### **Key disposals and material adjustments**

Sold
AGL Energy Limited (AGL)
Newcrest Mining (NCM)
Spark Infrastructure (SKI)

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.

**Newcrest Mining (NCM)** – seismic activity at Newcrest’s underground Cadia mine in April caused considerable damage to both mine equipment and possibly mine structure and was the trigger for us to exit our position. Gold production guidance for the current year was understandably reduced. In a subsequent announcement following the initial incident, NCM estimated that parts of the mine will be unable to resume gold production for up to 10 weeks. Understandably, NCM remains uncertain as to the true extent of damage and the time and expense necessary to restore both safety and mining to appropriate levels. History tells us that such incidents often take longer to resolve than first envisaged, involve higher-than-expected costs to fix and reduce mine output for a significant period. The incident also limits the ability of NCM to plan and execute on Cadia expansion plans at the mine which, if done properly, would be a key driver of NCM shares.

**Spark Infrastructure (SKI)** – electricity network operator SKI’s share price reached our valuation, prompting us to sell our holding. At the time of sale, SKI was trading at a

material premium to its regulated asset backing (RAB). At the time of acquisition, we felt that SKI had some optionality around future cash realization and upside to distribution payments, however this too appeared to be reflected in the price.

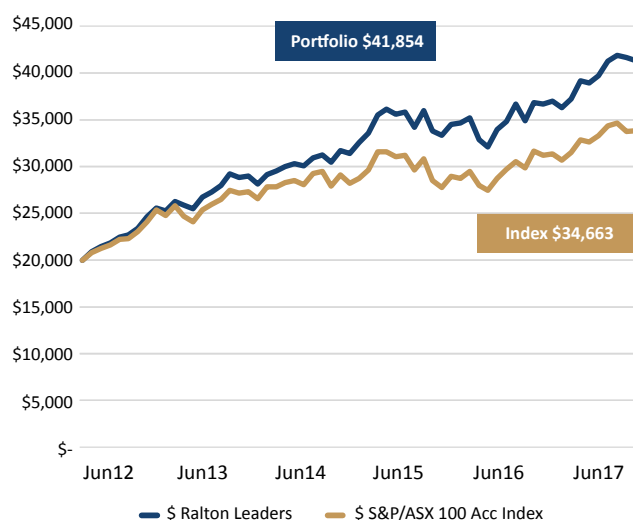
## Sector allocation

GICS sector	Ralton	Index	+/-
Consumer Staples	11.5%	6.8%	4.7%
Energy	6.7%	3.9%	2.8%
Consumer Discretionary	5.9%	3.4%	2.5%
Information Technology	3.1%	1.0%	2.1%
Telecommunication Services	3.9%	3.9%	0.0%
Materials	15.4%	16.0%	-0.6%
Health Care	6.8%	7.6%	-0.8%
Industrials	5.4%	7.2%	-1.8%
Utilities	0.0%	2.5%	-2.5%
Financials	37.1%	40.0%	-2.9%
Real Estate	4.1%	7.6%	-3.5%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>0.0%</b>

## Top 10 holdings<sup>#</sup>

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

## Performance comparison of \$20,000\*



## CONTACT COPIA

1800 442 129 | [clientservices@copiapartners.com.au](mailto:clientservices@copiapartners.com.au) | [copiapartners.com.au](http://copiapartners.com.au)



<b>John Clothier</b>	General Manager, Distribution	0408 488 549   <a href="mailto:jclothier@copiapartners.com.au">jclothier@copiapartners.com.au</a>
<b>Adam Tweedale</b>	State Manager, Southern Region	0425 804 727   <a href="mailto:atweedale@copiapartners.com.au">atweedale@copiapartners.com.au</a>
<b>Angela Vincent</b>	State Manager, Northern Region	0477 347 260   <a href="mailto:avincent@copiapartners.com.au">avincent@copiapartners.com.au</a>
<b>Sean Paul McGoldrick</b>	Account Manager, Northern Region	0421 050 370   <a href="mailto:spmgoldrick@copiapartners.com.au">spmgoldrick@copiapartners.com.au</a>
<b>Iain Mason</b>	Director, Institutional Business	0412 137 424   <a href="mailto:imason@copiapartners.com.au">imason@copiapartners.com.au</a>
<b>Jacinta King</b>	Business Development Associate	0413 962 922   <a href="mailto:jking@copiapartners.com.au">jking@copiapartners.com.au</a>

Performance of the Ralton Wholesale Leaders Model Portfolio is based on a model portfolio and is gross of investment management and administration fees, but net of transaction costs. The total return performance figures quoted are historical and do not allow the effects of income tax or inflation. Total returns assume the reinvestment of all portfolio income. Past performance is not a reliable indicator of future performance.

\*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 100 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 in an index. There is no guarantee these objectives will be met.

#Portfolio holdings may not be representative of current or future recommendations for the portfolio. The securities listed may not represent all of the recommended portfolio's holdings. Future recommended portfolio holdings may not be profitable.

This document is for general information only and does not take into account the specific investment objectives, financial situation or particular needs of any specific reader. As such, before acting on any information contained in this document, readers should consider whether the information is suitable for their needs. This may involve seeking advice from a qualified financial adviser. Ralton Asset Management (AFSL 298210, ABN 45 114 924 382) (Ralton) is the provider of the Ralton Wholesale Leaders Model Portfolio. To subscribe, contact Copia Investment Partners Ltd (AFSL 229316, ABN 22 092 872 056) (Copia) by calling 1800 442 129 or email [clientservices@copiapartners.com.au](mailto:clientservices@copiapartners.com.au). Any opinions or recommendations contained in this document are subject to change without notice. Ralton and Copia are under no obligation to update or keep information contained in this document current.