

## Total returns

At 30 June 2019	1 mth %	3 mths %	6 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	10 yrs % p.a.	Inception % p.a. (Mar 2008)
Ralton Leaders	2.74	6.51	14.85	7.76	11.75	9.70	12.99	10.85	7.46
Income return	0.15	0.90	2.69	5.04	4.45	4.27	4.30	4.40	4.59
Growth return	2.59	5.61	12.15	2.72	7.30	5.43	8.69	6.45	2.87
S&P/ASX 100 Accum. Index	3.97	8.57	20.21	12.63	13.10	8.86	12.21	10.24	6.34
Difference	-1.23	-2.06	-5.37	-4.87	-1.34	0.84	0.79	0.61	1.11

## Performance review

- The S&P/ASX 100 Accumulation Index returned 8.57% for the June quarter, with Financials and Materials the top performing sectors and Information Technology and Energy the weakest performers for the period.
- The Ralton Leaders portfolio returned 6.51% for the quarter, underperforming the benchmark by 2.06%.
- For the June quarter, being underweight Consumer Discretionary and overweight Materials added relative value to the portfolio. The portfolio's overweight to Information Technology and Financials were the key detractors from portfolio returns.

## Performance attribution

### Key contributors

Key contributors	Positioning
Aristocrat Leisure	Overweight
Amcor	Overweight
Star Entertainment Group	Overweight

**Aristocrat Leisure (ALL, +25.34%)** – delivered a strong 1H19 result which saw a restoration of investor confidence in management during the quarter. The key drivers of the result were continued strength in the core slots business, with growth in adjacent markets starting to gain traction. The market was looking for improvement in ALL's Digital business and the better than expected result saw renewed strength in the share price. Digital earnings have been a key area for concern and the 1H19 result revealed that recent investment is driving growth. Further, margins look to be sustainably higher than assumed. The result confirmed positive indications from surveys released during the prior quarter showing the company's gaming machine products continue to be industry leading and continue to take share from over-gear competitors. Despite the recent strong performance, at the current valuation we feel the market is discounting the strong earnings outlook supported by multiple growth options within ALL's core slot operations, expansion into adjacent markets, and continued momentum in its Digital businesses. The US economic backdrop remains supportive as low interest rates and tax cuts continue to support investment and consumer spending.

**Amcor (AMC, +5.20%)** - the global packaging company, outperformed the market during the quarter as it completed the merger with Bemis. The merged entity began trading from mid-June with the principal listing in the US and a secondary listing in Australia. The acquisition of Bemis is a strategically significant move by AMC as it gives the group a diversified global footprint across Flexible and Rigid Plastics. AMC has the opportunity to continue to take share given its scale benefits (greater resin purchasing scale, manufacturing and innovation capabilities) and it should continue to generate solid organic growth in emerging markets as more sophisticated packaging moves through the supply chain. The combined business is strongly cash generative and has a strong balance sheet, which will support acquisitive growth or buy-backs. The greater scale in the US provides AMC with a base to begin consolidating that market further now as well. The combined group is targeting \$180m of synergy benefits, and based on managements' past track record, we believe this is achievable. The company is aware of customer concerns around the use of plastic packaging and is working with them to develop more environmentally friendly options. AMC's scale places it in a far better position than peers to drive this transition. Overall, we believe AMC continues to offer a solid medium-term growth story.

**Star Entertainment Group (SGR, -1.44%)** – underperformed during the quarter as the stock suffered from an announcement during May indicating that the company would not meet the market's FY19 earning expectations. Key drivers of the downgrade were a deterioration in consumer sentiment in Sydney surrounding the election as well as weaker than expected spend from international tourists in the VIP gaming rooms. A feature that we have seen in the current market is that short-term headwinds are being extrapolated into the long-term as investors remain focused on investing in the certainty of growth, regardless of the price. We take the view that this trend is providing strong opportunities to invest in leading Australia companies at depressed multiples based on earnings expectations that do not reflect the medium-term earning potential. SGR remains a conviction position in the portfolio as its long-term licences and expanding asset base will provide long-term sustainable growth into the future. Short-term catalysts include the resolution of the Queensland Government's

request for bids to build a second casino on the Gold Coast where we view a negotiated outcome is likely, ultimately leading to a re-rate. We are also cognisant that SGR is a potential target for an offshore casino operator following the recent investment by Melco into Crown Australia.

#### **Key detractors**

Key detractors	Positioning
Link Administration Holdings	Overweight
Oil Search	Overweight
Challenger	Overweight

**Link Administration Holdings (LNK, -32.25%)** - was a substantial negative contributor to the performance of the portfolio during the quarter after the company downgraded earnings substantially just prior to the end of June. This is the second downgrade in the past 12 months and relates to the Funds Administration (changes to low balance super account laws in Australia) and Corporate Markets businesses in Australia, and the impact of Brexit uncertainty on the UK/European businesses. LNK operates a number of back office processes (which are low value, but high volume per transaction) for groups including industry funds, companies, fund managers, and debt owners. LNK is also a major shareholder in PEXA, which now plays a key role in the settlement of home sales/mortgages, etc. This mixture of businesses provides a stable annuity-style income stream and good medium-term growth through the European operations and interest in PEXA. The balance sheet is in strong shape which can also be used to drive future earnings growth. We have been surprised by the scale of the fall in the share price given it was not trading expensively to begin with, but believe the stock offers sound substantial upside over the next few years.

**Oil Search (OSH, -9.94%)** – underperformed the market in the June quarter. Key factors impacting OSH were the volatile oil price and uncertain PNG political landscape. During the quarter, the Brent oil price was driven up to US\$74/bbl by rising geopolitical tension (trade war, sanctions, etc.), and then fell down to US\$60/bbl due to reduced global growth forecasts and an uncertain extension of OPEC-led supply cuts. The Brent oil price ended the quarter at US\$64/bbl and OPEC has since agreed to extend its production cuts for another nine months. We think the change in PNG leadership will have a minimal impact on the value of the Papua LNG and PNG LNG expansion projects. We continue to expect a material OSH Alaskan resource and asset valuation upgrade over the next 12 months, confirmed by an OSH equity sell-down. The long-term value added from Papua/PNG LNG and Alaska remains very material for OSH - by 2024/25 they could drive a doubling of OSH production and free cash flow (FCF) generation of US\$2-3bn per annum.

**Challenger (CGF, -19.81%)** – fell during the quarter as short-term headwinds continue to pressure the core annuity business. CGF came out of the Hayne Royal Commission with its reputation intact and it is the key beneficiary from government pension rule changes that favour retirees acquiring annuities for their retirement asset mix. However, in the short-term, the disruption to the financial planning industry in the major financial institutions has negatively impacted flows into annuities more than expected. Whilst the independent advisors are a key target group, there will be short-term costs associated with the move deeper into this segment of the market. The medium to long-term outlook for this business is very solid given the aging of the Australian population and the government's desire to see people allocate at least part of their retirement savings to an annuity. On the Japanese annuity investor front, we have seen a deal signed recently with their partner and substantial shareholder, Mitsui Sumitomo Primary Life Insurance Company, which will deliver a substantial uplift in the volume of AUD and USD annuities to CGF on a medium-term basis. Although the near-term pressure on the business has been more than we had expected when we added the holding, the medium-term outlook for the business remains intact.

#### **Portfolio changes**

##### **Key additions and material adjustments**

Bought
Challenger Group (CGF)
WorleyParsons (WOR)
Ramsay Healthcare (RHC)

During the month we added a holding in **Challenger Group (CGF)** which provides investment management services to investors in the accumulation and the pension phases. Through Challenger Life, CGF is a leading provider of annuities and guaranteed income streams for domestic and Japanese investors. Also, CGF operates the multi-boutique funds management group, Fidante. We have taken the opportunity to add the holding after a substantial fall in the share price triggered by a sharp decline in flows into the Life business. We view the drivers of this slowdown as temporary in nature. The medium to long-term outlook for this business is very solid given the aging of the Australian population and the government's desire to see people allocate at least part of their retirement savings to an annuity. On the Japanese annuity investor front, we have seen a deal signed recently with their partner and substantial shareholder, Mitsui Sumitomo Primary Life Insurance Company, which will deliver a substantial uplift in the volume of AUD and USD annuities to CGF on a medium-term basis.

We also added a holding in **WorleyParsons (WOR)** during

the month. WOR has become a global E&C leader in hydrocarbons (No. 1), chemicals (No. 1) and metals and mining (No. 2). The future outlook for WOR is positive with EPS accretion from the Jacobs acquisition expected to be at least +50% post run-rate cost synergies of ~A\$130m p.a. that are to be delivered within the next 2 years. Cost synergies are expected to mainly come from the areas of IT, property and from G&A savings. This does not include potential revenue synergies which could be material. WOR is already winning new contracts jointly bidding with Jacobs, plus the pace of new contract awards has increased and margins are on track to improve from better pricing, higher utilisation, greater volume and from leveraging the new contracts through lower overhead rates per chargeable hour. The acquisition of Jacobs Engineering Group's energy, chemicals, and resources business has significantly expanded WOR's geographic and industry footprint and more than doubles the size and scale of WOR's business which means it is now more likely to be the partner of choice for many of its key customers.

**Ramsay Healthcare (RHC)** was added to the portfolio in May due to our view that a liberal leadership will support the private health care industry as well as evidence that offshore markets including France and the UK are showing signs of stabilisation. We are of the view that current management will continue to drive growth from a strong set of assets and global demographic tailwinds.

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

Sold
Star Entertainment Group (SGR)
Transurban (TCL)
Sonic Healthcare (SHL)
Ansell (ANN)
Cybg Plc (CYB)

While we remain attracted to the strong growth outlook driven by expansionary investment, we removed **Star Entertainment Group (SGR)** from the portfolio to enable reinvestment into more attractive opportunities.

We have elected to take profits in **Transurban (TCL)** after it delivered +20% outperformance over the last 6 months from the relative yield play that makes TCL a more attractive investment in an environment with the potential for a further decline in interest rates (0.7% contraction in the US and AU bond yields over this period).

**Sonic Healthcare (SHL)** has performed strongly in the recent period and has reached out target valuation. Consequently, we have removed the stock and reinvested the funds into other strong investment opportunities.

**Ansell (ANN)** was removed from the portfolio in May as the return of tariff tensions between the United States and China will likely result in lower growth and higher input costs within Ansell's key manufacturing markets. Furthermore, recent strong performance saw the share price reach our intrinsic valuation.

Whilst **Cybg Plc (CYB)** looks cheap on a medium-term view after the acquisition of Virgin Money, the backdrop has changed since we first acquired the stock. We had expected the resolution of Brexit to occur, with or without an agreement, and to provide a basis for consumers and business to move forward. However, the political wrangling over the exit arrangements continue with no clear sign of a resolution. Our view was further confirmed after attending the investor day. The expected synergies from the merger seem achievable, however, other aspects of the future direction of the group left us concerned.

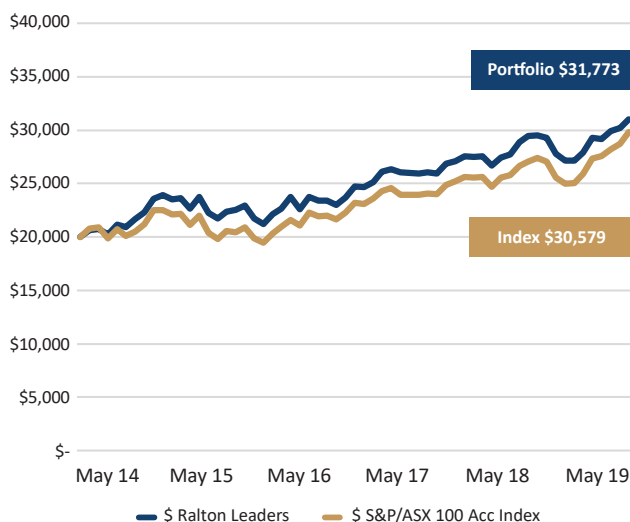
#### **Sector allocation**

GICS sector	Ralton	Index	+/-
Energy	10.4%	5.5%	4.9%
Materials	22.9%	18.7%	4.2%
Financials	37.4%	33.8%	3.6%
Health Care	10.3%	8.7%	1.5%
Utilities	2.3%	2.1%	0.2%
Consumer Staples	5.3%	5.2%	0.1%
Information Technology	1.4%	1.6%	-0.1%
Consumer Discretionary	4.5%	5.3%	-0.8%
Telecommunication Services	2.4%	3.6%	-1.3%
Real Estate	3.1%	7.2%	-4.1%
Industrials	0.0%	8.2%	-8.2%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>0.0%</b>

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

Company name	ASX code
BHP Group Limited	BHP
Commonwealth Bank.	CBA
ANZ Banking Grp Ltd	ANZ
Westpac Banking Corp	WBC
CSL Limited	CSL
Woolworths Group Ltd	WOW
Amcor PLC	AMC
Aristocrat Leisure	ALL
Suncorp Group Ltd	SUN
Ramsay Health Care	RHC

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



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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.

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