Ralton Leaders

Quarterly Portfolio Report | December 2022

RALTON ASSET MANAGEMENT

Key facts

Income versus growth target

Income — Growth

Market cap bias

Large — Small

Investment strategy

A portfolio of ASX-listed equities designed for long-term capital growth and some tax-effective income

Investment objective

Outperform index by over 3% p.a.

Benchmark index

S&P/ASX 100 Accumulation Index

Portfolio Manager

Will Riggall

Inception date

February 2008

Management fee

0.75% p.a. (may vary across platforms)

Number of stocks

25-35

Key platforms

Brightday, Linear, OneVue, Praemium

Performance (%, returns greater than one year are p.a.)[1]

At month end	1 mth	3 mth	1 yr	3 yr	5 yr	10 yr	Inception
Ralton	**-3.64%**	**8.78%**	**4.76%**	**7.70%**	**7.79%**	**10.00%**	**7.46%**
Income	*0.28%*	*0.81%*	*3.52%*	*3.36%*	*3.86%*	*3.96%*	*4.32%*
Growth	*-3.92%*	*7.97%*	*1.23%*	*4.33%*	*3.93%*	*6.03%*	*3.14%*
Index[2]	**-3.24%**	**9.32%**	**0.63%**	**6.07%**	**7.65%**	**8.98%**	**6.29%**
Outperformance	**-0.40%**	**-0.54%**	**4.12%**	**1.62%**	**0.13%**	**1.02%**	**1.17%**

[1] Performance is based on a model portfolio and is gross of investment management and administration fees, but net of transaction costs. Total returns assume the reinvestment of all portfolio income.

[2] Index means the S&P/ASX 100 Accumulation Index.

Portfolio Commentary

Looking back on the 2022 year, it was one of meaningful change as interest rates finally lifted, reversing a 30-year trend. The resulting impact on markets was seismic with fundamental changes in sector performance and valuations.

Breaking down the market drivers for the calendar year the sectors that once drove the market namely technology (-33.7%), healthcare (-7.2%) and retail (-20.8%) performed poorly while cashflow and earnings sustainability, often referred to “value” and “quality” drove the market. In 2022 it was important to be different to the market, with Banks (+5.6%), Energy (+48.5%) and Materials (+13.5%) the sectors to invest in. Fertile ground for active investment.

Looking back across the December quarter, performance was largely driven by strong stock selection. The investment team sought to minimise portfolio volatility in increasingly uncertain markets by focusing on companies with strong business models and structural themes. The portfolio’s exposure to Materials and Energy lifted returns, key stock drivers were Northern Star (+39.3%), Mineral Resources (+17.41%) Worley (+17.83%) and Woodside (+11.94%).

Our cash holding, while detracting from performance, was not excessive. We use the cash holding to allow us to react quickly to market opportunities. In addition, with rates again moving higher in December our holding in James Hardie (-14.4%) detracted. With rates nearing an inflexion point we are reviewing our exposure to key rate sensitive sectors.

In response to the ever-changing investment environment, we took the opportunity to position the portfolio during the quarter to take advantage of mispricing and changes in macro and policy. Post an extended period of being underweight resources we added to our exposure to allow the portfolio to benefit from the reopening of China. Moreover, with rates nearing a peak we added to REITS funded through profit taking in names which have performed strongly including Mineral Resources.

The portfolio now is more exposed to global growth as China opens post its COVID lockdown and should continue to deliver robust performance in an environment of slowing inflation. Key risks to continued performance would be a sharp return to inflation exacerbated by China policy changes and a sharper than expected recession in the US. At this point there is limited evidence of either of these events in key indicators and company commentary.

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Portfolio Performance

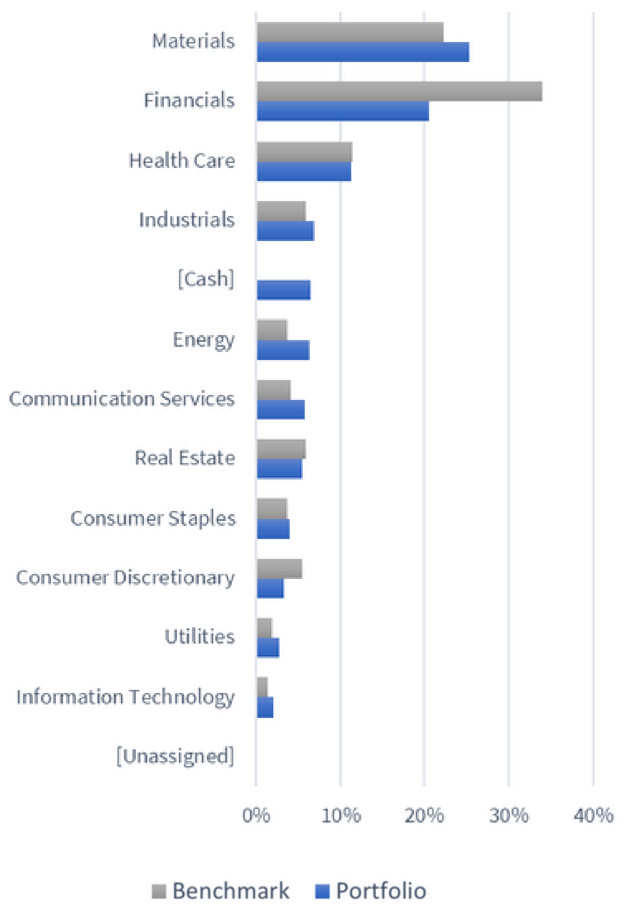
The Ralton Leaders Portfolio underperformed the ASX100 Accumulated Index in December and over the quarter, taking the total return over the last year to 4.76%, +4.12% ahead of the index return of 0.63%. A focus on investing in companies with strong competitive advantages and valuation support has held the portfolio in good stead during and extended period of volatility.

Contributors	Comment
Northern Star Resources Ltd (NST) 39.3%	NST continues to grow its output across four high quality gold operations in Australia and Canada. Yandal is expected to grow from 450k oz pa to 600k oz pa by 2024 and Pogo from 220k oz pa to 300k oz pa also in 2024. NST is a low cost gold producer with costs of circa $US1100 per oz and is a clear beneficiary of the currently rising gold price. The company is fully funded for its future growth projects and has excess cash on its balance sheet. We remain overweight.
Mineral Resources Limited (MIN) 17.4%	MIN has been a stellar performer with a surging lithium price and strong operational execution within its mining and services operations delivering significant growth in earnings, with earnings expected to further accelerate as projects come on stream. We see the potential for additional upside in the event that the group does progress with the proposed listing of its Lithium assets.
Worley Limited (WOR) 17.8%	Worley delivered strong performance in the quarter as a weaker Energy price was offset strong commodity prices and indications growth is set to accelerate. During the AGM in late October 2022 the company indicate 80% of their customers by revenue globally are committed to decarbonisation target, a key growth pillar for Worley. They are well positioned to meet the opportunities and challenges of the current market with a global leadership across key growth geographies. The geopolitical environment is elevating the need for energy independence and security of supply. In our view, the only main concern for WOR is managing inflationary impacts which the company appears to be managin well.
Detractors	
Downer EDI (DOW) -18.8%	Downer declined in December post a disappointing earnings update. While we were cognisant of the impact of weather on contractors, the 15% downgrade to FY23 NPAT guidance was worse than expected. What caused the sharp move lower was the additional information that DOW management had overstated booked earnings from a maintenance contract. Given the uncertainty we are reviewing the investment thesis and outlook.
Aristocrat Leisure Limited (ALL) 6.6%	ALL reported its FY22 results in the quarter, revealing a strong set of financials, however missing the strong consensus numbers. Standing out was the continued growth of gaming machines in the US, seeing strong outright unit sales growth and margin expansion. The one light area was digital/mobile gaming, with management flagging active users below forecasts and delays to launching a new digital platform.
James Hardie Industries PLC Chess Units of Foreign Securities (JHX) -14.4%	JHX traded weaker as the market reacted negatively to an update from the company flagging a weaker outlook. In the quarter JHX downgraded guidance by 10% as they are seeing a rapid deterioration in the US housing outlook due to higher interest rates. We had factored in a tough outlook, but the pace of the decline surprised. We see material upside however this will unlikely be met until interest rates plateau.

Portfolio Activity

BUY	
GPT Group (GPT)	We have been cautious about the listed property sector given increasing interest rates and uncertainty around workers returning to the office. With valuation now reset, reflective of the bottom of the cycle discounts to asset value, we see the risk/reward more balanced and look to increase exposure. Property historically performs well in periods of high inflation and GPT's diversified exposure to high quality assets across office, retail, industrial, and funds management provide a premium exposure to the sector.
Goodman Group (GMG)	While there are risks around cap rate expansion in the short term, we anticipate continued rental growth, with very low vacancy across the GMG portfolio which is located in highly desirable locations across global capital cities to drive long term earnings. We are very confident in the GMG strategy, and the enormous development pipeline that will generate long term value for shareholders.
SELL	
QBE Insurance Group (QBE)	QBE has performed well based on strength of USD earnings, as well as interest rates going up improving their future margins from investment in their reserves. Given its strong relative performance, volatile weather is likely to increase natural perils costs and possible claim inflation from strong commodity prices could offset these positive factors. At the current price, we believe the stock has captured most of its future upside and exited the position.
Downer EDI (DOW)	We have been long time supporters of the turnaround Grant Fenn has undertaken at Downer. However, the recent update from the company which talked to an overstatement of contracted earnings raises questions relating to risk controls, lowering our conviction. We exit the position, allowing us to reinvest capital into other opportunities identified by the team.

Sector Positioning



Top 10 holdings (alphabetical)

Aristocrat Leisure Limited
BHP Group Ltd
Coles Group Ltd
Commonwealth Bank of Australia
CSL Limited
National Australia Bank Limited
Northern Star Resources Ltd
Telstra Group Limited
Westpac Banking Corporation
Woodside Energy Group Ltd

Portfolio metrics*

	Ralton	XTOAI^
# of Securities	*28*	*98*
Market Capitalisation	*70,869.5*	*84,460.8*
Active Share	51.8	--
Tracking Error	2.86	*0.00*
Beta	0.91	*1.00*
Est 3-5 Yr EPS Growth	5.6	2.3
ROE	17.9	*18.8*
Dividend %	4.60	4.63
P/E using FY2 Est	13.4	14.2
Price/Cash Flow	7.9	9.0

* Source: FactSet

^ XTOAI means the S&P/ASX 100 Accumulation Index (Index). The Index is shown 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.