QUARTERLY REPORT
December 2011

RALTON ASSET MANAGEMENT

Ralton Smaller Companies

Winner of the 2010 Standard & Poors' Fund Awards - Separately Managed Accounts Category

Investment Profile

A Professionally Managed Portfolio of Australian Shares

The Ralton Smaller Companies 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 Smaller Companies SMA is to provide investors with long-term capital growth and some tax effective income from a concentrated portfolio of smaller capitalisation ASX listed shares. The Portfolio aims to deliver a return superior to that of the market over periods of five years or longer while at the same time seeking to minimise the risk of investment capital loss.

Key Portfolio Features	
Inception	1 February 2008
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Authorised Investments	ASX listed companies that are not included in the S&P/ASX 50 Index
No. of Stocks	25 to 40
Cash Allocation	0% to 15%
Tracking Error	5% to 9% per annum
Time Horizon	At least 5 years

Performance

Return %	3m	1yr	3yrs	Incept*
Ralton Smaller Comp.	**3.68**	**-8.66**	**12.10**	**-1.62**
Income Return	*1.11*	*3.73*	*4.05*	*4.02*
Growth Return	*2.57*	*-12.40*	*8.04*	*-5.64*
S&P/ASX Small Ords	-0.60	-21.43	11.83	-7.51
Difference	4.28	12.76	0.27	5.89

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

The Portfolio is designed for investors who…

- Seek long term capital growth & some tax-effective income
- Expect consistent above market returns
- Have a long term investment horizon of at least five years and accept the risk of significant price fluctuations.

Portfolio Structure

Top 10 Holdings

No.	Company Name	ASX Code
1	DUET GROUP	DUE
2	SAI GROUP LIMITED	SAI
3	GLOUCESTER COAL LTD	GCL
4	IINET LIMITED	IIN
5	RAMSAY HEALTH CARE LTD	RHC
6	AUSTRALIAN INFRASTRUCTURE FUND	AIX
7	NEW HOPE ORDINARY	NHC
8	ADELAIDE BRIGHTON	ABC
9	MICLYN EXPRESS	MIO
10	QUBE LOGISTICS	QUB

Industry Allocation *(ex-Cash)*

GICS Sector	Ralton	Index	+/-
Industrials	36.1%	17.5%	*+19.1%*
Financials (ex-Property)	8.5%	4.5%	*+4.0%*
Consumer Staples	5.3%	4.7%	*+0.6%*
Energy	16.8%	11.3%	*+5.5%*
Health Care	3.6%	3.7%	*-0.1%*
Utilities	4.5%	4.3%	*+0.2%*
Telecommunication Services	5.5%	3.4%	*+1.1%*
Property	2.7%	*5.0%*	*-2.3%*
Information Technology	0.00%	2.9%	*-2.9%*
Consumer Discretionary	4.1%	13.4%	*-9.3%*
Materials	13.0%	32.3%	*-19.3%*
Total	100.0%	100.0%	*0.00%*

Quarter in Review

Performance Summary

- The S&P/ASX Small Ordinaries Index finished largely flat, -0.6% after a highly volatile quarter. Materials and Energy sectors weighted on the market whilst Utilities and Telcos posted solid gains.
- Over the same period, the Ralton Small Companies portfolio delivered a positive return of **3.7%,** outperforming the market by **4.3%**.
- This was a pleasing result with good returns from several of our larger investments, together with a strong benefit from being underweight Resource [Material] stocks.

Portfolio Commentary

A number of our overweight positions added to performance during the period. MSF Sugar Ltd (+41.5%) and Gloucester Coal (+28.2%) were both the beneficiaries of corporate activity – for MSF Sugar, the proposed acquisition by major shareholder Mitr Phol looks highly likely to proceed, whereas for Gloucester Coal the transaction proposed with Chinese owned YanCoal will face further scrutiny. Investors in Gloucester Coal will need to better understand the assets that Yancoal are contributing to the combined company before the transaction proceeds. Defensive type stocks, Duet Group (+13.7%) and iiNet (+31.4%) both delivered strong returns, the latter making two strategic acquisitions late in the December quarter.

iiNet's share price gains were driven by the acquisition of two smaller competitors, TransACT in Canberra and InterNode in South Australia. Our view remains that iiNet is a well run business that produces good cash flow and hence will be a key player in the consolidation of internet service providers (ISPs) ahead of the National Broadband Network (NBN). For iiNet the introduction of the NBN creates greater regulatory certainty and with it an opportunity to build scale and continue to offer their service driven model to consumers. Competitor TPG Telecom has also been buying shares in iiNet, creating some price tension on the share registry.

Miclyn Express (+32.4%), who hire support vessels, namely tugs, barges and specialist boats to the offshore oil and gas industry also made good gains for the quarter. After struggling to deliver consistent profit results since listing, Miclyn now appear to be on track as demand for the offshore oil and gas industry improves.

We also held a number of positions in the portfolio which underperformed the market over the quarter. In the case of Dart Energy (-31.4%) and Perilya (-23.8%), both stocks were sold off heavily and were not alone in the Materials and Energy Sector. In the case of Perilya, a recent equity raise into a weakening share price further compounded the negative performance.

Outdoor retailer Kathmandu (-25.6%), whose results in recent times had demonstrated strong sales growth and demand for their outdoor product fell victim to the downturn in retail sales felt by the majority of the retail sector pre Christmas. The resultant downgrade to full year profit forecasts was not received well by the market.

During the quarter, a couple of stocks detracted from performance as they were not held in the portfolio. Aurora Oil & Gas, a US based shale gas producer made strong gains as did Regis Resources, an emerging gold producer with operations based in Western Australia. We added a small position to Regis, late in the quarter.

Quarterly Performance Attribution

Top Contributors	*Positioning*	Key Detractors	*Positioning*
Miclyn Express	*Overweight*	Dart Energy	*Overweight*
Gloucester Coal	*Overweight*	Aurora Oil	*Underweight*
MSF Sugar Ltd	*Overweight*	Regis Resources	*Underweight*
iiNet Ltd	*Overweight*	Perilya Ltd	*Overweight*
Duet Group	*Overweight*	Kathmandu	*Overweight*

Portfolio Adjustments

During the quarter we...

SOLD: Atlas Iron Ore (AGO), Fletcher Building (FBU), Monadelphous (MND), Kathmandu Holdings (KMD) & MSF Sugar Limited (MSF);

BOUGHT: Bega Cheese Limited (BGA), Decmil Group (DCG), Discovery Metals (DML), New Hope Ordinary (NHC) & Regis Resources (RRL);

During the quarter we made a number of changes to the portfolio where we saw the opportunity to add positions which were attractively priced relative to our view of their intrinsic value. Most of the buying centred on Resource stocks late in the quarter although we also took the opportunity to increase our holdings in the Agricultural sector.

The weakness in both commodity and stock prices lead to many good quality stocks in the sector being heavily sold down. Having held an overweight cash allocation for much of the quarter we elected to increase our exposure to Resources, adding a quality Copper (Discovery Metals), Gold (Regis Resources) and Coal (New Hope Ordinary) exposure to the portfolio. In the case of Discovery Metals we have been watching this stock and the development of their key Copper project for some time and have now gained sufficient comfort to begin buying the stock.

We also have purchased a holding in Bega Cheese, a NSW and Victorian based cheese manufacturer. Bega has a long history and strong brand and has over recent years been a key player in the aggregation of the industry and move away from the model of farming 'co-ops.' Given that Bega is predominantly a cheese processor it faces minimal 'seasonal' risk and benefits from long contract agreements with both farmers (suppliers) and end customers.

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)

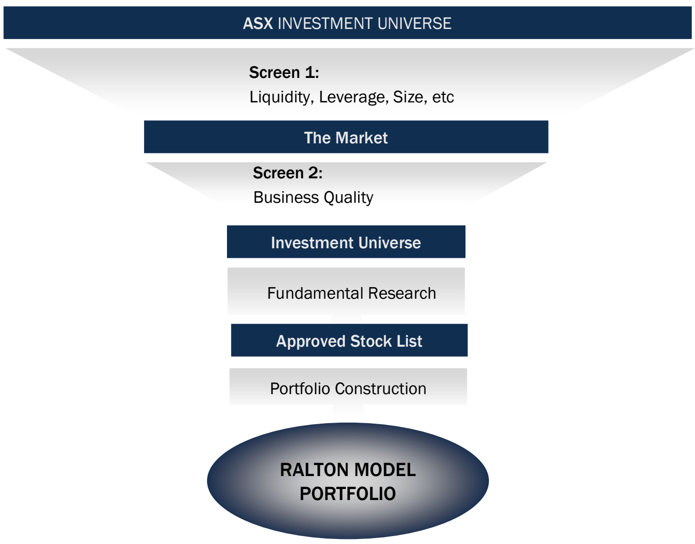
The first stage of the process is to narrow the number of stocks in the investment universe by applying a number of screens. This approach systematically eliminates companies that do not meet certain minimum standards, allowing the Investment team to focus more intensely on companies of potential interest.

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 part of the Armytage group, a boutique investment specialist majority owned by members of its investment team and key executives. Founded in 1997, Armytage is a pioneer in Australia's investment industry, offering a suite of actively managed SMAs, IMAs and managed funds.

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*
Portfolio Manager, 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 19 years, including the past 5 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.

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