WATERMARK FUNDS MANAGEMENT | AUSTRALIAN LEADERS FUND

NTA and Monthly Update – March 2020

Company at a Glance

ASX Code	ALF
Fund Size	AU$208.8
Fund Strategy	Variable Beta
Share Price	$0.87
Shares on Issue	199.0m
Net Exposure	-6.6%

Net Tangible Asset (NTA) Backing

	Feb 20	Mar 20
NTA Before Tax	**$1.15**	**$1.13**
NTA After Tax	$1.13	$1.13*

Gross Portfolio Structure

	Feb 20	Mar 20
Long Exposure	71.8%	23.6%
Short Exposure	-78.8%	-30.3%
Gross Exposure	150.6%	53.9%
Cash	107.0%	106.6%

*The After-Tax NTA includes a $0.075 per share deferred tax asset, which is net of tax liabilities accrued in the current financial year.

Month in Review

The Australian share market suffered further falls in March, as the shockwaves from the COVID-19 pandemic reverberated through asset markets. Volatility in the share market has risen to the highest level seen since the European sovereign debt crisis, with precipitous falls in the month punctuated by sharp relief rallies. From the peak on February 20, the market fell 36% before staging a rally in the final week of March, finishing down over 20%.

The Fund has been fully hedged for some time, given our view that stretched valuations and narrow leadership from a small group of high growth companies had left the share market vulnerable to a shock. However, the onset of the Coronavirus pandemic took us by surprise, along with the rate at which markets fell as the crisis took hold. While the Fund was protected from any major loss, we were carrying a small long bias towards smaller companies, which were much harder hit than the broader market. This bias took some time to neutralize and the Fund fell by 3.3% in the month.

We have taken several decisive steps to ensure the Fund is well-positioned to withstand further shocks. We have significantly decreased the gross exposure of the Fund, which is currently sitting at around 55% down from an average level of around 180%. To explain this setting, the Fund now has around $22 invested long and $31 short for every $100 of capital. We also use futures to modulate the Fund's net exposure to the share market, in this case buying $2 of SPI futures to deliver a net short exposure of 7%.

We have also significantly cut the number of positions in the portfolio and tightened our risk settings to ensure we are not carrying any unintended bias or skew, which can manifest as losses in a volatile market.

Our task from here is to capitalize on the mispricing opportunities that are currently presenting themselves. A key feature of our long/short investment process is the ability to create value through stock selection without taking directional position on the market. We will of course continue to closely monitor the macroeconomic landscape for signs of a breakout, or further break down in the share market. Given the uncertainty which has shrouded the market, we prefer to maintain our conservative settings for now, and look for opportunities to add value wherever we can.

Commodities mostly held their value in the month, or in some cases increased in A$ terms. Given its importance for the Australian economy, the mining sector has been deemed essential. Most companies responded quickly by changing work patterns and implementing social distancing. While impacts will still be felt, the level of business interruption is likely to be lower than in other sectors. The oil markets were rocked by a dispute between Russia and Saudi Arabia over production cuts - the oil price fell to below US$19/bbl. Our shorts didn't keep pace with the falls in our longs this month, with oil exposures hit particularly hard. Key performers were WPL, the position in the S&P Oil & Gas Exploration & Production ETF, AWC and MIN while detractors were ORG, KAR, BHP and NIC. Going into April, we have positioned defensively in metals & mining and oil and gas while we are long gold, given continued uncertainty in markets, quantitative easing and strong margins being generated by gold miners.

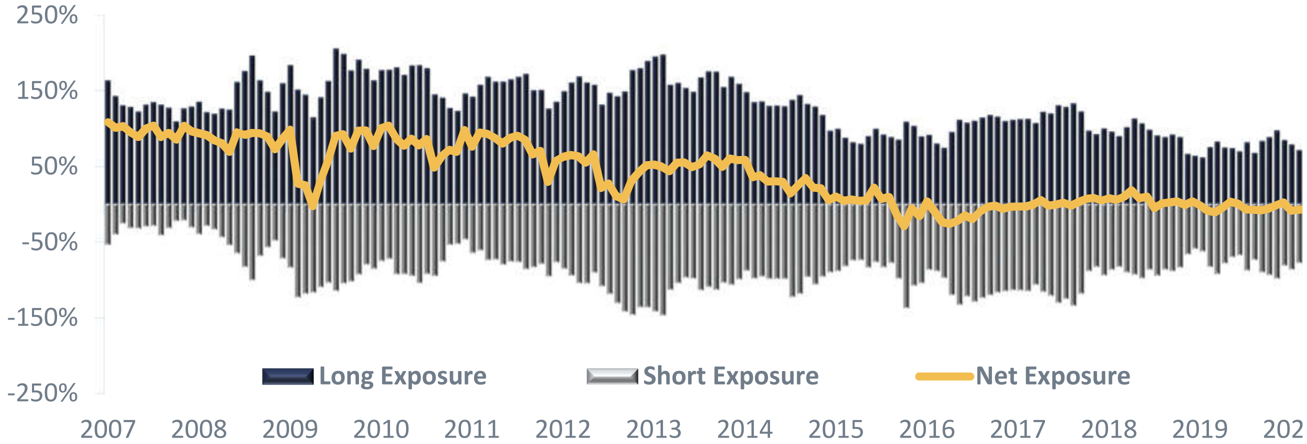
Financials contributed positively in March due to short positions in real estate names. We now think the worst has passed for these companies and have moved to long positions into April. Other key contributors were shorts across the banking sector, which continued to experience large sell-offs. Investors remain wary of the scope for broad balance sheet provisions against poor performing loans. While we have pared back our shorts in the sector, the banks have failed to fully participate in the recent market rally. A handful of longs also contributed to returns in the back half of the month, for example Pendal. We continue to see Pendal as a quality fund manager with a solid management team. The business has faced a myriad of macro pressures, moving from Brexit to COVID-19, reaching its lowest ever PE of 6.7x which we consider shows appealing value.

The Healthcare portfolio detracted in March. Despite significant wins on short positions in domestic service providers that were heavily impacted by falling utilisation rates, a handful of midcap investments also got caught in the indiscriminate selloff, effectively offsetting the gains on the shorts. As activity normalises post-lockdown, we expect to take advantage of these dislocations. On the positive side, a core investment in CSL outperformed most of its healthcare peers as its operations are less disrupted by COVID-19 than other activities like elective surgeries (Cochlear, Ramsay). While the virus can cause short term difficulties in the collection of plasma, inventory in the supply chain as well as the 6-9 month processing time leave plenty of headroom for CSL to make up the shortage later in the year.

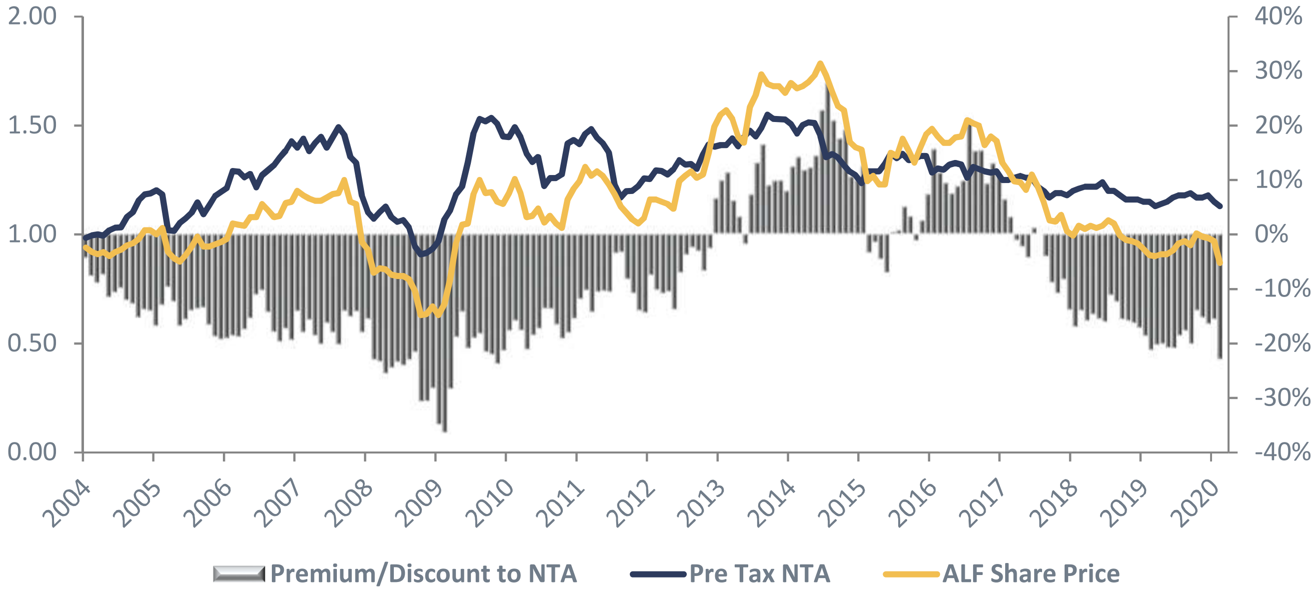
With a tilt towards value names coming into the month, the TMT portfolio also suffered. Going into March, our bottom-up work had flagged compelling value opportunities emerging in the Australian media and internet space. Low valuations, easy comps and accelerating activity presented a solid set up for these positions. However, the sudden spread of COVID-19 and the ensuing shutdown of economic activity turned the playbook upside down, as our value names tend to have more cyclical exposure than some our expensive (short) hedges which were more tilted towards growth.

The Consumer/Industrials sectors also detracted from portfolio returns in March. While we did have hedges in place, the aggressive sell down and the abrupt correction in the final week of the month, made managing the portfolio challenging, given the size and severity of the movement. In particular, we were impacted by the decision by several governments globally to close licenced venues, theme parks and casinos as part of COVID-19 social distancing initiatives. Our position in Aristocrat, a global leader in gaming suffered losses due to closure of many of its casinos. Governments have since come out with several funding packages to assist these companies in trading through this difficult period. Interestingly, some governments have now signalled a likely softening in social distancing restrictions, which could see a rapid recovery in the valuation of these assets.

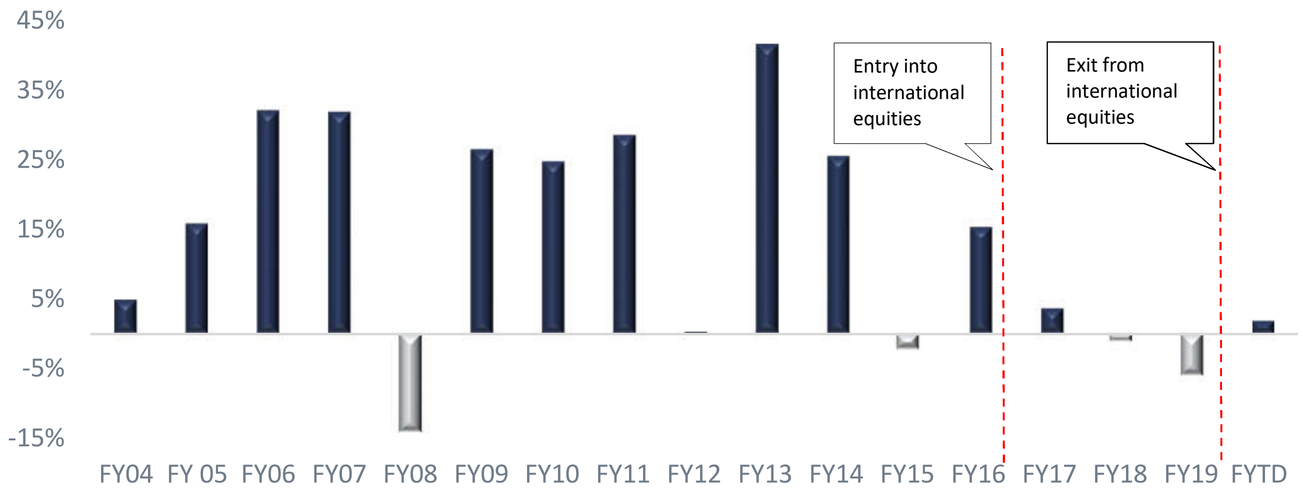
Net Equity Exposure



Premium/Discount to NTA History



Gross Portfolio Return



Monthly Net Performance (%)

Year	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
FY04								0.4	1.4	0.2	0.0	2.3	**4.3**
FY05	1.1	-0.3	4.6	2.8	4.4	2.4	0.3	1.3	-0.9	-6.1	-0.4	4.8	**14.3**
FY06	2.0	2.7	4.8	-3.0	3.9	3.7	1.5	2.0	6.4	2.9	-2.1	1.4	**29.0**
FY07	-3.2	4.3	1.7	7.2	2.8	2.5	3.1	-1.6	3.5	1.1	2.7	2.0	**29.2**
FY08	-1.0	3.4	3.3	1.0	-0.3	-1.9	-11.5	-8.4	1.4	4.4	1.5	-7.2	**-15.5**
FY09	-1.3	5.1	-5.4	-16.3	-6.6	3.0	2.2	2.9	16.0	6.7	7.9	7.0	**18.7**
FY10	9.2	12.4	6.5	-0.7	0.8	0.1	-3.5	2.2	4.2	-2.1	-7.1	-2.3	**19.9**
FY11	2.8	-3.9	2.3	0.0	2.7	12.0	2.0	1.9	3.6	1.7	-1.8	-1.8	**22.9**
FY12	-4.1	-6.8	-8.4	6.5	-1.5	0.9	4.9	4.7	3.3	1.2	-2.4	0.7	**-2.3**
FY13	3.7	3.6	0.3	-1.3	6.5	3.4	3.4	1.6	3.0	2.7	0.5	2.2	**33.9**
FY14	3.8	3.5	2.8	4.0	-0.6	0.0	-0.2	4.0	-1.4	2.6	1.2	0.3	**21.6**
FY15	-3.6	-2.4	1.4	-1.3	-2.5	-1.1	-1.2	1.0	3.0	0.8	-0.5	3.1	**-3.4**
FY16	3.8	3.0	1.5	-1.6	0.4	2.0	0.0	-2.1	1.4	-0.4	1.9	1.0	**11.2**
FY17	-0.3	-0.6	3.9	-0.5	-0.9	-0.2	-0.7	-0.1	0.1	1.2	0.7	-0.5	**2.0**
FY18	0.3	-1.8	-0.4	-3.1	1.3	0.1	-0.6	0.7	0.9	0.9	0.0	-0.6	**-2.3**
FY19	2.6	-1.6	0.2	-2.0	-2.9	-1.4	0.5	0.7	-1.0	-2.3	-0.8	0.7	**-7.2**
FY20	2.1	1.0	0.1	1.3	0.0	-0.4	1.3	-1.2	-3.3				**0.8**

Dividend History

The Board is committed to paying fully franked dividends to shareholders, provided the Company has sufficient profit reserves and franking credits and it is within prudent business practices.