

Investment Update and NTA Report

31 October 2014



Month in Review

October saw a sharp rebound in the All Ordinaries Accumulation Index, which went on to recover some 70% of the previous months' losses. In fact, Australian Equities outperformed all other developed and developing markets in the month. The rebound was led by defensive names, with Banks, REITS and Telstra Corp all contributing strongly to the performance of the index.

The fund lost 1.87% in October. The long portfolio lagged the market with investments in Energy, Resources and the Contractors weighing on performance. The short portfolio also rose with the market, detracting from performance.

The flight of capital into Defensive industries offering attractive dividend yields continues. While defensive shares appear expensive they are likely to remain so, as long as Central Banks keep cash rates low.

Cyclical shares followed the broader market higher during the month. This advance was in spite of ongoing weakness in the domestic economy which shed 30,000 jobs in September. Retail sales remained flat and the NAB business confidence index slipped to the lowest level since the federal election.

The Financial sector was stronger in October, with particular strength in the Diversified Financials and Insurers. We remain of the view that earnings growth for the major banks will be elusive now that falling bad debt charges have bottomed. Coupled with higher capital requirements, the ability of the banks to continue increasing their dividend payout ratios will be constrained.

Shares in the Resources sector continued to perform poorly in October. Oil was in focus for the month as the price per barrel dropped by a further \$15 to levels not seen since 2010. Prices of bulk commodities and gold also moved lower, which presented an opportunity to add to the Company's mining exposure given the underperformance relative to other sectors.

Net Tangible Asset (NTA) Backing

Month	September 2014	October 2014
NTA before tax on unrealised gains	\$0.99	\$0.97
NTA after tax	\$0.99	\$0.98

Performance (Net of all Fees and Expenses)

Performance at 31 October 2014	1 Mth	6 Mths	Fin. YTD	1 Yr	3 Yrs %pa	5 Yrs %pa	Since Inception %pa
WMK (net return)	-1.9%	-3.2%	-5.1%	1.3%	N/A	N/A	4.7%
RBA Cash Rate	0.2%	1.3%	0.8%	2.5%	N/A	N/A	2.5%
Outperformance (net)	-2.1%	-4.5%	-6.0%	-1.2%	N/A	N/A	2.2%

Watermark Market Neutral Fund

ASX Code	WMK
Listed	Jul 2013
Capital	\$85.0m
Market capitalisation	\$84.9m
Share price	\$0.97
NTA before tax	\$0.97
Shares on issue	87.5m
Fully franked dividend (FY14)	5c
Dividend yield (fully franked)	5.1%

Company Overview

The Watermark Market Neutral Fund (WMK) is a listed investment company that invests predominantly in Australian shares. The fund will maintain a market neutral structure with no greater than 10% of the company's assets exposed to the share market on a net basis at any one time. It is the Board's intention to try and deliver to shareholders a consistent and growing stream of fully franked dividends over time.

Investment Strategy

The primary goal of the investment process is the identification of mispriced securities. In a market neutral strategy the manager constructs two portfolios: a "long" portfolio of preferred shares and a "short" portfolio of less preferred shares. As the portfolios are roughly of equal size, this is a fully hedged structure aiming to minimise exposure to market movements. The fund profits to the extent the long portfolio outperforms the short portfolio plus the interest received on the fund's capital which is retained in cash.

Investment & Management Team

Justin Braitting
Chief Investment Officer/
Portfolio Manager

Tom Richardson, CFA
Senior Investment Analyst

Joshua Ross
Investment Analyst

Omkar Joshi, CFA
Investment Analyst

Delian Entchev
Investment Analyst

Tim Bolger
COO & Head of Distribution

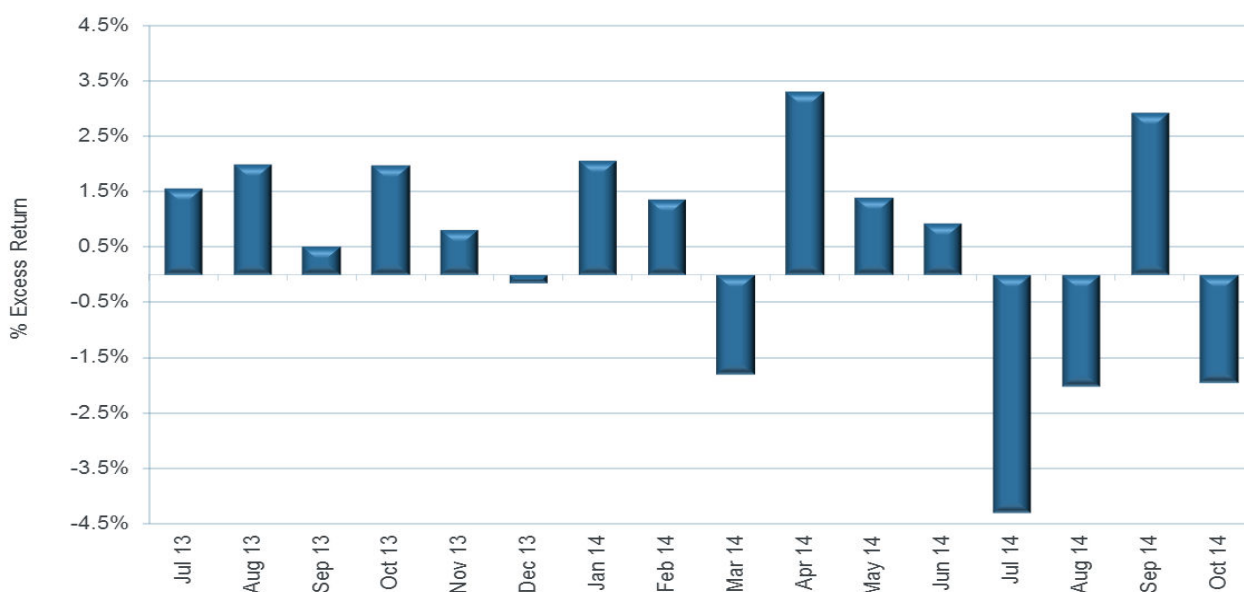
Shannon Wells
Office Manager

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Monthly Excess Returns (Gross Alpha)



Fund Attribution

In this strategy, shareholders benefit to the extent that shares in the long portfolio which the manager prefers outperform the shares in the short portfolio. In October, the Long Portfolio increased in value by 0.3%, underperforming the short portfolio which increased by 2.0%. Since inception the long portfolio has outperformed the short portfolio, resulting in a positive return for shareholders despite volatile markets.

	1 Month Return (%)	3 Month Return (%)	6 Month Return (%)	Financial YTD Return (%)
	Portfolio ¹	Portfolio ¹	Portfolio ¹	Portfolio ¹
Long Portfolio	0.3%	-4.8%	-1.3%	-1.4%
Short Portfolio	2.0%	-4.5%	0.2%	2.4%
Cash	0.0%	0.3%	0.7%	0.3%
Total	-1.7%	-0.5%	-1.9%	-4.6%

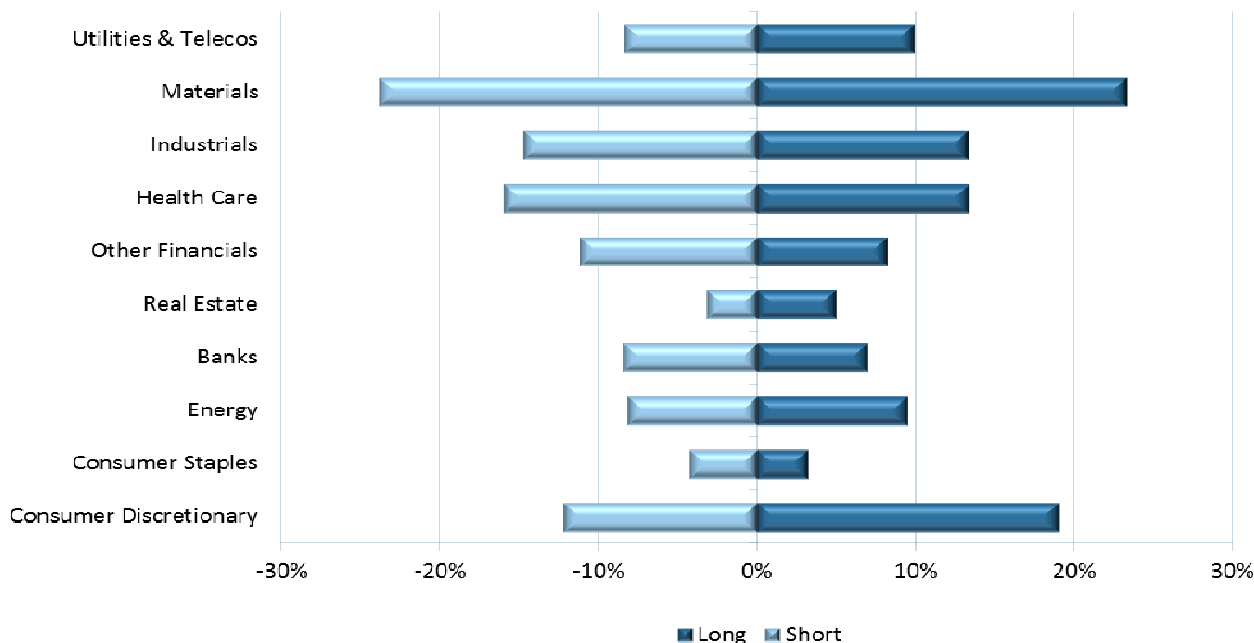
¹ The "Portfolio" column displays the return achieved in the period from the Investment Portfolio (long) and from the Borrowed Securities portfolio (short) separately. A negative return for the short portfolio is a good outcome and adds to performance. The Total Portfolio performance, representing the underlying return achieved on Shareholder's Funds is a weighted return of the long and short portfolios as well as cash.

Gross Portfolio Structure

Investment Type	30 September 2014		31 October 2014	
	\$m	%	\$m	%
Listed Securities - Long	98	110%	95	112%
Listed Securities - Short	-91	-102%	-95	-112%
Net Exposure	7	8%	0	0%
Cash	82	92%	85	100%
Capital	89	100%	85	100%

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Sector Exposures



Option Issue

As part of IPO the Company issued options to acquire ordinary shares in the Company at an exercise price of \$1.00.

The options can be exercised at any time on or before 31 December 2014. The options give the shareholders the right but not the obligation to subscribe for shares in WMK at \$1.00 per share. The options can be exercised in full or in part. The options are currently trading on the ASX under the code WMKO.

As at 31 October 2014, 6,803,781 options have been exercised and allotted for a total consideration of \$6,803,781. The remaining balance of outstanding options at 31 October 2014 is 63,714,844.

Dividend History

The Board is committed to paying an increasing stream of fully franked dividends to shareholders, provided the Company has sufficient profit reserves and franking credits. Dividends are paid on a six-monthly basis and the dividend reinvestment plan is available to shareholders for both the interim and final dividend. In August 2014 the Board declared a 2.5c fully franked dividend, taking the full year dividend to 5c and in line with the 5% full year dividend targeted by the Board.

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