

# Investment Update and NTA Report



31 December 2014

## Month in Review

After dropping to mid-month lows, the All Ordinaries Accumulation Index rallied in the final weeks of December to close 1.93% higher for the month. The continued fall in the price of oil has undermined confidence in the global economy generally, leading to falls in most major share markets. The exception was China, with the Shanghai Composite Index continuing its strong rally to finish the year up over 50%.

Returns for investors in shares were modest in 2014 relative to recent years. For the Australian share market, some 80% of the total market return came from dividends, with capital returns anaemic in most sectors and strongly negative in the resource and energy sectors. The falling Australian dollar continues to provide both a help and hindrance in varying parts of the share market. This is evident across and within sectors, as winners and losers emerge from what could be a prolonged trend. We retain a cautious outlook for the Australian share market in 2015, with only modest growth in GDP forecast and domestic demand expected to languish at near recessionary levels.

The portfolio returned -1.1% in December with the short portfolio accounting for most of the negative performance. While the portfolio has been positioned conservatively in respect of several major macroeconomic trends, stock specific issues have hurt performance.

We have maintained the Company's neutral exposure to the energy sector, resulting in a small positive contribution to performance for the month. While the portfolio has a small net exposure to mining shares overall, positions include smaller resource names such as Tiger Resources and Base Resources which have suffered sharp falls in recent months.

Surprise rallies from a handful of short positions detracted from performance in December. These included a number of biotech names which have been profitable positions over the long term. We remain confident that the investment theses supporting these positions will continue to play out as expected.

## Net Tangible Asset (NTA) Backing

Month	November 2014	December 2014
NTA before tax on unrealised gains	\$0.96	\$0.95
NTA after tax	\$0.97	\$0.96

## Performance (Net of all Fees and Expenses)

Performance at 31 December 2014	1 Mth	6 Mths	Fin. YTD	1 Yr	3 Yrs %pa	5 Yrs %pa	Since Inception %pa
WMK (net return)	-1.1%	-7.5%	-7.5%	-1.8%	N/A	N/A	2.4%
RBA Cash Rate	0.2%	1.3%	1.3%	2.5%	N/A	N/A	2.5%
Outperformance (net)	-1.3%	-8.8%	-8.8%	-4.3%	N/A	N/A	-0.1%

### Watermark Market Neutral Fund

ASX Code	WMK
Listed	Jul 2013
Capital	\$83.1m
Market capitalisation	\$77.9m
Share price	\$0.89
NTA before tax	\$0.95
Shares on issue	87.5m
Fully franked dividend (FY14)	5¢
Dividend yield (fully franked)	5.6%

### 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

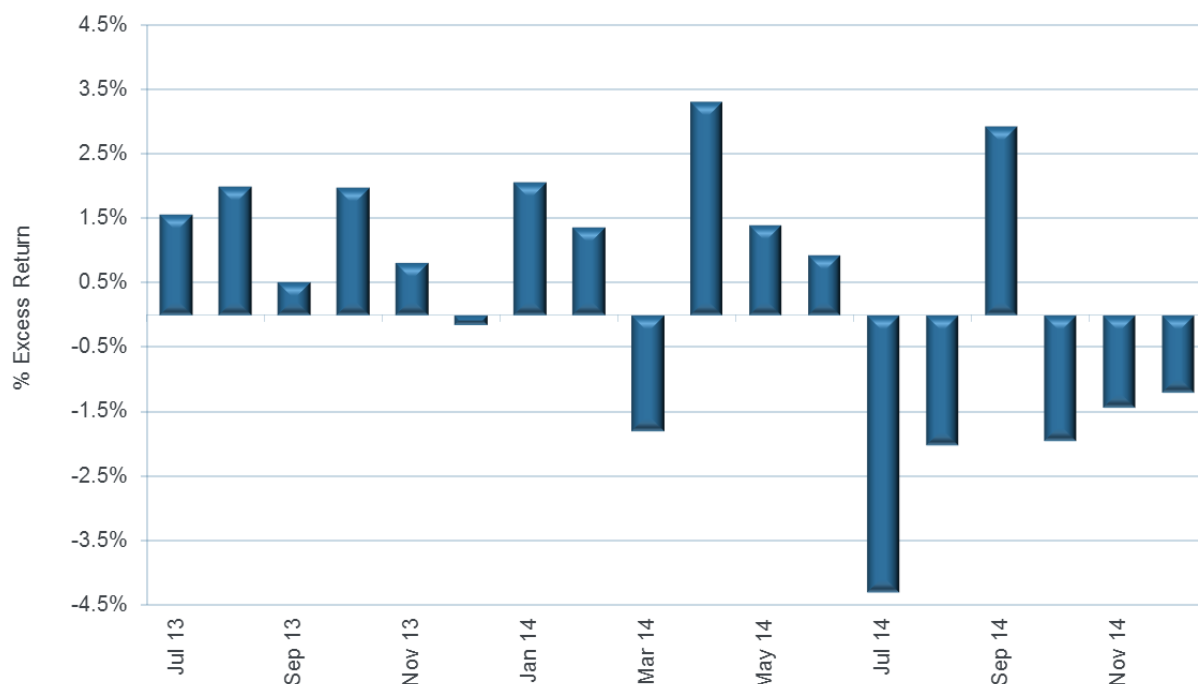
**Shannon Wells**  
Office Manager

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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 December, the Long Portfolio increased in value by 1.5%, underperforming the short portfolio which increased by 2.5%. 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 <sup>1</sup>	Portfolio <sup>1</sup>	Portfolio <sup>1</sup>	Portfolio <sup>1</sup>
Long Portfolio	1.5%	-2.0%	-3.6%	-3.6%
Short Portfolio	2.5%	2.0%	2.4%	2.4%
Cash	0.2%	0.5%	0.8%	0.8%
<b>Total</b>	<b>-1.0%</b>	<b>-4.0%</b>	<b>-6.8%</b>	<b>-6.8%</b>

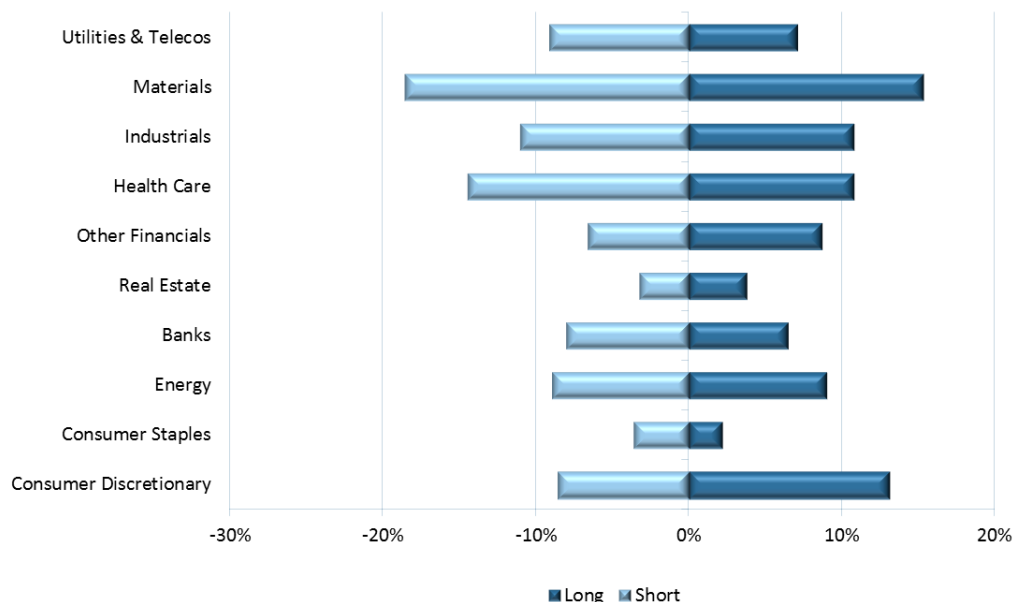
<sup>1</sup> The "Portfolio" column displays the return achieved in the period from the Investment Portfolio (long) and from the Borrowed Securities portfolio (short) separately. A negative return for the short portfolio is a good outcome and adds to performance. The Total Portfolio performance, representing 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 November 2014		31 December 2014	
	\$m	%	\$m	%
Listed Securities - Long	88	105%	72	87%
Listed Securities - Short	-83	-99%	-77	-93%
<b>Net Exposure</b>	<b>5</b>	<b>6%</b>	<b>-5</b>	<b>-6%</b>
Cash	79	94%	88	106%
<b>Capital</b>	<b>84</b>	<b>100%</b>	<b>83</b>	<b>100%</b>

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## Sector Exposures



## 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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