

# Investment Update and NTA Report

31 January 2015



## Month in Review

January was a strong month for share markets around the world as Central Banks sought to battle falling rates of growth and inflation with interest rate cuts and quantitative easing. In Europe, the ECB's announcement of a large scale bond buying program saw European stock markets post strong gains. The US market was weaker however, as a rising US dollar weighed on corporate profits.

The domestic share market rose by 3.2% in January, buoyed by a falling currency and in anticipation of a drop in the RBA cash rate. With further rate cuts expected, investors' demand for income continues to be a dominant theme. Notwithstanding this recent market rally, growth in the economy is forecast to be weak and risks are elevated.

The portfolio delivered a return of -1.18% for the month. After a promising start, early gains were lost as a number short positions suffered adverse moves in the final week of January. This negative momentum was exacerbated on the last day of the month, with a significant fall in the price of Tiger Resources, a copper miner in which the Company has a small position. Weaker performance was offset in part by strong returns from exposures in the gold sector.

As a sector of the market buoyed by the stimulatory forces mentioned above, defensive shares look fully valued. The Company retains a net positive exposure in the sector however, with infrastructure and telecommunications as preferred industries.

Financial shares rallied with the broader market in January, with wealth managers, banks and real estate companies posting strong gains as a result of the continued decline in government bond yields. A key contributor was the Company's position in Henderson Group which benefited from positive sentiment around the announcement of quantitative easing in Europe.

Gains were also made in January from positions in retailers such as Super Retail Group. Despite our cautious outlook for the domestic economy in general, interest rate cuts and a marked drop in petrol prices have provided relief for household budgets, which in turn stimulates discretionary spending.

Resource companies continued to struggle in January, with further falls in commodity prices. This sector has proven difficult to manage in recent months, with stock and commodity specific issues weighing on the performance of the portfolio despite having no net exposure in the sector. While short-term volatility is a distraction, we are confident that the investment theses supporting the Company's individual positions in the sector will play out as expected over time.

## Net Tangible Asset (NTA) Backing

Month	December 2014	January 2015
NTA before tax on unrealised gains	\$0.95	\$0.94
NTA after tax	\$0.96	\$0.95

## Performance (Net of all Fees and Expenses)

Performance at 31 January 2015	1 Mth	6 Mths	Fin. YTD	1 Yr	3 Yrs pa	5 Yrs pa	Since Inception pa
WMK (net return)	-1.2%	-4.6%	-8.6%	-4.5%	N/A	N/A	1.5%
RBA Cash Rate	0.2%	1.3%	1.5%	2.5%	N/A	N/A	2.5%
Outperformance (net)	-1.4%	-5.9%	-10.1%	-7.0%	N/A	N/A	-1.0%

### Watermark Market Neutral Fund

ASX Code	WMK
Listed	Jul 2013
Capital	\$82.2m
Market capitalisation	\$73.1m
Share price	\$0.84
NTA before tax	\$0.94
Shares on issue	87.5m
Interim Dividend (1H15)	2¢
Dividend yield	5.3%

### 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

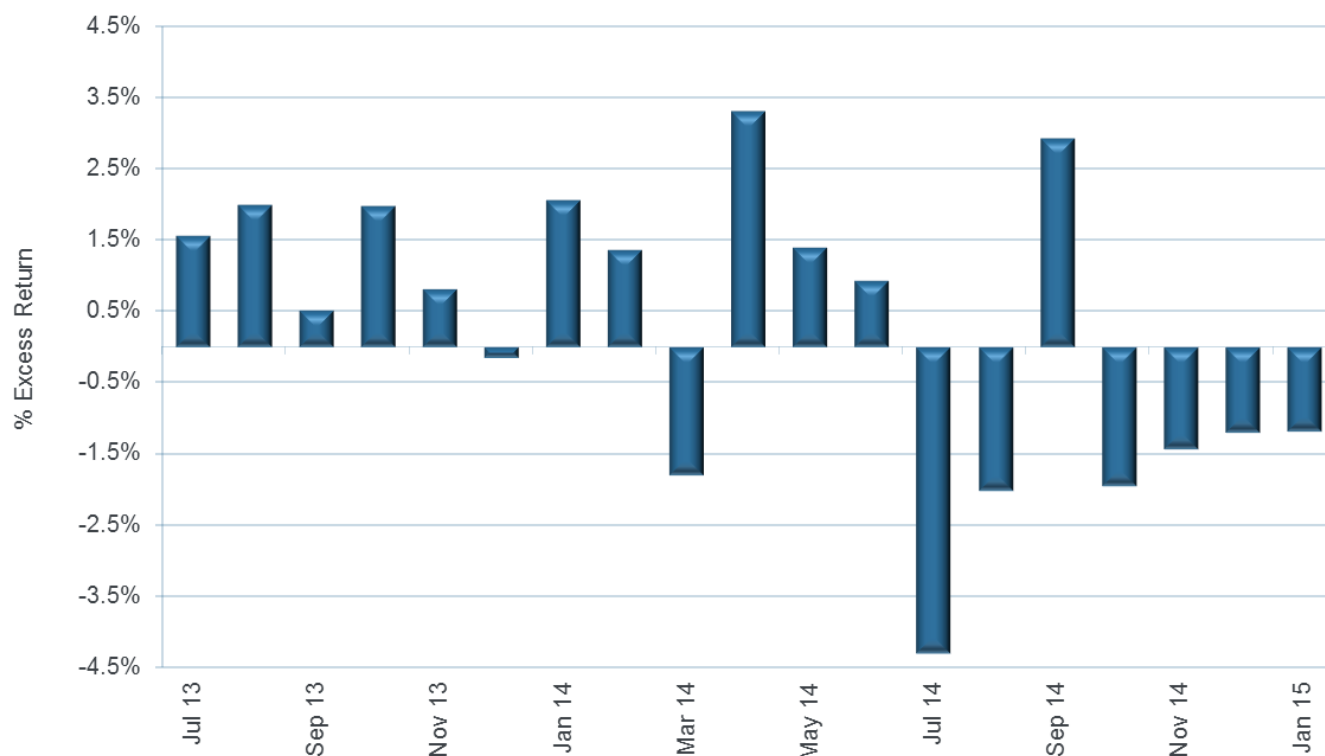
**Shannon Wells**  
Office Manager

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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 January, the Long Portfolio increased in value by 1.4%, underperforming the short portfolio which increased by 2.9%. 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	1.4%	-0.9%	-5.6%	-2.3%
Short Portfolio	2.9%	2.9%	-1.8%	5.4%
Cash	0.2%	0.7%	0.9%	1.0%
Total	-1.0%	-3.3%	-3.8%	-7.7%

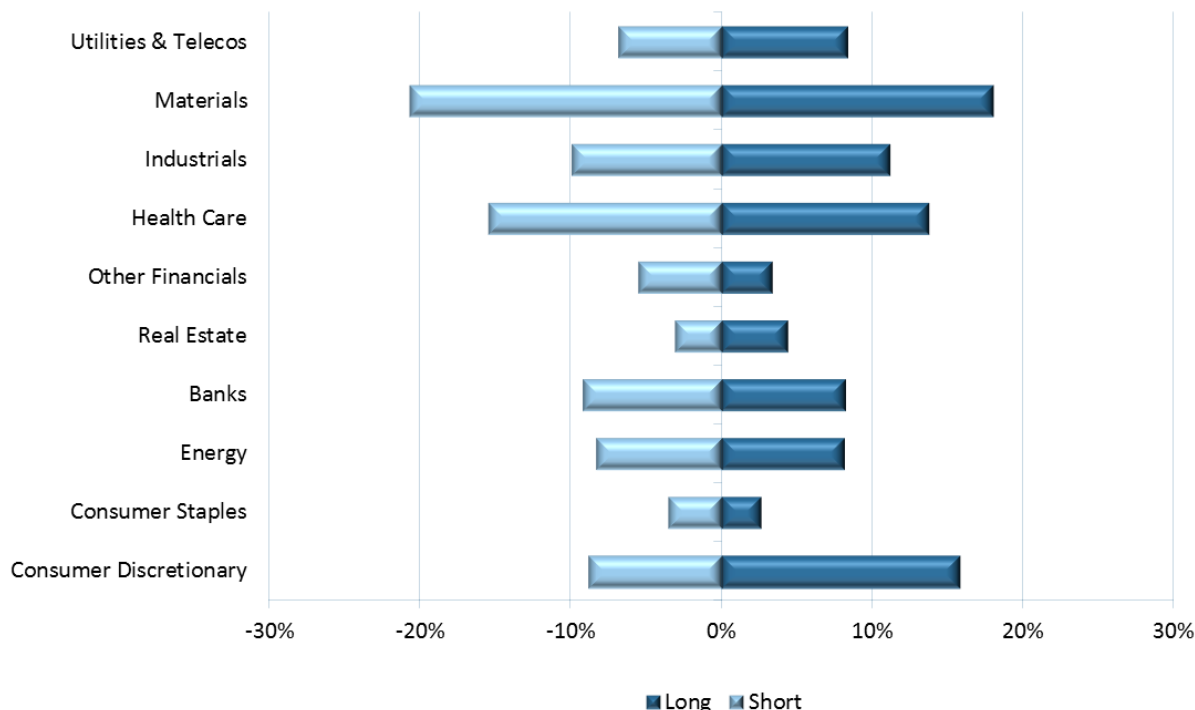
<sup>1</sup> The "Portfolio" column displays the return achieved in the period from the Investment Portfolio (long) and from the Borrowed Securities portfolio (short) separately. A negative return for the short portfolio is a good outcome and adds to performance. The Total Portfolio performance, representing 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	31 December 2014		31 January 2015	
	\$m	%	\$m	%
Listed Securities - Long	72	87%	77	94%
Listed Securities - Short	-77	-93%	-76	-93%
Net Exposure	-5	-6%	1	1%
Cash	88	106%	81	99%
Capital	83	100%	82	100%

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## Sector Exposures



## Dividend History

In February 2015, the Board declared a 2 cent interim dividend, franked to 70%. It remains an objective of the Board to pay a growing stream of franked dividends to shareholders over time, provided the Company has sufficient profit reserves and franking credits. Dividends are paid on a six-monthly basis. The Board maintains its target of delivering a yield of 5% and has a preference for the payment of fully franked dividends where possible.

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