WATERMARK
FUNDS MANAGEMENT

# The Leading Edge

QUARTERLY REPORT • September 2015

In this edition of *The Leading Edge* we consider the important role emerging markets play in global growth, along with the outlook for commodities.

Level 6, 139 Macquarie Street, NSW Sydney 2000

TEL (02) 9252 0225 • FAX (02) 9252 1220 • info@wfunds.com.au • www.wfunds.com.au

Justin Braitling
Portfolio Manager

## Could global growth moderate further? We look at the key role that emerging markets play.

Potential growth across the developed world has been slowing for decades due to an array of structural and demographic factors. Policymakers, mistaking this deceleration for a shortfall in demand, have implemented fiscal and monetary reflation to stimulate growth.

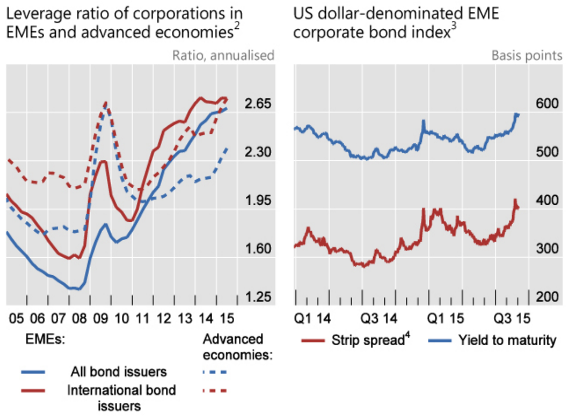
This additional demand has been funded primarily by debt, creating large balance sheet imbalances. As demand continues to fall short of expectations, markets are oversupplied everywhere, particularly in China and Europe where current account surpluses are running cumulatively above $US 1 trillion p.a. We appear to have reached the natural limits of these policies as consumers are no longer willing to accumulate more debt to absorb these surpluses, even with interest rates close to zero. While governments have been quick to pick up the baton, in many cases they are also now fully committed.

As the effectiveness of such stimulatory policy wanes, markets have become more exposed to the underlying deflationary forces at play. We are transitioning from a reflation cycle that has reached its natural limits to a classic debt deflation cycle where these imbalances are unwound.

The reflation cycle has initially played out in developed markets (DM) before being exported to Emerging Markets (EM) as excess liquidity looks for a home. The Bank of England's chief economist, Andy Haldane, has identified three clear waves in this cycle: "The first ended in the 'Anglo-Saxon' crisis of 2008-09. Part two was the 'euro-area' crisis of 2011-12. And we may now be entering the early stages of part three of the trilogy, the 'emerging market' crisis of 2015 onwards." History has shown that a rapid accumulation of foreign currency denominated debt in EM ends badly.

Given the weak growth backdrop in DM, and with fewer investment opportunities in the western world, capital has moved eastward in search of yield. The prime example would be China, where overall debt has risen to 229% of GDP – an increase of 50% in just 6 years. In **Fig 1** you can see how leverage has increased for companies in EM (mainly via US dollar borrowings).

**Leverage has increased across emerging markets** **FIG 1**




Source: BIS

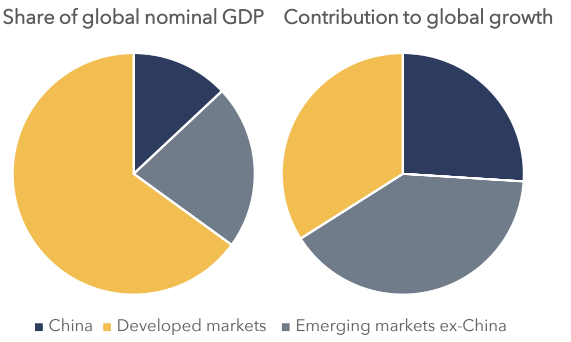
As the liquidity tap runs dry with the end of quantitative easing (QE) and the threat of rate normalisation emerges, capital flows are reversing out of EM and being repatriated home. This, along with an improvement in the US current account driven by shale oil production, has driven the US dollar sharply higher. The end result is a tightening in financial conditions for those foreign entities that have borrowed in US dollars. Credit spreads have also blown out in recognition of the elevated leverage and stress, as seen in **Fig 1**.

The importance of capital flows into emerging markets in bolstering global demand is clear from their contribution to overall growth. In the last three years, DM have inched along at just 1.7% growth on average each year, with EM contributing the vast majority of global economic expansion.

**Fig 2** shows that while EM constitutes just one third of the global economy, it contributes two thirds of the growth – with China alone accounting for 26%. Simply put, global growth is coming first and foremost from EM, and EM are experiencing a rapid slowdown as financial conditions tighten and commodity prices fall.

EM contribute most to global growth

FIG 2




Source: IMF data

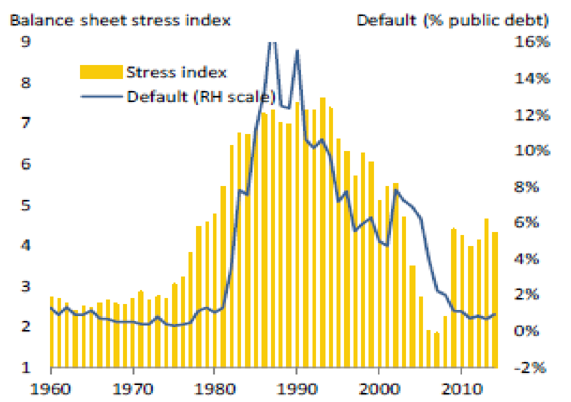
Global growth will slow further in the period ahead unless we see a miraculous acceleration in DM growth, which we believe is unlikely given we are already six years into the current business cycle. The credit expansion which has pushed growth above its natural level has given rise to balance sheet imbalances that will now have to be unwound, resulting in softer growth for some time.

Harvard professor Carmen Reinhart summaries it as such: “EM are seeing a significant slowdown in economic growth and exports, the unwinding of asset-price booms, growing current-account and fiscal deficits, rising leverage and a reduction or outright reversal in capital flows”.

She goes on to suggest that with every financial crisis there are hidden debts and asked the question: “where are the hidden debts in emerging markets?” The opacity of financial transactions and reported data would suggest that the indebtedness is understated and the reversal in capital flows may create more stress than is being considered. As **Fig 3** indicates, stress levels are rising quickly but have not yet manifested in elevated defaults, which are clearly going to rise and increasingly weigh on growth.

Emerging market stress vs. default incidence

FIG 3




Source: Emerging Advisors

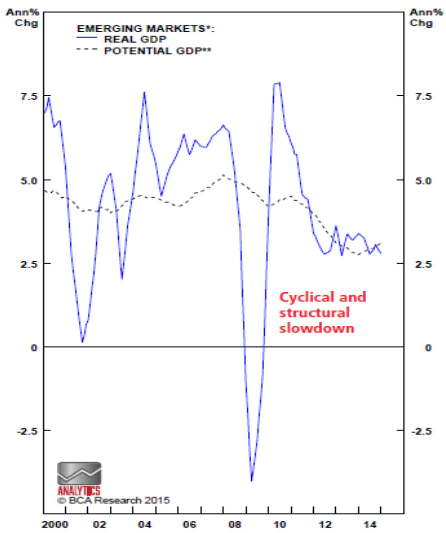
In a sense, this policy has been the reaction to an excess of savings over investment, particularly in China, Japan and Europe, with surplus capacity as the outcome. Such a gap has created further downward pressure on interest rates, pushing them below the natural rate. Lower costs of funding have led to inefficient investment decisions and capital misallocation. While investment funded by cheap debt may add to GDP in the short term, as incremental investments become less and less productive with the capital misallocation that has occurred, the debt servicing capacity of this investment diminishes. This can be seen in China – as the incremental return on investment has reduced, debt has grown well in excess of the capacity to service it.

Further accumulation in debt ultimately becomes unsustainable unless the growth in credit moderates. A sustained “credit gap” between credit growth and debt servicing capacity must at some stage be closed by reducing excess credit, and this can create significant stress on borrowers. Brazil, Thailand, and Turkey are all running large credit gaps in addition to China.

Furthermore, the DM are not alone in seeing a structural slowing in growth. In **Fig 4**, BCA Research have modelled this same trend in EM, being a consequence of lower productivity and capital efficiency. They conclude that: “The lack of supply side reform and political complacency has seen a sharp fall in productivity across EM”.

Potential GDP growth has declined across EMs

FIG 4



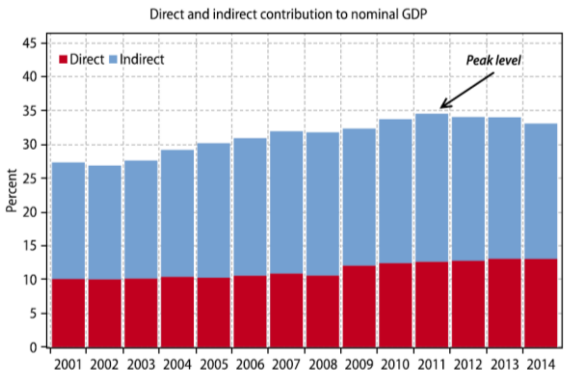

Source: BCA Research

Arthur Budaghyan at BCA has a rather sobering view of how it plays out: “EM policymakers will be incapable of enacting genuine structural reforms without more pain. An economic, market, and quite possibly socio-political bloodbath will be required to force EM policymakers into action.”

Turning to China, which is the largest single contributor to global growth: we would expect to see some stabilisation in recently decelerating industrial activity, as the effects of easier domestic credit conditions and further fiscal stimulus begin to be felt through the economy. We are not expecting a miraculous recovery next year however, as the housing and construction sectors are likely to slow further which will weigh on overall growth.

**Fig 5** portrays the importance of building and construction's contribution to the Chinese economy.

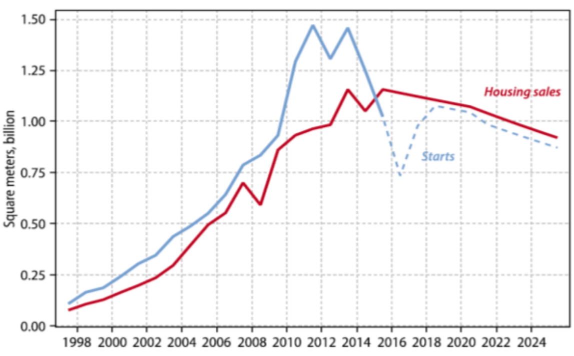
Construction & real estate contribution to China GDP has peaked **FIG 5**




Source: NBS, CEIC, Gavekal

It is hard to envisage an uptick in growth in China without the participation of the property sector. Construction starts, which fell sharply in 2015, are likely to fall further in 2016 as excess housing inventories – which currently stand at 30 months of supply – are worked through. A cyclical rebound is unlikely before 2017.

Construction starts must correct to get back in line with demand **FIG 6**



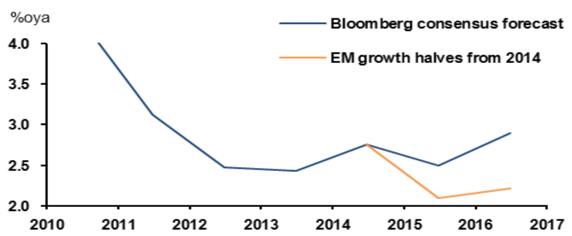

Source: CEIC, Gavekal

A view of EM is central to any global growth outlook. The aforementioned tightening credit conditions and falling commodity prices are causing a sharp deceleration in EM activity. While we are unlikely to see a replay of the late 1990s Asian crisis, growth will be slower in the medium term.

In **Fig 7** below we have run a scenario where DM continue to grow at 1.7% p.a. while growth across EM halves. This is a reasonable base case for China at least, the largest contributor in the group, where growth of 3-4% in 2016/2017 looks more reasonable than what official reports might suggest.

Given we also expect commodity prices to remain depressed for some time, key commodity exporters such as Russia and Brazil are unlikely to recover in a hurry. This base case scenario will see 'real' global growth below where it has been in recent years. In 'nominal' terms the deceleration will be even more pronounced, as deflationary forces reassert themselves.

Global growth simulations **FIG 7**




Source: JP Morgan

With global growth slowing and policy makers running out of options, key share markets are again looking fully valued after having recovered from recent losses.

As we have discussed in previous issues of *The Leading Edge*, Australia faces its own challenges as it transitions out of the mining boom. Our base case is for the Australian economy to muddle through, with softer growth being the order of the day. A new Coalition frontbench has bolstered business confidence, and household spending is holding up quite well despite weaker income trends.

Many of the structural challenges confronting key industrial sectors that we have discussed recently were evident in the quarter. Heightened competition in banking, retail and telecom have seen downgrades among listed companies operating in these industries. The 'magnificent 7' industrial companies (four major banks, Woolworths, Wesfarmers and Telstra) are all struggling.

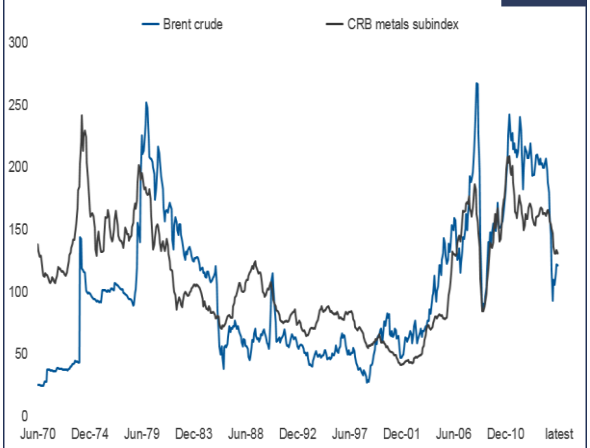
Against this backdrop of weaker growth, elevated risks and full valuations, we retain our short net exposure to the Australian share market in our directional funds. Time will tell whether the recent sell-off marked the start of a new down cycle or merely a setback amidst an ongoing expansion. Either way, offshore markets are not far off their highs of this cycle, so the risks to us appear to be on the downside.

## Feature article: Outlook for commodity prices

Commodity prices have continued to grind lower in 2015 after precipitous falls early in the year. While the mining boom is clearly over, investors are asking "where to next for commodity prices?" To help frame our thinking we decided to put the recent rout in a historical context.

**Fig 8** is a 50 year history of the price for oil and a range of metals adjusted for inflation. It shows that during most of this period real commodity prices actually fell. As with many industries, mining and energy have seen continual technical advancement. Through innovation, costs for the industry generally decrease in real terms and prices in a balanced market tend to follow cost support. It is also clear in **Fig 8** that from the turn of the century prices have rallied. This naturally brought in new high cost supply to meet China's insatiable demand for raw materials. However, after a 12 year period of rising costs and increasing prices, we are now seeing a rapid unwind of cyclical cost inflation. In an oversupplied market, prices have in many instances fallen below the cost of production.

Prices deflated by US CPI, 1984-2014 avg = 100 **FIG 8**

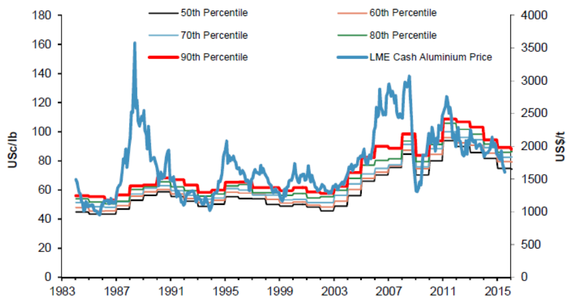



Source: Macrobond, US BLS, LSR

In predicting where commodity prices will head we must examine the cost curve for individual commodities (i.e. the cost profile for each unit of production across the industry). It is important to understand that in all periods other than through boom times, prices tend to track cost support.

In **Fig 9** we show a long term price chart for aluminium. It also includes the 50th to 90th percentiles on the cost curve. The chart highlights that for most of the last 30 years, prices traded at cost support. Over the last decade, prices moved higher to incentivise new supply. However as this demand impulse faded and markets became fully supplied, again prices have moved back to cost support. The key question now is how far costs will fall. It's worth noting that this relationship between production costs and prices holds true for any commodity.

Aluminium cash costs vs. price **FIG 9**

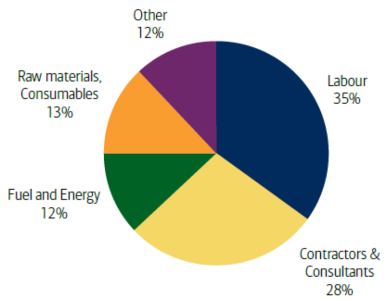



Source: Wood Mackenzie, Bloomberg, Morgan Stanley

## Cost deflation

The cost structure for a mining company is fairly straightforward. Labour, fuel (largely oil), consumables, tax and royalties account for the majority of costs. **Fig 10** shows a cost breakdown of BHP's iron ore business, with labour comprising roughly half of the costs.

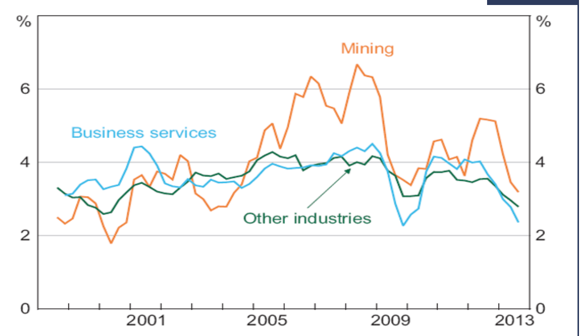
Cost breakdown in BHP's WA iron ore business **FIG 10**




Source: Company data

Truck drivers in the Pilbara were routinely receiving $300kpa, as the mining industry was challenged by a skills shortage that resulted in rampant wage inflation (**Fig 11**).

Wage growth by industry **FIG 11**




Source: ABS, RBA

This cyclical inflation has begun to reverse. While outright pay cuts are difficult to achieve in the short term, Fortescue Metals recently announced a change to their workforce roster. Workers on Fly-In-Fly-Out (FIFO) basis previously enjoyed 8 days on and then 6 days off, but with the iron ore price collapsing this has shifted to 14 days on and 7 days off. Other measures such as employing non-unionised contractors have contributed to labour cost reductions across the industry.

Importantly, commodities are priced in US dollars. Key mining regions such as Australia, Brazil and Canada have seen their local currencies depreciate significantly as the Chinese economy has slowed. Such currency devaluation has further reduced the US dollar cost structure for mines in these regions. Combined with lower energy costs and royalties, costs have already fallen meaningfully.

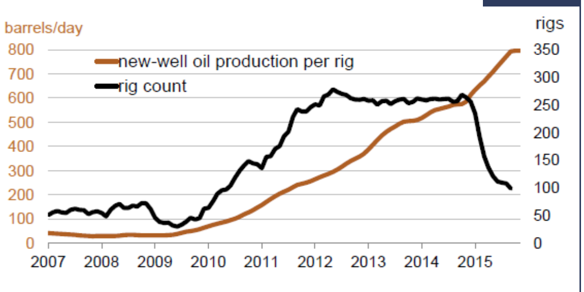
We expect these deflationary forces to continue, pushing prices lower toward cost support, where they have resided historically.

## Oil

In last December's edition of *The Leading Edge*, we explained OPEC's strategy to increase supply and squeeze high-cost shale producers. However, as with many disruptive technologies, productivity continues to improve – further lowering the cost of oil for shale companies.

**Fig 12** shows that while we have seen a marked drop-off in the rig count in the key US basin, Eagle Ford, oil production per rig has continued to rise. Overall US oil production has thus remained relatively unchanged. Shale companies now produce more oil with two rigs than they did just a few years ago with three. This rapid increase in efficiency has surprised many.

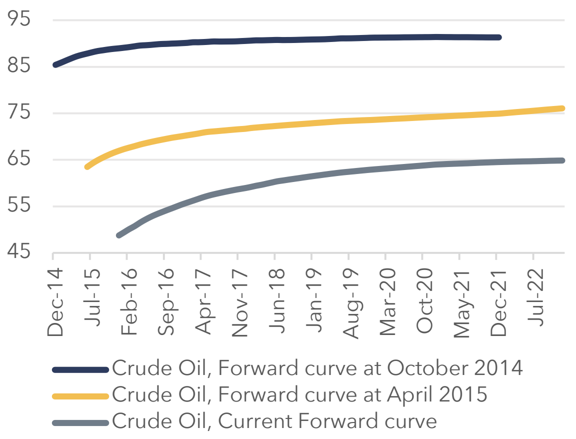
New-well oil production per rid vs. rig count in Eagle Ford — FIG 12




Source: EIA

The Saudi central bank commented in a recent stability report: "It is becoming apparent that non-OPEC producers are not as responsive to low oil prices as had been thought, at least in the short-run". The net effect has been to lower the oil cost curve and equilibrium prices further. The forward curve for oil is determined in a highly liquid market where sellers and buyers agree on future prices. The current forward curve is $10 per barrel lower than just six months ago, and $25 lower than one year ago (**Fig 13**).

Change in the forward curve for Brent oil (US$/barrel) — FIG 13



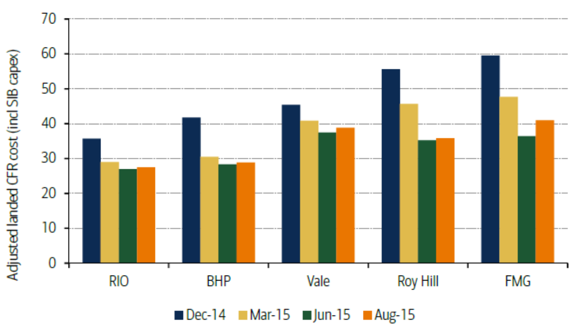

Source: Bloomberg

It's worth noting we believe the current forward curve is a good representation of the medium-term path for the oil price.

## Bulk commodities

We have written previously of our dour outlook for both coal and iron ore. Weak demand coupled with significant new low-cost supply has driven prices much lower. However the impact on the cost curve has been even more dramatic than we anticipated. **Fig 14** depicts the reduction in "breakeven" iron ore prices for five key producers in just one year. These reductions are due to lower currencies, both the Australian dollar and Brazilian real, as well as labour, fuel, mine planning and royalties.

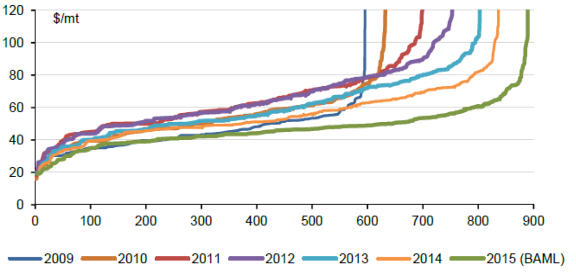
Trends in 'breakeven' seaborne iron ore prices — FIG 14




Source: BofA Merrill Lynch

It is remarkable to see the cost deflation in this industry in the absence of any technological breakthrough like the one that has transformed the oil industry. Coal markets are arguably further into this downturn than other commodities and the changing cost curve is also quite dramatic (**Fig 15**).

Seaborne thermal coal cost curve **FIG 15**




Source: BofA Merrill Lynch

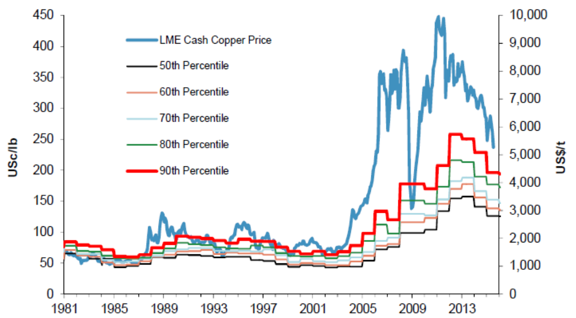
Global demand is set to remain weak for some time given our view on EM growth, and with further cost reductions to come, we expect prices for most commodities will stay low for many years ahead.

## Copper

Until recently most investors felt the copper price would defy these trends. Copper miners are facing similar deflationary pressures. While we acknowledge that long term grades (density of copper in the rock) are declining – which will support the copper price – the impact is small relative to the super cycle we have witnessed.

**Fig 16** shows that copper prices and costs came down in real terms from 1980 through to 2000. We had weak demand, including a recession in the early 1980s, and consistent supply from the emergence of new technologies including solvent extraction and electrowinning. Prices generally stayed between the 80th and 90th percentile on the cost curve. If we contrast this to the boom period thereafter, prices only briefly touched the upper end of the cost curve in the GFC.

Copper cash costs vs. price **FIG 16**



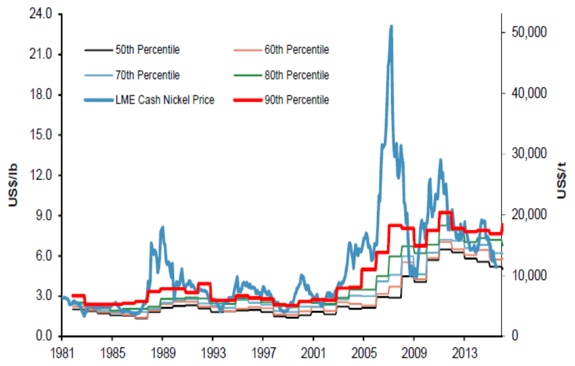

Source: Wood Mackenzie, Bloomberg, Morgan Stanley

Our concern for copper is that in a forthcoming period of weak demand, prices are likely to head to cost support, suggesting more downside. We were alerted to this disconnect between the copper price and its cost of production back in May and initiated short positions in two highly leveraged copper producers: Glencore and First Quantum Minerals. These positions have been highly profitable for the fund as expectations for copper have fallen.

## Nickel

Chinese manufacturers developed a new nickel pig iron (NPI) smelting technology back in 2007 in response to rapidly rising prices. NPI is a low grade ferronickel utilising laterite nickel ores instead of the more scarce pure nickel. Such innovation in metallurgy has altered the industry and lowered the cost curve. In January 2014 Indonesia banned the export of unprocessed ore. This was a major source of feed for the Chinese NPI industry and was expected to result in a significant reduction in NPI, so nickel prices rallied in anticipation. Contrary to expectations, prices halved as Filipino ore was substituted and inventories built up ahead of the export ban, which saw a collapse in nickel prices.

Nickel cash costs vs. price **FIG 17**




Source: Wood Mackenzie, Bloomberg, Morgan Stanley

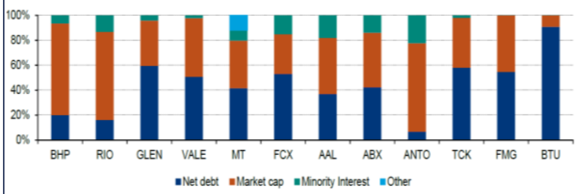
Prices are now deep into the cost curve. Based on Wood Mackenzie data, half of the global industry is now losing money. This position is clearly unsustainable, but nickel miners are holding fast with only minimal production cuts so far. The longer prices remain low, the more likely we will see a meaningful supply response. Glencore has taken capacity reductions in coal, copper and zinc already this year. It would not surprise us if they made a similar announcement on nickel in the near future. We are more positive on the medium term outlook for nickel with limited downside to the price given cost support. Our preferred exposure is Independence Group.

## Zombie mining companies

Rapid expansion in China over the past decade has led to a credit-fuelled boom across the mining industry. As commodity prices have moved sharply lower, many of the companies that expanded aggressively with debt are now financially unviable. Amid very low interest rates we end up with insolvent structures that are unresolved. This was the case with the Japanese banks in the 1990s. Without resolution, these zombie banks became a major overhang to the Japanese economy. We may see a similar outcome in mining, where rebalancing does not occur as quickly as it should, weighing on the industry for years to come.

Enterprise value breakdown normalised to 100%

FIG 18




Source: BofA Merrill Lynch

Peabody Energy (on the far right of Fig 18 as "BTU") is a great example. With a market capitalisation of $270 million and debt of over $6 billion it is clear that this company is insolvent. Its creditors are not inclined to close mines and take losses; rather they are incentivised to increase production, and service their loans at extremely low interest rates. We have similar examples here in Australia too. Atlas Iron recently went into a trading halt only to re-emerge with $30 million in debt and a large reduction in costs with its contractors working for no profit. This persistent supply becomes a deadweight on the industry, making it hard for the industry to rebalance. If these insolvent structures are left unsettled, the down-cycle will be extenuated.

While the price adjustment seen in commodity markets have been large already, weak demand, deflationary impacts and unsustainable debt positions may require further price falls if markets are to rebalance. Hence, we believe that it is still too early to consider going long the mining sector.

## Performance Review

Watermark funds performed strongly during the September quarter. By virtue of their ability to hedge market risk, the Funds have historically done well when markets fall, providing returns that are uncorrelated with the share market. This was particularly evident in August, where all funds rose in value by 3% or more, while the share market suffered its worst monthly fall since the GFC.

In order to derive a positive return from a long/short investment strategy, the long portfolio of shares must outperform the portfolio of shares that have been sold short. While the gross value of Watermark's long portfolios fell marginally during the quarter, the short portfolios fell by in excess of 13%, delivering a positive spread for the Funds. This illustrates clearly the objective of a long/short investor with a bias to quality and value. With a long portfolio comprised of high quality businesses, the Funds are outperforming in a weak market. A short portfolio built around weaker businesses will tend to underperform during periods of market weakness as investors sell down what are perceived to be riskier shares. This clear quality bias in portfolio construction sees our funds tending to do well when markets fall.

As has already been discussed in this newsletter, the mining and energy sectors suffered particularly large falls during the quarter. The Funds were well-positioned to benefit from these moves and short positions in mining and energy companies were amongst the strongest contributors to performance. With the prices of many commodities having fallen precipitously over the past 12 months, prices are in many cases at cost support, suggesting that downside for mining shares is limited. Balance sheet strength will be a differentiating factor for mining companies, while commodity prices remain low and markets over-supplied. We continue to look for winners and losers across the commodity complex, allowing us to profit from relative moves within the sector while maintaining an overall hedged position.

The financial sector was another strong source of performance during the quarter. We have written extensively on the challenges facing the Australian banks. Sustained pressure from APRA to raise levels of capital finally saw each of the major banks launch initiatives in order to strengthen their capital position. While this was one factor weighing on bank shares in the quarter, of equal concern was mounting evidence that the credit cycle is turning and that the headwinds for profits are building. Our short exposure to banks resulted in solid performance as these themes played out.

Volatility creates opportunity for an active long/short investor. We are expecting more volatility ahead as interest rates normalise and debt imbalances are resolved. Given this environment, alternative investment strategies will play an increasingly important role in preserving capital when share markets fall, providing genuine diversification.

## Company at a Glance – Sept 2015

| | |
|---|---|
| ASX Code | ALF |
| Fund Size | AU$361m |
| Fund Strategy | Variable Beta |
| Share Price | $1.44 |
| NTA Before Tax | $1.42 |
| Shares on Issue | 256.3m |
| Dividend (1H15) | 5 cents |
| Dividend Yield (annualised) | 7.6 % |

## Net Tangible Asset (NTA) Backing

| | Aug 15 | Sept 15 |
|---|---|---|
| **NTA Before Tax** | **$1.40** | **$1.42** |
| NTA After Tax | $1.39 | $1.41 |
| Dividend Declared | ($0.05) | ($0.05) |
| **NTA After Tax & Div (5₵)** | **$1.34** | **$1.36** |

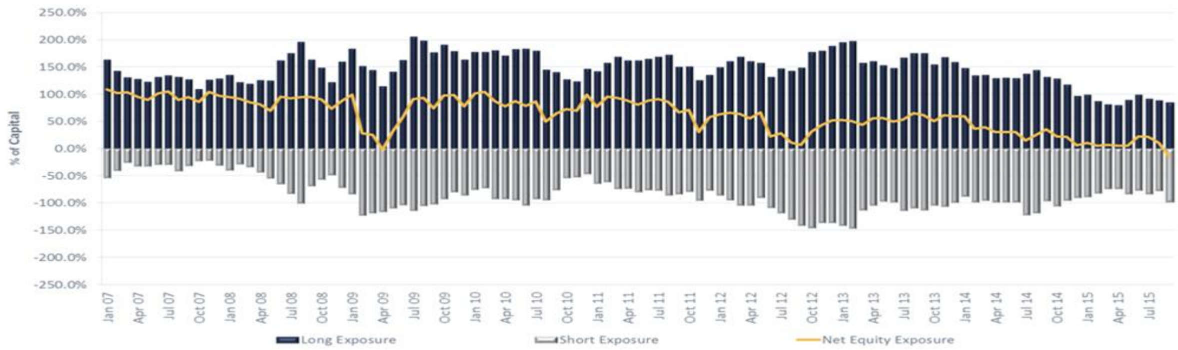
## Gross Portfolio Structure

| | Aug 15 | Sept 15 |
|---|---|---|
| Long Exposure | 88.9% | 85.5% |
| Short Exposure | -78.9% | -99.3% |
| Gross Exposure | 167.7% | 184.7% |
| Cash | 90.0% | 113.8% |

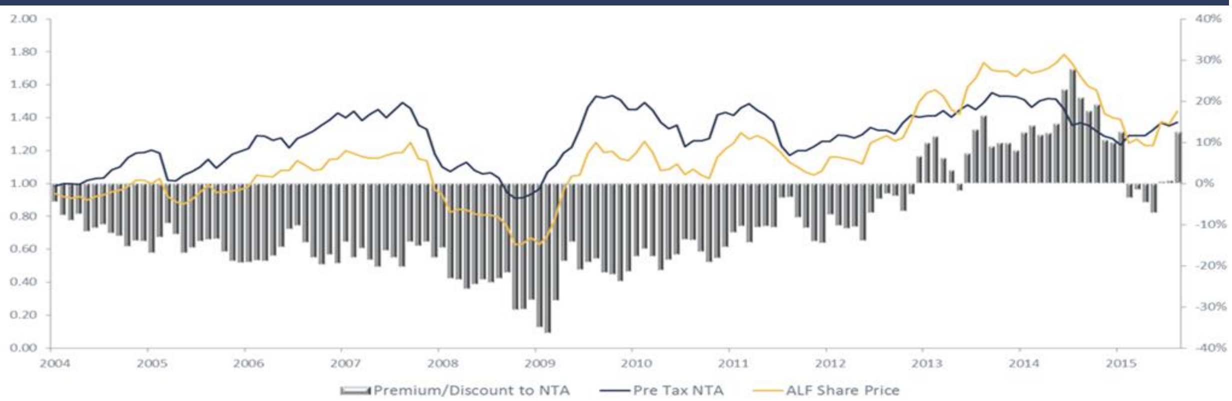
## ALF Performance

| | 1 Mth | 6 Mths | 1 Yr | 3 Yrs (pa) | 5 Yrs (pa) | 7 yrs (pa) | S.I. (pa) |
|---|---|---|---|---|---|---|---|
| Portfolio Return (net) | 1.5% | 12.2% | 9.8% | 16.5% | 15.2% | 16.8% | 14.6% |
| All Ords Accum Index | -2.5% | -11.7% | -0.2% | 9.3% | 6.3% | 5.8% | 8.3% |
| Outperformance (net) | 4.0% | 23.9% | 10.0% | 7.2% | 8.9% | 11.0% | 6.3% |

## Net Equity Exposure




## Historical Premium/Discount to NTA History



WATERMARK FUNDS MANAGEMENT

# Market Neutral Trust

APIR: WMF0001AU

## Fund at a Glance – Sept 2015

| | |
|---|---|
| Fund Size | AU$38.1m |
| Strategy FUM | AU$129.3m |
| Fund Inception Date | August 2012 |
| Fund Strategy | Equity Market Neutral |
| Application/Redemption | Daily |
| Management Fee | 1.5% |
| Performance Fee | 20% |
| Benchmark | RBA Cash Rate |

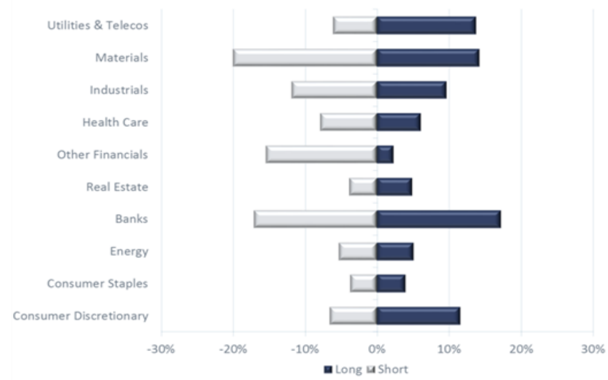
## Return Characteristics[1]

| | |
|---|---|
| Positive Months | 71.05% |
| Portfolio Beta | -0.28% |
| Sharpe Ratio | 1.82 |
| Sortino Ratio | 5.36 |
| Standard Deviation | 7.92% |
| No. Long Positions | 57 |
| No. Short Positions | 64 |
| Gross Exposure | 186.8% |

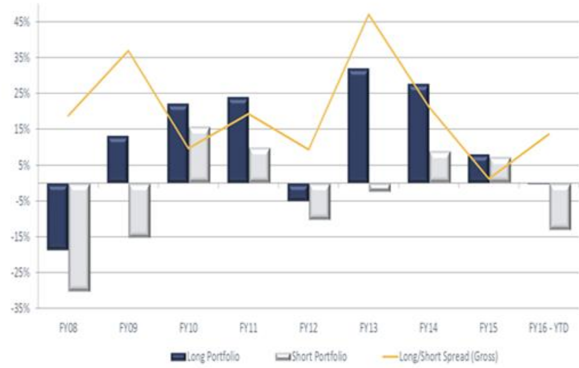
## Performance[2]

| | 1 Mth | 6 Mths | Fin. YTD | 1 Yr | 2 Yrs (pa) | S.I (pa) |
|---|---|---|---|---|---|---|
| WMNT (net return) | 2.7% | 15.1% | 11.0% | 13.1% | 9.1% | 17.7% |
| RBA Cash Rate | 0.2% | 1.0% | 0.5% | 2.3% | 2.4% | 2.7% |
| Outperformance | 2.5% | 14.1% | 10.5% | 10.8% | 6.7% | 15.0% |

## Sector Exposures




## Long/Short Spread[3]




## Monthly Net Performance (%)

| Cal. Yr | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | Annual |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 2012 | - | - | - | - | - | - | - | 1.36 | 0.97 | 0.00 | 6.51 | 2.88 | - |
| 2013 | -0.71 | 0.21 | 4.60 | 1.55 | 5.83 | 5.31 | 1.11 | 2.57 | 1.43 | 1.86 | 0.35 | -0.06 | **24.05** |
| 2014 | 1.71 | 1.45 | -1.17 | 2.80 | 1.21 | 0.84 | -4.38 | -1.77 | 2.52 | -1.57 | -1.58 | -1.32 | **-1.26** |
| 2015 | -1.18 | 0.70 | 3.23 | 0.96 | -0.61 | 3.39 | 3.82 | 4.04 | 2.73 | | | | - |

[1] Return Characteristics are in relation to the market neutral strategy using long/short return series recorded from April 2008

[2] Performance data is net of all fees and expenses. The Fund's inception date is August 2012

[3] Long/Short spread shows the gross performance of the long and short portfolios. The Fund makes a profit where the long portfolio outperforms the short portfolio, after the payment of fees. Returns prior to the Fund's inception date are based on return series from the long and short portfolios of the Australian Leaders Fund Ltd in a market neutral structure

# Watermark Market Neutral Fund Ltd

## Company at a Glance – Sept 2015

| | |
|---|---|
| ASX Code | WMK |
| Fund Size | AU$91.2m |
| Fund Strategy | Equity Market Neutral |
| Share Price | $0.98 |
| NTA Before Tax | $1.09 |
| Shares on Issue | 84.1m |
| Dividend (1H15) | 2.5 cents |
| Dividend Yield (annualised) | 4.6% |

## Net Tangible Asset (NTA) Backing

| | Aug 15 | Sep 15 |
|---|---|---|
| **NTA Before Tax** | **$1.06** | **$1.09** |
| NTA After Tax | $1.05 | $1.07 |
| Dividend Declared | ($0.025) | ($0.025) |
| **NTA After Tax & Div (2.5₵)** | **$1.02** | **$1.05** |

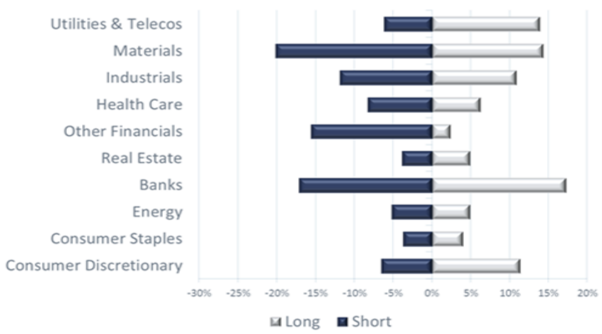
## Gross Portfolio Structure

| | Aug 15 | Sep 15 |
|---|---|---|
| Long Exposure | 85.0% | 89.8% |
| Short Exposure | -87.8% | -99.2% |
| Gross Exposure | 172.8% | 188.9% |
| Cash | 102.9% | 109.4% |

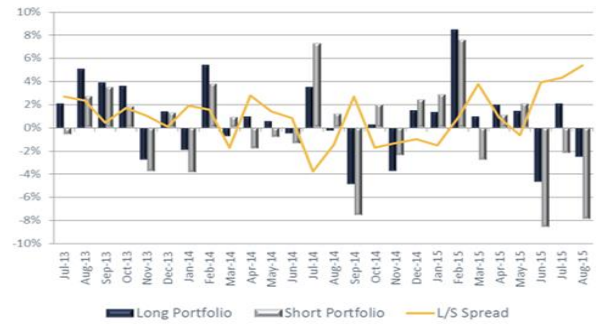
## WMK Performance

| | 1 Mth | 6 Mths | 1 Yr | S.I. (pa) |
|---|---|---|---|---|
| Portfolio Return (net) | 2.63% | 14.74% | 12.65 % | 9.30% |
| RBA Cash Rate | 0.17% | 1.03% | 2.26% | 2.42% |
| Outperformance (net) | 2.47% | 13.71% | 10.39% | 6.88% |

## Sector Exposures

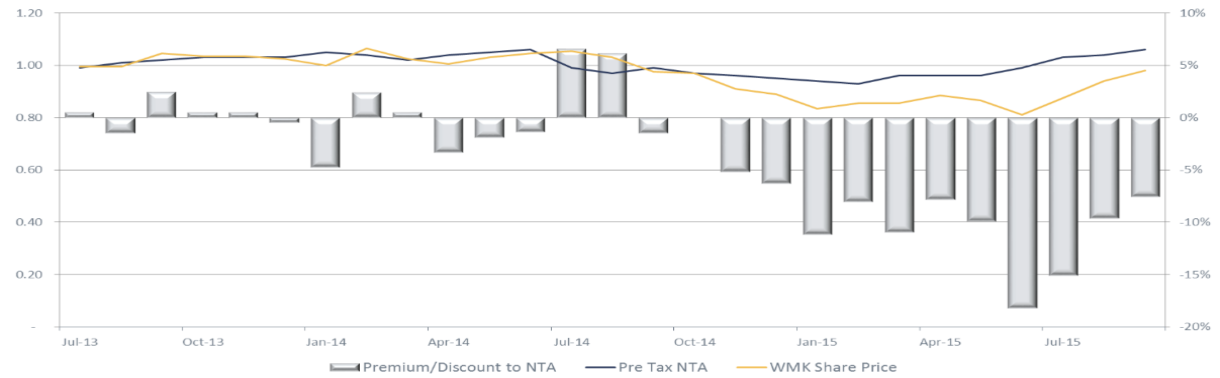



## Long Short Spread*




* Long Short spread shows the gross monthly performance of the Company's long and short portfolios. The difference between the two represents the gross performance of the portfoio as a whole. The company will make a profit where the long portfolio outperforms the short portfolio, after the payment of fees and expenses

## Historical Premium/Discount to NTA



## Notes

## Notes

WATERMARK
FUNDS MANAGEMENT

Level 6, 139 Macquarie Street, NSW Sydney 2000

TEL (02) 9252 0225 • FAX (02) 9252 1220 • info@wfunds.com.au • www.wfunds.com.au