



**WATERMARK**  
MARKET NEUTRAL FUND

# Watermark Market Neutral Fund Limited

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**ABN 45 163 980 498**

## Annual Report 2016

YEAR ENDED 30 JUNE 2016

Watermark Market Neutral Fund Limited  
Level 6, 139 Macquarie Street NSW Sydney 2000

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**Watermark Market Neutral Fund Limited**  
**Corporate directory**

**Directors**

Matthew Kidman  
*Chairman*

Justin Braithling  
*Non-Independent Director*

John Abernethy  
*Independent Director*

Stephen Van Eyk  
*Independent Director*

Robert Ferguson  
*Independent Director*

**Company secretary**

Matthew McShane

**Registered office**

Level 6  
139 Macquarie Street  
Sydney NSW 2000  
Phone: (02) 9252 0225  
Fax: (02) 9252 1220  
Email: [info@wfunds.com.au](mailto:info@wfunds.com.au)

For enquiries regarding net asset backing (as advised each month to the Australian Securities Exchange) refer to [www.asx.com.au](http://www.asx.com.au) or call (02) 8262 2800.

**Share registrar**

Boardroom Pty Limited  
Level 12  
225 George Street  
Sydney NSW 2000  
Phone: (02) 9290 9600  
Fax: (02) 9223 1762

For enquiries relating to shareholdings, dividends (including participation in the Dividend Reinvestment Plan) and related matters, please contact the share registrar.

**Auditors**

Pitcher Partners  
Level 22 MLC Centre  
Sydney NSW 2000  
Phone: (02) 9221 2099

**Securities exchange listing**

Australian Securities Exchange (ASX)  
The home exchange is Sydney.  
ASX code: WMK Ordinary shares

# **Watermark Market Neutral Fund Limited** ABN 45 163 980 498

## **Annual Report - 30 June 2016**

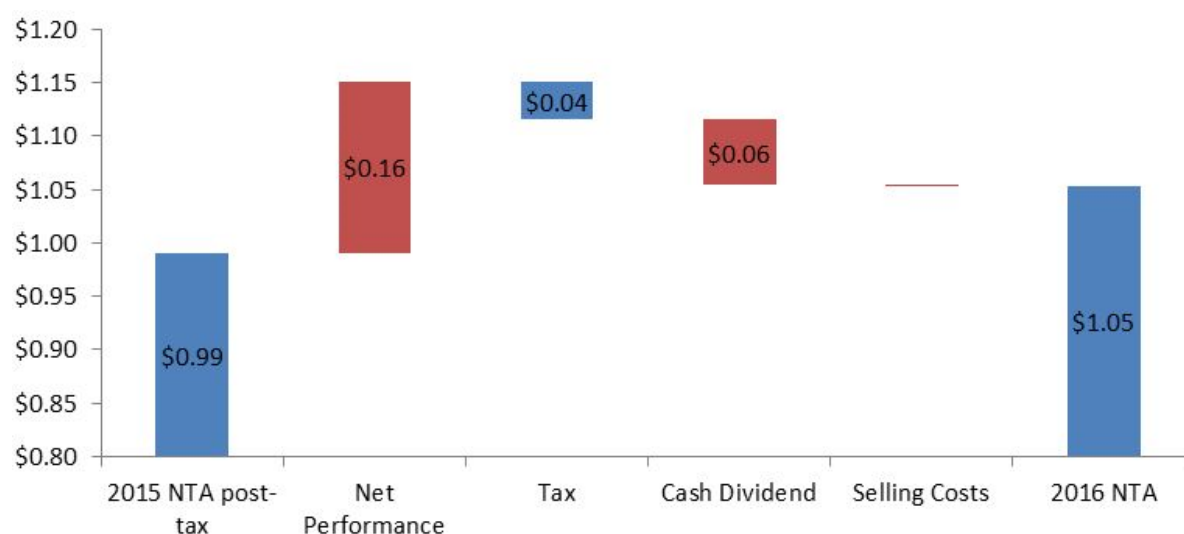
### **Contents**

	Page
Chairman's Letter	1
Chief Investment Officer's Report	3
Company Profile	5
Investments at Market Value	7
Corporate Governance Statement	8
Directors' Report	9
Auditor's Independence Declaration	21
Financial Statements	
Statement of Comprehensive Income	22
Statement of Financial Position	23
Statement of Changes in Equity	24
Statement of Cash Flows	25
Notes to the Financial Statements	26
Directors' Declaration	53
Independent Auditor's Report to the Members	54
Shareholder Information	56

## Chairman's Letter

Watermark Market Neutral Fund (WMK) reported strong profit growth for the period ending June 30 2016 with after tax profit rising from a loss in FY15 of \$753,232 to \$10.6 million. As at the 30 June, the after tax net tangible asset backing (NTA) of WMK was \$1.05 per share, up from \$0.99 at the prior year end. The Company paid 5 cents of partially franked dividends in the period and a special dividend at the half year of 1 cent per share. By virtue of its market neutral investment strategy, WMK can generate investment returns independent of the prevailing direction of share markets. As such, the Investment Manager was able to deliver a very strong result in a difficult year for the Australian share market.

Figure 1. NTA Bridge



The Company's investment portfolio performed strongly in FY16, increasing in value by 22.3% before fees and costs. This is compared with the All Ordinaries Accumulation Index which increased by 2%, with all of the return coming by way of dividends which offset a negative capital return for the period. With the outlook for shares domestically and abroad increasingly uncertain, the value of an investment strategy that provides scope to hedge out share market risk will be starkly realised, with little or no net exposure to the overall share market at any point in time.

Since inception, the gross value of the portfolio has increased by 43.5% while the benchmark RBA Cash Rate has increased by 7%. The investment process has added 36.4% to the value of your Company (before fees and expenses). The Board has endeavoured to return a significant portion of this to shareholders via ordinary and special dividends (13c paid to date; 15.5c declared to date).

The 2015 financial year was a difficult one for WMK. After weaker than normal performance, the Company's shares slipped to a discount to NTA, notwithstanding a stronger second half of FY15. The share price rebounded strongly in the 2016 new financial year and continued to perform well, appreciating by 23.8% over the course of the year. The shares have consistently traded at or around NTA in recent months.

Having generated solid returns from its investments in international shares, the Investment Manager has validated the Board's decision in December 2014 to extend the Company's investment mandate to allow for investments in offshore markets. In recognition of the value that has been created the board has lifted the limit on international shares further to up to 50% of the balance sheet.

The Australian share market rose again in FY16 as the global deflation cycle continued, spurred on by ultra-easy monetary policy from central banks around the world. Notwithstanding this continued support for risk assets such as shares, weak global growth has led to brittle recoveries in many developed economies, with risks weighing heavily on investor sentiment.

As we enter the early stages of what will be a prolonged period of normalisation in interest rates around the world, the medium-term outlook for global share markets is unclear and risks remain. It is clear however, from economic data and anecdotal information from Australian companies, that top line growth will be subdued and that we are in a low-return environment for shares for some time.

Your Company is well positioned to deal with the prevailing market conditions. By virtue of its ability to hedge share market risks, WMK offers protection against a major set-back in the share market. With lower returns expected from shares in the medium term, an investment strategy such as that employed by WMK will be more relevant than ever, as a means to average up returns while reducing volatility.

Matthew Kidman  
Chairman

Dated at Sydney 16 August 2016

## Chief Investment Officer's Report

The first half of FY16 saw the portfolios maintain their strong performance, even as share markets globally lost ground. Whilst conditions for long/short investors turned more challenging in the new calendar year, portfolio returns were stable and the solid performance continued. The Fund delivered a strong net return of 16.2% for the full year to June 30 2016.

Our endeavours in international shares have continued to make strong a strong contribution to Fund returns. Having remained relatively constant at 10-12% of our gross balance sheet for much of 2015, international exposure was increased in the 3rd quarter as new investment ideas in international shares were incorporated into the portfolios. Having approached our 20% limit by the end of 2015 and with more opportunities presenting themselves, the Board's resolution to increase the limit for international investments provided scope to incorporate successful investments in companies such as *Group Eurotunnel* and *Merck & Co*. International shares contributed 14% of the Fund's gross portfolio return in FY16 and importantly, our international research continues to yield deeper insights into our investigation of Australian companies.

Global share markets were volatile for the most part in FY16, although there were several key themes presenting both challenges and opportunities through the period. Mining and energy shares continued to come under pressure, with sustained falls in the price of most commodities, in particular oil, bulk commodities and certain industrial metals. These sectors led the market lower in the first half of the year, before renewed stimulus in China led to a surprise improvement in demand and a sharp, counter-cyclical rally.

The domestic banking sector was another part of the market that saw significant falls in the first half. Australian banks in particular came under pressure as APRA announced new policies in respect of the Banks' capital strength, with most forced into repeated capital management initiatives. Coupled with weak earnings trends and increased default rates in their corporate loan books, the major banks now face the daunting prospect of cutting dividends.

The RBA has been walking a tightrope for some time, balancing effervescent residential property prices on the east coast of Australia, with the deflationary effects of the mining downturn and a general lethargy in the industrial economy. Property-related sectors such as building materials and discretionary retail have been significant beneficiaries of these trends providing rare pockets of growth. The RBA's hand was forced in the second half, with rate cuts designed to stave off looming deflationary pressures trends and to devalue the resilient Australian dollar. Nevertheless, it is difficult to see further appreciation in property prices form here, and with household income stalling, we see risks ahead for many of the industries than have benefitted from these favourable trends.

Defensive shares were a strong contributor to performance in the period. The healthcare sector performed particularly well as a weight of funds flowing out of banks and miners forced prices of many market darlings sharply higher, pushing valuations to extreme levels. Short positions in a number of expensive, weaker businesses performed well through the year. We have held a negative view of the major Australian grocery sector for some time, with both major players battling competition from discount retailers.

Fortunes have been mixed for cyclical shares over the last 12 months. Business and consumer sentiment has been subdued, given the weak outlook for global growth and the unstable political backdrop. There continues to be pronounced bifurcation within the media sector as winners and losers emerge in an evolving digital landscape. *Fairfax Media Ltd* is an interesting example of a company that had fallen out of favour with investors due to challenges for its traditional media business, which has nevertheless performed well as a result of its strong digital real estate franchise in *Domain*. FY16 also saw the demise of the recently listed *Spotless Group* and *Dick Smith Holdings*. Brought to market by their private equity owners, both companies were burdened with debt and had inexperienced management teams at the helm. This has been an all too common set up for corporate collapses in recent years and both were successful shorts for the Company in FY16.

The portfolios were well-positioned in the first half of FY16 for the downturn in banking shares. The capital impost imposed by APRA was clearly flagged and with bad and doubtful debts at all-time lows, the major banks looked vulnerable to a de-rating by the market. Given its poorly executed Asian strategy and the capital strain that it caused, a short position in *Australia and New Zealand Banking Group* made a strong contribution. An investment in *Smartgroup Corporation* was the best performer in the period, an example of a high quality IPO with strong prospects for growth.

Given the violent falls in mining and energy shares followed by a rapid rebound in February 2016, positions in this sector provided some of the largest individual contributions. The dramatic fall in the price of oil saw speculative developments in shale oil and natural gas post big losses. The Company's core short in *Liquefied Natural Gas Ltd* was the best performing short in the period. Short positions in *Glencore* and *First Quantum Minerals* also performed well as the price of copper fell. The lithium sector has enjoyed a resurgence in recent times, enjoying increases in demand with the electric vehicle revolution. The Company's investment in *Orocobre Ltd* was a beneficiary of this theme.

One clear trend in recent years has been the secular slowing in global growth. Shifting demographics, weak productivity, and deleveraging are all features of this deceleration. The precipitous fall in bond yields over the course of FY16 reflects this outlook, with many sovereign bond issues now trading below the zero bound. Our own 10 year Commonwealth government bond has slipped to 1.8%, fractionally above the cash rate. With the yield structure so flat and no carry or compensation for duration, it is hard to see any scenario where bonds can deliver anything but horrible returns in the medium term. Investors have been left with few choices, explaining the resilience of shares in the face of disturbing developments both politically and economically.

We feel more confident than ever in the merits of hedging strategies like those employed by Watermark. Bond yields are telling us the outlook for growth is as weak as it has been in a generation. There is no carry, a passive, buy and hold strategy will deliver low returns at best. Only an active strategy that can deliver enhanced returns through security selection stands a chance of delivering acceptable returns in this climate.

Justin Braitling  
Chief Investment Officer  
Watermark Funds Management

## **Company Profile**

### **Investment Objective**

The Company's investment objective is to deliver consistent positive returns with reduced market risk, irrespective of movements in the underlying share market. The Company will also seek to return a consistent stream of fully franked dividends to Shareholders.

### **Investment Strategy**

The Company's Investment Manager employs an equity market neutral strategy in managing the portfolio. A market neutral strategy aims to profit from the outperformance of a long portfolio over a short portfolio of shares. As the portfolios are roughly of equal value, the structure is fully hedged, minimising exposure to the changes in the broader share market. It provides the Company an opportunity to gain exposure to mispriced listed securities; as identified by the Investment Manager, without being fully exposed to the volatility and risks of the share market.

The value of Company's assets (longs) and its liabilities (shorts) move up and down together with movements in the share market, thereby minimising their impact on the portfolio. The Company profits to the extent that the long portfolio outperforms the short portfolio, irrespective of prevailing market direction. In this way, portfolio returns in a market neutral strategy will almost entirely reflect the Manager's success in choosing shares to buy and sell (short).

### **Investment Philosophy**

The Manager believes successful investing requires the following skills:

- An ability to evaluate the true worth of a business and the management charged with running it;
- An understanding of how and why a company's shares come to be mispriced; and
- An appreciation of the risks that may undermine the investment case.

Employing these skills, the Manager believes the best investment opportunities arise when shares in strong, well managed companies can be purchased on attractive terms. These companies typically exhibit the following characteristics:

- A history of superior returns through the economic cycle;
- Management with a track record of creating and distributing value to shareholders; and
- Businesses with a capacity to grow.

Consistent with these same principles, in selecting shares to short sell the Manager looks to sell the shares of companies with weak fundamentals on occasions when they become overvalued.

### **Investment Universe**

The universe from which investments can be selected comprises companies listed in Australia and on international exchanges. The Company may invest up to 50% of its gross exposure in international shares. While the primary focus is Australian shares, access to international shares provides the Manager with the opportunity to better express its investment ideas while developing deeper insights into Australian companies that compete in global markets.



## **Investment Process**

The Manager's investment process is a fundamentally driven, security selection process based on sound investment ideas taken from the investment of public companies. A summary of the investment process is set out below.

### *Security Selection*

Investment ideas come from monitoring economic and industry trends as well as extensive contact with company management and industry sources.

Once identified, investment opportunities are screened to ensure they are of an investment grade. A full qualitative assessment of the proposed investment is completed to establish whether the business is of a suitable quality and attractively priced.

### *Qualitative Review*

Once a suitable investment opportunity has been identified, a full review of financial performance will be completed. This is usually followed by a meeting with management to further develop an understanding of the business and the management philosophy. Where possible, representatives of the Manager will also meet with suppliers, regulators, competitors and customers to gauge the competitive environment.

### *Short Selling*

Short selling is an important part of the investment strategy employed by the Manager. In a market neutral structure, the manager will seek to match long and short exposures to maintain a fully hedged portfolio.

The Manager employs a similar security selection process as above, but is looking for the opposite qualities in companies to borrow and sell. The Manager believes the best "shorting" opportunities are found in poorly managed companies with weak fundamentals where the shares in those companies can be sold for more than they are worth.

When targeting companies to borrow and sell (short), the Manager will target:

- A history of inferior returns.
- Management with a poor track record.
- Businesses operating in highly competitive industries that are struggling to grow.
- Securities which are expensive on a range of valuation measures.

### *Portfolio Construction*

Unlike a traditional fund, the Manager constructs two portfolios, a long and a short portfolio with the weighting of each investment in each portfolio loosely correlated with the level of conviction around individual investment ideas.

This process ensures the Manager constructs portfolios around the best individual investment ideas, with the highest conviction, while retaining a bias in favour of good, well managed companies to buy (long), and weaker businesses to sell (short).

The manager will retain 100% of investors' capital in cash and cash equivalents, held with the Prime Broker and on deposit with an Australian bank. Funds are then raised through the short-sale of securities, with the proceeds invested in the long portfolio. As such, the company can maintain a gross market exposure of up to 400% of Shareholders' capital in mispriced securities while ensuring the portfolio is fully hedged against movements in the underlying share market.

**Watermark Market Neutral Fund Limited**  
**Investments at Market Value**  
**30 June 2016**

**Investments at Market Value**

**Consumer Services**

Ainsworth Game Technology Limited	817,385.04	0.78%
Crown Resorts Limited	1,730,066.78	1.66%
SKYCITY Entertainment Group Limited	1,373,216.88	1.31%
Tabcorp Holdings Limited	2,019,789.19	1.93%
	<b>5,940,457.89</b>	<b>5.68%</b>

**Media**

APN Outdoor Group Ltd.	932,631.60	0.89%
Fairfax Media Limited	2,873,999.46	2.75%
Village Roadshow Limited	1,024,384.41	0.98%
	<b>4,831,015.47</b>	<b>4.62%</b>

**Retailing**

Automotive Holdings Group Limited	1,194,657.28	1.14%
Kathmandu Holdings Limited	729,933.32	0.70%
Super Retail Group Limited	2,333,065.56	2.23%
	<b>4,257,656.16</b>	<b>4.07%</b>

**Food Beverage & Tobacco**

Bega Cheese Limited	394,360.50	0.38%
Coca-Cola Amatil Limited	1,635,589.05	1.56%
Pernod Ricard SA	956,438.11	0.92%
	<b>2,986,387.66</b>	<b>2.86%</b>

**Energy**

Eni SpA Sponsored ADR	1,407,394.38	1.35%
Karoo Gas Australia Ltd	906,676.73	0.87%
Royal Dutch Shell Plc Class B	1,912,100.84	1.83%
	<b>4,226,171.95</b>	<b>4.04%</b>

**Banks**

ABN AMRO Group N.V. Shs Depositary receipts	895,006.04	0.86%
Bank of Queensland Limited	2,363,105.55	2.26%
	<b>3,258,111.59</b>	<b>3.12%</b>

**Diversified Financials**

AMP Limited	847,359.72	0.81%
IOOF Holdings Ltd	1,253,755.26	1.20%
ING Groep NV Cert. of Shs	895,032.94	0.86%
	<b>2,996,147.92</b>	<b>2.87%</b>

**Insurance**

American International Group, Inc.	1,925,377.76	1.84%
Suncorp Group Limited	1,902,649.98	1.82%
	<b>3,828,027.74</b>	<b>3.66%</b>

**Real Estate**

Goodman Group	1,385,568.36	1.33%
Westfield Corporation	2,013,329.25	1.93%
	<b>3,398,897.61</b>	<b>3.25%</b>

**Health Care Equipment & Services**

Impedimed Limited	1,060,813.53	1.02%
Quintiles Transnational Holdings, Inc.	1,497,113.99	1.43%
Ramsay Health Care Limited	2,951,919.36	2.82%
Resmed Inc CHESS Depositary Interests on a ratio of 10 CDIs per ord.sh	2,328,814.00	2.23%
	<b>7,838,660.88</b>	<b>7.50%</b>

**Pharmaceuticals Biotechnology & Life Sciences**

Ionis Pharmaceuticals, Inc.	1,176,135.57	1.13%
Celgene Corporation	1,649,264.14	1.58%
Merck & Co., Inc.	3,199,343.29	3.06%
Novartis AG	2,370,614.26	2.27%
	<b>8,395,357.26</b>	<b>8.03%</b>

**Capital Goods**

Austal Limited	446,752.57	0.43%
RCR Tomlinson Ltd	499,053.70	0.48%
Reliance Worldwide Corp. Ltd.	1,283,128.68	1.23%
	<b>2,228,934.95</b>	<b>2.13%</b>

**Commercial & Professional Services**

Downer EDI Limited	1,316,871.00	1.26%
Smartgroup Corporation Ltd	1,514,187.75	1.45%
	<b>2,831,058.75</b>	<b>2.71%</b>

**Transportation**

Auckland International Airport Limited	2,128,807.20	2.04%
Transurban Group Ltd.	3,488,466.52	3.34%
	<b>5,617,273.72</b>	<b>5.37%</b>

**Semiconductors & Semiconductor Equipment**

Ambarella, Inc.	877,267.44	0.84%
	<b>877,267.44</b>	<b>0.84%</b>

**Software & Services**

Alphabet Inc. Class C	1,337,539.43	1.28%
MYOB Group Ltd.	1,895,902.65	1.81%
NYX Gaming Group Limited	1,121,371.12	1.07%
	<b>4,354,813.20</b>	<b>4.17%</b>

**Technology Hardware & Equipment**

Nokia Oyj	2,340,842.40	2.24%
	<b>2,340,842.40</b>	<b>2.24%</b>

**Materials**

Adelaide Brighton Ltd	1,559,522.02	1.49%
Alacer Gold Corp Shs Chess Depositary Interests repr 1 Sh	1,248,358.00	1.19%
CSR Limited	1,869,802.48	1.79%
Eastern Goldfields Ltd.	901,667.86	0.86%
Evolution Mining Limited	1,991,047.91	1.91%
Goldcorp Inc.	1,475,162.90	1.41%
Independence Group NL	1,277,648.56	1.22%
Iluka Resources Limited	1,114,865.18	1.07%
Incitec Pivot Limited	1,564,723.71	1.50%
Orora Ltd.	2,715,845.52	2.60%
Orocobre Limited	1,571,642.11	1.50%
Rio Tinto Limited	3,819,588.50	3.65%
Sims Metal Management Limited	492,620.90	0.47%
Tiger Resources Limited	280,123.08	0.27%
	<b>21,882,618.73</b>	<b>20.94%</b>

**Telecommunication Services**

China Mobile Limited	2,481,678.92	2.37%
BT Group plc	1,004,886.87	0.96%
Vivendi SA	3,450,742.08	3.30%
Vocus Communications Limited	1,299,836.76	1.24%
	<b>8,237,144.62</b>	<b>7.88%</b>

**Utilities**

AGL Energy Limited	2,253,226.32	2.16%
Spark Infrastructure Group Ltd.	1,932,787.44	1.85%
	<b>4,186,013.76</b>	<b>4.01%</b>

Total Long Portfolio	<b>104,512,860.00</b>	<b>100.00%</b>
Total Short Portfolio	<b>(106,552,187.00)</b>	

## **Corporate Governance Statement**

As an ASX-listed company, Watermark Market Neutral Fund Ltd ("Watermark MNF") and its directors are committed to responsible and transparent financial and business practices to protect and advance shareholders' interests. The Company's strong corporate governance practices are based on the ASX Corporate Governance Principles and Recommendations.

The Board has adopted these ASX principles and recommendations which are complemented by the Company's core principles of honesty and integrity. The corporate governance policies and practices adopted by the Board are outlined in Watermark MNF's Corporate Governance section (<http://wffunds.com.au/fund/watermark-market-neutral-fund-ltd/>).

## **Directors' Report**

The Directors present their report together with the financial statements of Watermark Market Neutral Fund Limited ("the Company") for the year ended 30 June 2016.

### **Directors**

The following persons held office as directors of Watermark Market Neutral Fund Limited during the financial year:

Matthew Kidman (Chairman)  
 Justin Braitling (Non-Independent Director)  
 John Abernethy (Independent Director)  
 Stephen Van Eyk (Independent Director)  
 Robert Ferguson (Independent Director)

Directors have been in office since the start of the financial year to the date of this report unless otherwise stated.

### **Principal activities**

During the financial year, the principal activities of the Company included making investments in listed companies and unlisted companies.

There was no significant change in the nature of the activity of the Company during the year.

### **Dividends**

Dividends paid to members were as follows:

	<b>Dividend Rate</b>	<b>Total Amount</b>	<b>Date of Payment</b>	<b>% Franked</b>
<b>2016</b>				
Ordinary shares - interim special 2016	\$0.010	\$871,201	29/04/2016	50
Ordinary shares - interim 2016	\$0.025	\$2,178,002	29/04/2016	50
Ordinary shares - final 2015	\$0.025	\$2,102,619	20/10/2015	50
<b>2015</b>				
Ordinary shares - interim 2015	\$0.020	\$1,747,948	14/04/2015	70
Ordinary shares - final 2014	\$0.025	\$2,183,325	20/10/2014	100

In addition to the above dividends, since the end of the financial year the Directors have recommended the payment of a final ordinary dividend of 3.0 cents per fully paid share, 75% franked to be paid on 20 October 2016 out of profits reserve at 30 June 2016.

### **Review of operations**

Information on the operations and financial position of the Company and its business strategies and prospects is set out in the review of operations and activities on pages 3 to 4 of this Annual Report.

The profit from ordinary activities after income tax amounted to \$10,615,257 (2015: loss of \$753,232).

The net tangible asset backing for each ordinary share as at 30 June 2016 amounted to 105 cents per share (2015: 99 cents per share). The equivalent asset backing before tax was 105 cents per share (2015: 99 cents per share).

### **Review of operations (continued)**

The gross portfolio value increased 22.3% over the financial year while the Reserve Bank of Australia's cash-rate increased by 2.0%, representing an outperformance of 20.3%. After deducting costs in funding the balance sheet, along with management fees and other expenses, the fund reported a positive 14.2% return for the year.

Further information on the operating and financial review of the Company is contained in the Chairman's Letter on page 1 and the Chief Investment Officer's Report on page 2 of the Annual Report.

### **Financial Position**

The net asset value of the Company for the current financial year ended was \$92,151,212 (2015: \$83,609,816).

### **Significant changes in the state of affairs**

It was announced on 15 February 2016 that the Board had approved an amendment to the Company's investment mandate, increasing the Fund's allowable investments in international shares. The Investment Manager can now invest up to 50% of the Fund's gross exposure in international shares.

Other than the matters noted above, there were no other significant changes in the state of affairs of the Company during the year ended 30 June 2016.

### **Matters subsequent to the end of the financial period**

Other than the dividend declared after year end, no other matter or circumstance has occurred subsequent to year end that has significantly affected, or may significantly affect, the operations of the Company, the results of those operations or the state of affairs of the Company in subsequent financial years.

### **Likely developments and expected results of operations**

The Company will continue to pursue its investment objectives for the long term benefit of the members. This will require continual review of the investment strategies that are currently in place and may require changes to these strategies to maximise returns.

### **Environmental regulation**

The Company is not affected by any significant environmental regulation in respect of its operations.

To the extent that any environmental regulations may have an incidental impact on the Company's operations, the Directors of the Company are not aware of any breach by the Company of those regulations.

## **Information on directors**

**Matthew Kidman** Chairman Age 47.

### ***Experience and expertise***

Matthew Kidman has over 20 years' experience in the finance industry. He spent four years as finance journalist at the Sydney Morning Herald, during which time he was appointed finance editor of the newspaper. In 1998 Matthew joined the funds management group Wilson Asset Management as a portfolio manager, his roles since then included positions as stock analyst, dealer, portfolio manager and senior executive of the management group. He was appointed to the board of WAM Capital Pty Limited in 1999.

Matthew holds a Bachelor of Economics and Bachelor of Laws degree and a Graduate Diploma in Applied Finance, all from Macquarie University.

### ***Other current directorships***

Matthew is the director of WAM Capital Pty Limited, WAM Research Pty Limited, WAM Active Limited, Incubator Capital Limited and Sandon Capital Investments Limited. He is also founder of funds management group Centennial Asset Management Pty Limited.

### ***Former directorships in last 3 years***

Matthew Kidman resigned as director of financial planning group Centrepont Alliance Limited in November 2015.

### ***Special responsibilities***

Chairman of the Board.

### ***Interests in shares and options***

Details of Matthew Kidman's interests in shares of the Company are included later in this report.

### ***Interests in contracts***

Matthew Kidman has no interests in contracts of the Company.

**Information on directors (continued)**

**Justin Braitling** Non-Independent Director Age 49.

***Experience and expertise***

Justin Braitling has over 25 years' experience in investing in Australian and international companies. He was an Investment Analyst and Portfolio Manager at Bankers Trust for 12 years from January 1991 to June 2002. He was a key member of the investment team at Bankers Trust that was consistently ranked in the top quartile of managers by InTech.

***Other current directorships***

Justin Braitling is the sole Director of the investment management company, Watermark Funds Management Pty Limited.

Justin Braitling has been a Director of Australian Leaders Fund Limited since October 2003 of which he became Chairman in February 2007.

***Former directorships in last 3 years***

Justin Braitling has not held any other directorships of listed companies within the last three years.

***Special responsibilities***

Investment Manager of the Company.

***Interests in shares and options***

Details of Justin Braitling's interests in shares of the Company are included later in this report.

***Interests in contracts***

Details of Justin Braitling's interests in contracts of the Company are included later in this report.

**Information on directors (continued)**

**John Abernethy** Independent Director Age 57.

***Experience and expertise***

John Abernethy has over 30 years' experience in funds management and corporate advisory. He holds a Bachelor of Commerce and Bachelor of Laws (BCom/LLB) from the University of New South Wales. He spent ten years at NRMA Investments as Head of Equities. In 1994 he joined Poynton Corporate Limited as an Executive Director before forming Clime Investment Management Limited in 1996.

***Other current directorships***

John Abernethy is the Chairman of Clime Capital Limited. He is a Director of Clime Investment Management Limited, Jasco Holdings Limited, WAM Research Limited (appointed May 2002), WAM Active Limited (appointed November 2007) and Australian Leaders Fund Limited.

***Former directorships in last 3 years***

John Abernethy has not held any other directorships of listed companies within the last three years.

***Special responsibilities***

Chairman of the Audit Committee

***Interests in shares and options***

John Abernethy has no interests in shares and options of the Company.

***Interests in contracts***

John Abernethy has no interests in contracts of the Company.



**Information on directors (continued)**

**Robert Ferguson** Independent Director Age 70.

***Experience and expertise***

Robert Ferguson's career spans over 30 years' in research, finance, investment management and property. Robert commenced employment in 1971 with Bankers Trust Australia Ltd and was its CEO between 1985 and 1999 and Chairman from 1999 to 2001. Robert has extensive experience in both executive and non-executive roles.

Robert holds a B.Ec (Hons) from the University of Sydney.

***Other current directorships***

Robert is the Chairman of GPT Management Holdings Limited; Non-Executive Chairman of Primary Health Care Limited; Non-Executive Director of Tyro Payments Limited and Chairman of SmartWard Holdings Pty Ltd.

***Former directorships in last 3 years***

Robert Ferguson has not held any other directorships of listed companies within the last three years.

***Special responsibilities***

Member of the Audit Committee

***Interests in shares and options***

Details of Robert Ferguson's interests in shares of the Company are included later in this report.

***Interests in contracts***

Robert Ferguson has no interests in contracts of the Company.

**Information on directors (continued)**

**Stephen Van Eyk** Independent Director Age 64.

***Experience and expertise***

Stephen has over 25 years' experience in the financial services industry, with over 15 years as Managing Director of research house van Eyk Research. Stephen was presented with the Lifetime Achievement Award at the 2013 Fund Manager awards.

Stephen holds a Commerce Degree from the UNSW and is a fellow of the Financial Services Institute.

***Other current directorships***

Stephen Van Eyk has not held any other directorships of listed companies outside the Company.

***Former directorships in last 3 years***

Stephen Van Eyk has not held any other directorships of listed companies within the last three years.

***Special responsibilities***

Member of the Audit Committee

***Interests in shares and options***

Details of Stephen Van Eyk's interests in shares of the Company are included later in this report.

***Interests in contracts***

Stephen Van Eyk has no interests in contracts of the Company.

**Company secretary**

Peter Roberts of White Outsourcing Pty Limited had resigned as Company Secretary, effective 27 April 2016. Following the resignation, Matthew McShane of White Outsourcing Pty Limited was appointed as Company Secretary, effective 27 April 2016.

Matthew McShane has more than 20 years' experience in the financial services industry covering executive roles in Custody, Administration and Funds Management. Mr McShane has a Masters degree in Applied Finance and is a member of the Australian Institute of Company Directors.

**Watermark Market Neutral Fund Limited**  
**Directors' Report**  
**For the year ended 30 June 2016**  
(continued)

**Meetings of directors**

The numbers of meetings of the Company's board of Directors and of each board committee held during the year ended 30 June 2016, and the numbers of meetings attended by each Director were:

	Directors' Meetings		Meetings of committees					
			Audit		Nomination		Remuneration	
	A	B	A	B	A	B	A	B
Matthew Kidman	4	4	3*	3	-	-	-	-
Justin Braitling	4	4	3*	3	-	-	-	-
John Abernethy	4	4	3	3	-	-	-	-
Stephen Van Eyk	4	4	3	3	-	-	-	-
Robert Ferguson	3	4	2	3	-	-	-	-

A = Number of meetings attended

B = Number of meetings held during the time the Director held office or was a member of the committee during the year

\* Not a member of the relevant committee

**Remuneration report (audited)**

This report details the nature and amount of remuneration for key management personnel of Watermark Market Neutral Fund Limited in accordance with the *Corporations Act 2001*.

Fees and payments to Directors reflect the demands that are made on and the responsibilities of the Directors and are reviewed annually by the Board. The Company determines the remuneration levels and ensures they are competitively set to attract and retain appropriately qualified and experienced Directors.

Directors' base fees are set at a maximum of \$180,000 per annum. Directors do not receive bonuses nor are they issued options on securities. Directors' fees cover all main board activities and membership of committees. Under the ASX Listing Rules, the maximum fees paid to Directors may not be increased without approval from the Company at a general meeting. Directors will seek approval from time to time as appropriate.

**Details of remuneration**

The following tables show details of the remuneration received by key management personnel of the Company for the current and previous financial year.

2016	Short-term employee benefits		Post-employment benefits	
	Salary and fees		Superannuation	Total
Name	\$		\$	\$
<b>Non-executive Directors</b>				
Matthew Kidman	27,397		2,603	30,000
John Abernethy	27,397		2,603	30,000
Stephen Van Eyk	27,397		2,603	30,000
Robert Ferguson	27,397		2,603	30,000
<b>Sub-total non-executive directors</b>	<b>109,588</b>		<b>10,412</b>	<b>120,000</b>
<b>Executive Director</b>				
Justin Braitling	9,132		868	10,000
<b>Other key management personnel</b>				
Peter Roberts *	-		-	-
Matthew McShane *	-		-	-
<b>Total key management personnel compensation</b>	<b>118,720</b>		<b>11,280</b>	<b>130,000</b>

**Watermark Market Neutral Fund Limited**  
**Directors' Report**  
**For the year ended 30 June 2016**  
(continued)

**Remuneration report (audited) (continued)**

**Details of remuneration (continued)**

2015	Short-term employee benefits	Post-employment benefits	
Name	Salary and fees \$	Superannuation \$	Total \$
<b>Non-executive Directors</b>			
Matthew Kidman	27,397	2,603	30,000
John Abernethy	27,397	2,603	30,000
Stephen Van Eyk	27,397	2,603	30,000
Robert Ferguson	27,397	2,603	30,000
<b>Sub-total non-executive directors</b>	<b>109,588</b>	<b>10,412</b>	<b>120,000</b>
<b>Executive Director</b>			
Justin Braithling	9,132	868	10,000
<b>Other key management personnel</b>			
Peter Roberts *	-	-	-
Matthew McShane *	-	-	-
<b>Total key management personnel compensation</b>	<b>118,720</b>	<b>11,280</b>	<b>130,000</b>

\* Accounting and company secretarial duties are outsourced to White Outsourcing Pty Limited. Peter Roberts (resigned 27/04/2016) is a director and Matthew McShane (appointed 27/04/2016) is the Head of Operations of White Outsourcing Pty Limited which received fees net of reduced input tax credits of \$115,230 during the year (2015: \$113,127) for the services rendered pursuant to an Administrative Services Agreement entered into by the Company. As at 30 June 2016, the balance payable to White Outsourcing Pty Limited was \$16,776 (2015: \$7,830). Neither Mr Roberts nor Mr McShane received any fees as an individual. White Outsourcing Pty Limited is remunerated in accordance with the Service Level Agreement dated 25 June 2013. The agreement has no fixed term.

The following table comprises the company performance and non-executive directors' remuneration:

	<b>2016</b>	<b>2015</b>	<b>2014*</b>
Operating profit/(loss) after tax	\$10,615,257	(\$753,232)	6,656,726
Dividends paid (cents per share)	6.0	4.5	2.5
Net tangible asset (\$ per share)	\$1.05	\$0.99	\$1.06
Total Directors' remuneration	\$120,000	\$120,000	\$128,383
Total Shareholder's Equity	\$92,151,212	83,609,816	\$88,034,515

\* The profit and loss balances are reflecting the reporting period from 28 May 2013 to 30 June 2014.

**Director Related Entity Remuneration**

All transactions with related entities were made on normal commercial terms and conditions.

Justin Braithling is the sole Director and beneficial owner of Watermark Funds Management Pty Limited, the entity appointed to manage the investment portfolio of Watermark Market Neutral Fund Limited. In its capacity as manager, Watermark Funds Management Pty Limited was paid a management fee of 1%p.a. (plus GST) on the net value of the portfolio amounting to \$925,571 (2015: \$861,539). As at 30 June 2016, the balance payable to the manager was \$84,406 (2015: \$73,247).

In addition, Watermark Funds Management Pty Limited is to be paid, annually in arrears, a performance fee being 20% of:

- where the level of the Reserve Bank of Australia's cash-rate has increased over that year, the amount of the increase in the Value of the Portfolio exceeds this increase; or
- where the Reserve Bank of Australia's cash-rate has decreased over that year, the amount of the increase in the Value of the Portfolio.

**Remuneration report (audited) (continued)**

**Details of remuneration (continued)**

**Director Related Entity Remuneration (continued)**

No performance fee is payable in respect of any performance period where the portfolio has decreased in value over that period. On the 19 May 2015, the Company announced, if the portfolio underperforms the benchmark over a financial year that underperformance is to be recouped before any entitled performance fee can be accrued.

For the year ended 30 June 2016, in its capacity as manager, Watermark Funds Management Pty Limited was paid a performance fee amounting to \$2,750,119 (2015: Nil).

These amounts are in addition to the above Directors remuneration.

No Director has received or become entitled to receive a benefit (other than those detailed above) by reason of a contract made by the Company or a related Company with the Director or with a firm of which he is a member or with a Company in which he has substantial financial interest.

**Remuneration of Executives**

Justin Braitling is considered an Executive Director on the basis that he is a director and a shareholder of Watermark Fund Management Pty Limited and due to his role of an Investment Manager in that entity, is integrally involved in the operation of the Company. Watermark Funds Management Pty Limited remunerates Justin Braitling as an employee and also provides day to day management of the Company and is remunerated as outlined above.

**Equity Instrument Disclosures Relating to Directors**

As at the date of this report, the Company's Directors and their related parties held the following interests in the Company:

*Ordinary Shares Held*

**2016**

<b>Director</b>	<b>Position</b>	<b>Balance at 28 August 2015</b>	<b>Acquisitions</b>	<b>Disposals</b>	<b>Balance at 16 August 2016</b>
Matthew Kidman	Chairman	50,000	14,563	-	64,563
Justin Braitling	Non-Independent Director	683,001	30,000	-	713,001
Robert Ferguson	Independent Director	1,000,000	-	-	1,000,000
Stephen Van Eyk	Independent Director	48,780	66,646	-	115,426
John Abernethy	Independent Director	-	-	-	-
		<b>1,781,781</b>	<b>111,209</b>	<b>-</b>	<b>1,892,990</b>

**2015**

<b>Director</b>	<b>Position</b>	<b>Balance at 13 August 2014</b>	<b>Acquisitions/ Options Exercised</b>	<b>Disposals</b>	<b>Balance at 27 August 2015</b>
Matthew Kidman	Chairman	50,000	-	-	50,000
Justin Braitling	Non-Independent Director	300,001	583,000	(200,000)	683,001
Robert Ferguson	Independent Director	1,000,000	-	-	1,000,000
Stephen Van Eyk	Independent Director	48,780	-	-	48,780
John Abernethy	Independent Director	-	-	-	-
		<b>1,398,781</b>	<b>583,000</b>	<b>(200,000)</b>	<b>1,781,781</b>

**Remuneration report (audited) (continued)**

**Details of remuneration (continued)**

**Equity Instrument Disclosures Relating to Directors (continued)**

*Options Held*

None of the Directors held options during the year ended 30 June 2016.

**2015**

Director	Position	Balance at 13 August 2014	Options Acquired	Options Forfeited	Balance at 27 August 2015
Matthew Kidman	Chairman	50,000		(50,000)	
Justin Braitling	Non-Independent Director	100,000		(100,000)	-
Stephen Van Eyk	Independent Director	-	-	-	-
Robert Ferguson	Independent Director	1,000,000		(1,000,000)	-
John Abernethy	Independent Director	-	-	-	-
		<b>1,150,000</b>		<b>(1,150,000)</b>	

Directors and Director related entities acquired options in the Company on the same terms and conditions available to other shareholders.

The Directors have not, during or since the end of the financial year, been granted options over unissued shares or interests in shares of the Company as part of their remuneration.

*End of remuneration report*

**Insurance and indemnification of officers and auditors**

*(a) Insurance of officers*

During the financial year, the Company paid a premium in respect of a contract insuring the Directors of the Company, the Company Secretary and any related body corporate against liability incurred as such by a Director or Secretary to the extent permitted by the *Corporations Act 2001*. The contract of insurance prohibits disclosure of the nature of the liability and the amount of the premium.

No indemnities have been given or insurance premiums paid during or since the end of the financial year, for any person who is or has been an auditor of the Company.

*(b) Indemnity of auditors*

No indemnities have been given or insurance premiums paid during or since the end of the financial year, for any person who is or has been an auditor of the Company.

**Proceedings on behalf of the company**

No person has applied to the Court under section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the Company with leave of the Court under section 237 of the *Corporations Act 2001*.

### **Non-audit services**

The Board of Directors, in accordance with advice from the Audit & Risk Committee, is satisfied that the provision of non-audit services during the year is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. The Directors are satisfied that the services disclosed in Note 19 did not compromise the external auditor's independence for the following reasons:

- all non-audit services have been reviewed by the audit committee to ensure they do not impact the impartiality and objectivity of the auditor
- none of the services undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*.

### **Auditor's independence declaration**

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 21.

### **Rounding of amounts**

The Company is an entity of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 issued by the ASIC relating to the 'rounding off' of amounts in the financial statements. Amounts in the financial statements have been rounded to the nearest dollars in accordance with that ASIC Corporations Instrument, unless otherwise indicated.

This report is made in accordance with a resolution of Directors.



Matthew Kidman  
Chairman

Sydney  
16 August 2016

**AUDITOR'S INDEPENDENCE DECLARATION  
TO THE DIRECTORS OF WATERMARK MARKET NEUTRAL FUND LIMITED  
ABN 45 163 980 498**

In relation to the independent audit for the year ended 30 June 2016, to the best of my knowledge and belief there have been:

- (i) no contraventions of the auditor independence requirements of the *Corporations Act 2001*; and
- (ii) no contraventions of any applicable code of professional conduct.

This declaration is in respect of Watermark Market Neutral Fund Limited during the year.



**S M WHIDDETT**  
Partner

**PITCHER PARTNERS**  
Sydney

16 August 2016



**Watermark Market Neutral Fund Limited**  
**Statement of Comprehensive Income**  
**For the year ended 30 June 2016**

**Statement of Comprehensive Income**

		Year ended	
	Notes	2016 \$	2015 \$
<b>Investment income from ordinary activities</b>			
Net realised gains on investments		17,708,291	3,537,347
Net unrealised gains/(losses) on investments		1,222,287	(2,792,142)
Dividends		2,714,737	2,447,230
Interest		2,782,466	3,758,928
Trust distributions		236,174	217,028
Other income		88,428	85,413
Net foreign exchange gains		22,677	118,657
		<u>24,775,060</u>	<u>7,372,461</u>
<b>Expenses</b>			
Management fees	21(b)	(925,571)	(861,539)
Performance fees	21(b)	(2,750,119)	-
Brokerage expense		(1,548,997)	(1,170,174)
Short dividend expense		(3,387,306)	(3,388,001)
Interest expense		(1,238,621)	(2,091,147)
Stock loan fees		(686,575)	(1,028,235)
Accounting fees		(115,230)	(113,127)
Share registry fees		(61,639)	(65,448)
Legal fees		(9,788)	(13,600)
Directors' fees	18(a)	(130,000)	(130,000)
ASX fees		(49,216)	(53,093)
Audit fees	19	(60,075)	(48,546)
Other expenses		(189,812)	(248,900)
		<u>(11,152,949)</u>	<u>(9,211,810)</u>
<b>Profit/(loss) before income tax</b>		<b>13,622,111</b>	<b>(1,839,349)</b>
Income tax (expense)/benefit	7	(3,006,854)	1,086,117
<b>Profit/(loss) for the year</b>		<b>10,615,257</b>	<b>(753,232)</b>
<b>Other comprehensive income for the year, net of tax</b>		<b>-</b>	<b>-</b>
<b>Total comprehensive income/(loss) for the year</b>		<b>10,615,257</b>	<b>(753,232)</b>
		<b>Cents</b>	<b>Cents</b>
<b>Earnings per share for profit/(loss) attributable to the ordinary equity holders of the Company:</b>			
Basic earnings/(loss) per share	24	12.52	(0.87)
Diluted earnings/(loss) per share	24	12.52	(0.87)

*The above Statement of Comprehensive Income should be read in conjunction with the accompanying notes.*

**Watermark Market Neutral Fund Limited**  
**Statement of Financial Position**  
**As at 30 June 2016**

**Statement of Financial Position**

		<b>At</b>	
	Notes	<b>2016</b> \$	2015 \$
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents	8	93,247,732	77,318,497
Trade and other receivables	9	4,179,652	8,193,429
Financial assets at fair value through profit or loss	10	104,512,860	76,651,953
Current tax assets		1,534,384	2,689,021
<b>Total current assets</b>		<b>203,474,628</b>	164,852,900
<b>Non-current assets</b>			
Deferred tax assets	11	253,992	378,155
<b>Total non-current assets</b>		<b>253,992</b>	378,155
<b>Total assets</b>		<b>203,728,620</b>	165,231,055
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Trade and other payables	12	4,869,408	9,047,727
Financial liabilities at fair value through profit or loss	13	106,552,187	72,373,875
<b>Total current liabilities</b>		<b>111,421,595</b>	81,421,602
<b>Non-current liabilities</b>			
Deferred tax liabilities	14	155,813	199,637
<b>Total non-current liabilities</b>		<b>155,813</b>	199,637
<b>Total liabilities</b>		<b>111,577,408</b>	81,621,239
<b>Net assets</b>		<b>92,151,212</b>	83,609,816
<b>EQUITY</b>			
Issued capital	15	86,552,644	83,474,683
Reserves	16(a)	6,364,468	888,365
Accumulated losses	16(b)	(765,900)	(753,232)
<b>Total equity</b>		<b>92,151,212</b>	83,609,816

*The above Statement of Financial Position should be read in conjunction with the accompanying notes.*

**Watermark Market Neutral Fund Limited**  
**Statement of Changes in Equity**  
**For the year ended 30 June 2016**

**Statement of Changes in Equity**

	Notes	Issued Capital \$	Profits Reserves \$	Accumulated losses \$	Total \$
<b>Balance at 1 July 2014</b>		83,214,877	4,819,638	-	88,034,515
Loss for the year		-	-	(753,232)	(753,232)
<b>Transactions with owners in their capacity as owners:</b>					
Dividends provided for or paid	17	-	(3,931,273)	-	(3,931,273)
On market buy back	15	(2,967,298)	-	-	(2,967,298)
Shares issued on options exercised	15	2,983,171	-	-	2,983,171
Shares issued under dividend reinvestment plan	15	251,654	-	-	251,654
Costs of issued capital	15	(7,721)	-	-	(7,721)
		259,806	(3,931,273)	-	(3,671,467)
<b>Balance at 30 June 2015</b>		<b>83,474,683</b>	<b>888,365</b>	<b>(753,232)</b>	<b>83,609,816</b>
<b>Balance at 1 July 2015</b>		83,474,683	888,365	(753,232)	83,609,816
Profit for the year		-	-	10,615,257	10,615,257
<b>Transactions with owners in their capacity as owners:</b>					
Dividends provided for or paid	17	-	(5,151,822)	-	(5,151,822)
On market buy back	15	(9,500)	-	-	(9,500)
Share placement share issued	15	3,116,045	-	-	3,116,045
Costs of issued capital	15	(28,584)	-	-	(28,584)
Transfer to profits reserve	16	-	10,627,925	(10,627,925)	-
		3,077,961	5,476,103	(10,627,925)	(2,073,861)
<b>Balance at 30 June 2016</b>		<b>86,552,644</b>	<b>6,364,468</b>	<b>(765,900)</b>	<b>92,151,212</b>

*The above Statement of Changes in Equity should be read in conjunction with the accompanying notes.*

**Watermark Market Neutral Fund Limited**  
**Statement of Cash Flows**  
**For the year ended 30 June 2016**

**Statement of Cash Flows**

		Year ended	
	2016	2015	
	\$	\$	
Notes			
<b>Cash flows from operating activities</b>			
Purchase of financial assets	(293,048,266)	(213,485,593)	
Proceeds from sale of financial assets	280,052,641	233,694,947	
Proceeds from short sale of financial liabilities	311,380,185	209,027,014	
Re-purchase of financial liabilities	(275,485,273)	(226,173,266)	
Interest received	2,785,402	3,950,442	
Interest paid	(1,253,258)	(2,150,878)	
Dividends and trust distributions received	2,684,153	2,751,885	
Dividends paid on short stocks	(3,493,930)	(3,475,294)	
Underwriting income	79,126	81,990	
Other income received	8,696	-	
Income taxes paid	(1,759,628)	(2,952,113)	
Investment management fees paid	(916,867)	(885,933)	
Performance fees paid	-	(2,259,714)	
Brokerage expense	(1,536,450)	(1,210,693)	
Stock loan fees	(681,360)	(1,042,905)	
Payments for other expenses	(592,178)	(658,374)	
<b>Net cash inflow/(outflow) from operating activities</b>	23(a) <u>18,222,993</u>	<u>(4,788,485)</u>	
<b>Cash flows from financing activities</b>			
Payments for shares bought back	(233,015)	(2,743,783)	
Share issue transaction costs	(40,833)	(11,030)	
Dividends paid	(5,158,629)	(3,672,827)	
Shares purchased under share purchase plan	3,116,045	-	
Shares issued on options exercised	-	2,983,171	
<b>Net cash outflow from financing activities</b>	<u>(2,316,432)</u>	<u>(3,444,469)</u>	
<b>Net increase/(decrease) in cash and cash equivalents</b>	15,906,561	(8,232,954)	
Cash and cash equivalents at the beginning of the year	77,318,497	85,432,794	
Effects of exchange rate changes on cash and cash equivalents	22,674	118,657	
<b>Cash and cash equivalents at end of the year</b>	8 <u>93,247,732</u>	<u>77,318,497</u>	
<b>Non-cash investing and financing activities</b>			
Dividends reinvested	23(b) <u>-</u>	<u>251,654</u>	

*The above Statement of Cash Flows should be read in conjunction with the accompanying notes.*

## **1 General information**

Watermark Market Neutral Fund Limited (the "Company") is a listed public company domiciled in Australia. The address of Watermark Market Neutral Fund Limited's registered office is Level 6, 139 Macquarie Street, Sydney, NSW 2000. The financial statements of Watermark Market Neutral Fund Limited are for the year ended 30 June 2016. The Company is primarily involved in making investments, and deriving revenue and investment income from listed securities and unit trusts in Australia.

## **2 Summary of significant accounting policies**

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated. The financial statements are for the entity Watermark Market Neutral Fund Limited.

### **(a) Basis of preparation**

These general purpose financial statements have been prepared in accordance with Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board and the *Corporations Act 2001*. Watermark Market Neutral Fund Limited is a for-profit entity for the purpose of preparing the financial statements.

The financial statements were authorised for issue by the Board of Directors on 16 August 2016.

#### *(i) Compliance with IFRS*

The financial statements of the Watermark Market Neutral Fund Limited also comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

#### *(ii) New and amended standards adopted by the Company*

There are no standards, interpretations or amendments to existing standards that are effective for the first time for the financial year beginning 1 July 2015 that have a material impact on the Company.

#### *(iii) Historical cost convention*

These financial statements have been prepared under the accruals basis and are based on historical cost convention, as modified by the revaluation of financial assets and liabilities at fair value through profit or loss.

#### *(iv) Critical accounting estimates*

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 5.

#### *(v) New standards and interpretations not yet adopted*

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2016 reporting periods and have not been early adopted by the Company. The Company's assessment of the impact of these new standards and interpretations is set out below.

## 2 Summary of significant accounting policies (continued)

### (a) Basis of preparation (continued)

Title of standard	Nature of change	Impact	Mandatory application date/ Date of adoption by the Company
AASB 9 <i>Financial Instruments</i>	AASB 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities and introduces new rules for hedge accounting. In December 2014, the AASB made further changes to the classification and measurement rules and also introduced a new impairment model. These latest amendments now complete the new financial instruments standard.	<p>Following the changes approved by the AASB in December 2014, the Company no longer expects any impact from the new classification, measurement and derecognition rules on the Company's financial assets and financial liabilities.</p> <p>There will also be no impact on the Company's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the Company does not have any such liabilities.</p> <p>The derecognition rules have not changed from the previous requirements, and the Company does not apply hedge accounting. The new standard also introduces expanded disclosure requirements and changes in presentation.</p> <p>The new impairment model is an expected credit loss (ECL) model which may result in the earlier recognition of credit losses.</p> <p>The Company has not yet assessed how the impairment provisions would be affected by the new rules.</p>	<p>Must be applied for financial years commencing on or after 1 January 2018.</p> <p>Based on the transitional provisions in the completed IFRS 9, early adoption in phases was only permitted for annual reporting periods beginning before 1 February 2015. After that date, the new rules must be adopted in their entirety.</p> <p>The Company has not yet decided whether it will early adopt AASB 9.</p>

## 2 Summary of significant accounting policies (continued)

### (a) Basis of preparation (continued)

<b>Title of standard</b>	<b>Nature of change</b>	<b>Impact</b>	<b>Mandatory application date/ Date of adoption by the Company</b>
AASB 15 <i>Revenue from Contracts with Customers</i>	<p>The AASB has issued a new standard for the recognition of revenue. This will replace AASB 118 which covers contracts for goods and services and AASB 111 which covers construction contracts.</p> <p>The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer - so the notion of control replaces the existing notion of risks and rewards.</p> <p>The standard permits a modified retrospective approach for the adoption. Under this approach entities will recognise transitional adjustments in retained earnings on the date of initial application (eg 1 July 2017), ie without restating the comparative period. They will only need to apply the new rules to contracts that are not completed as of the date of initial application.</p>	<p>The Company's main sources of income are interest, dividends and distributions and gains on financial instruments held at fair value. All of these are outside the scope of the new revenue standard. As a consequence, the Directors do not expect the adoption of AASB 15 to have a significant impact on the Company's accounting policies or the amounts recognised in the financial statements.</p>	<p>Mandatory for financial years commencing on or after 1 January 2017.</p> <p>The Company has not yet decided whether it will early adopt AASB 15.</p>

There are no other standards that are not yet effective and that would be expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

### (b) Foreign currency translation

#### (i) *Functional and presentation currency*

Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The financial statements are presented in Australian dollars, which is Watermark Market Neutral Fund Limited's functional and presentation currency.

## 2 Summary of significant accounting policies (continued)

### (b) Foreign currency translation (continued)

#### *(ii) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Comprehensive Income.

Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Translation differences on assets and liabilities carried at fair value are reported as part of the fair value gain or loss in the Statement of Comprehensive Income.

### (c) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable. Amounts disclosed as revenue are net of rebates and amounts collected on behalf of third parties.

Revenue is recognised where it is probable that the economic benefit will flow to the entity and can be reliably measured.

#### *(i) Investment income*

Profits and losses realised from the sale of investments and unrealised gains and losses on securities held at fair value are included in the Statement of Comprehensive Income in the year they are incurred in accordance with the policies described in Note 2(h).

#### *(ii) Dividends and trust distributions*

Dividends and trust distributions are recognised as revenue when the right to receive payment is established.

#### *(iii) Interest income*

Interest income is recognised as it accrues, taking into account the effective yield on the financial asset.

#### *(iv) Other income*

The Company recognises other income when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity. The Company bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

### (d) Income tax

The income tax expense/(income) for the year comprises current income tax expense/(income) and deferred tax expense/(income).

Current income tax expense charged to profit or loss is the tax payable on taxable income. Current tax liabilities/(assets) are measured at the amounts expected to be paid to/(recovered from) the relevant taxation authority.

Deferred income tax expense reflects movements in deferred tax asset and deferred tax liability balances during the year as well as unused tax losses.

Current and deferred income tax expense/(income) is charged or credited outside profit or loss when the tax relates to items that are recognised outside profit or loss.

Deferred tax assets and liabilities are calculated at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled and their measurement also reflects the manner in which management expects to recover or settle the carrying amount of the related asset or liability.

Deferred tax assets relating to temporary differences and unused tax losses are recognised only to the extent that it is probable that future taxable profit will be available against which the benefits of the deferred tax asset can be utilised.



## 2 Summary of significant accounting policies (continued)

### (d) Income tax (continued)

Current tax assets and liabilities are offset where a legally enforceable right of set-off exists and it is intended that net settlement or simultaneous realisation and settlement of the respective asset and liability will occur. Deferred tax assets and liabilities are offset where: (a) a legally enforceable right of set-off exists; and (b) the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where it is intended that net settlement or simultaneous realisation and settlement of the respective asset and liability will occur in future periods in which significant amounts of deferred tax assets or liabilities are expected to be recovered or settled.

### (e) Cash and cash equivalents

For the purpose of presentation in the Statement of Cash Flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the Statement of Financial Position.

### (f) Due from/to brokers

Amounts due from/to brokers represent receivables for securities sold and payables for securities purchased that have been contracted for but not yet delivered by the end of the year. Trades are recorded on trade date, and for equities normally settled within three business days. A provision for impairment of amounts due from brokers is recognised in the Statement of Comprehensive Income when there is objective evidence that the Company will not be able to collect all amounts due from the relevant broker. Indicators that the amount due from brokers is impaired include significant financial difficulties of the broker, probability that the broker will enter bankruptcy or financial reorganisation and default in payments.

### (g) Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. Trade and other receivables are generally due for settlement within 30 days. They are presented as current assets unless collection is not expected for more than 12 months after the reporting date.

Collectability of trade and other receivables is reviewed on an ongoing basis. Debts which are known to be uncollectible are written off by reducing the carrying amount directly.

### (h) Financial assets and liabilities

The Company's investments are classified as at fair value through profit or loss. They comprise:

#### **Classification**

##### *(i) Financial assets and liabilities at fair value through profit or loss - held for trading*

Financial assets are classified in this category if acquired principally for the purpose of selling in the short term. Assets in this category are classified as current assets if they are expected to be settled within 12 months; otherwise they are classified as non-current.

The Company makes short sales in which a borrowed security is sold in anticipation of a decline in the market value of that security, or it may use short sales for various arbitrage transactions. Short sales are classified as current financial liabilities at fair value through profit or loss.

Dividends expense on short sales of securities, which have been classified at fair value through profit or loss, is recognised in the Statement of Comprehensive Income.

## 2 Summary of significant accounting policies (continued)

### (h) Financial assets and liabilities (continued)

#### (ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for those with maturities greater than 12 months after the reporting period which are classified as non-current assets. Loans and receivables are included in trade and other receivables (note 9) in the Statement of Financial Position.

#### (iii) Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company's management has the positive intention and ability to hold to maturity. If the Company were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available-for-sale. Held-to-maturity financial assets are included in non-current assets, except for those with maturities less than 12 months from the end of the reporting period, which are classified as current assets.

#### **Recognition and derecognition**

Purchases and sales of financial assets and liabilities at fair value through profit or loss are recognised on trade-date - the date on which the Company commits to purchase or sell the asset or liability. Investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

#### **Measurement**

At initial recognition, the Company measures its financial assets and liabilities at fair value excluding any transaction costs that are directly attributable to their acquisition.

Transaction costs of financial assets and financial liabilities at fair value through profit or loss are expensed in the Statement of Comprehensive Income.

Loans and receivables are subsequently carried at amortised cost using the effective interest method.

Subsequent to initial recognition, all instruments held at fair value through profit or loss are measured at fair value with changes in their fair value recognised in the Statement of Comprehensive Income.

When an investment is disposed, the cumulative gain or loss, net of tax thereon, is recognised as realised gains and losses from the sale of financial instruments in the Statement of Comprehensive Income.

#### **Determination of Fair Value**

AASB 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Company has access at that date. The fair value of a liability reflects its non-performance risk.

The Company's accounting policy on fair value measurements is discussed in Note 4.

Under AASB 13, if an investment has a bid price and an ask price, the price within the bid-ask spread that is more representative of fair value in the circumstances shall be used to measure fair value. Accordingly, the Company uses the last sale price as a basis of measuring fair value.

### (i) Trade and other payables

These amounts represent liabilities for goods and services provided to the Company prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition. Trade and other payables are presented as current liabilities unless payment is not due within 12 months from the reporting date. They are recognised initially at their fair value and subsequently measured at amortised cost using the effective interest method.

## 2 Summary of significant accounting policies (continued)

### (j) Finance costs

Finance costs are recognised as expenses in the year in which they are incurred using the effective interest rate method.

### (k) Issued capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

### (l) Profits reserve

A profits reserve has been created representing an amount allocated from current and retained earnings that is preserved for future dividend payments.

### (m) Dividends

Provision is made for the amount of any dividend declared, being appropriately authorised and no longer at the discretion of the entity, on or before the end of the reporting period but not distributed at the end of the reporting period.

In accordance with the *Corporations Act 2001*, the Company may pay a dividend where the Company's assets exceed its liabilities, the payment of the dividend is fair and reasonable to the Company's shareholders as a whole and the payment of the dividend does not materially prejudice the Company's ability to pay its creditors.

It is the Directors' policy to pay fully franked dividends provided the Company has sufficient profit reserves and franking credits and to distribute the majority of franking credits received each year. Franking credits are generated by receiving fully franked dividends from shares held in the Company's investment portfolio, and from the payment of corporate tax on its other investment income, unfranked income and net realised gains.

From time to time the Board will offer a dividend reinvestment plan, although the DRP was suspended in respect of the interim dividend for the current reporting years.

### (n) Earnings per share

#### (i) Basic earnings per share

Basic earnings per share is calculated by dividing:

- the profit attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares
- by the weighted average number of ordinary shares outstanding during the financial year and adjusted for bonus elements in ordinary shares issued during the year.

#### (ii) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:

- the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares, and
- the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

### (o) Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of associated GST, unless the GST incurred is not recoverable from the taxation authority. In this case it is recognised as part of the cost of acquisition of the asset or as part of the expense.

## **2 Summary of significant accounting policies (continued)**

### **(o) Goods and Services Tax (GST) (continued)**

Where applicable, the Company qualifies for Reduced Input Tax Credits (RITC) at a rate of at least 75%; hence fees for these services have been recognised in the Statement of Comprehensive Income net of the amount of GST recoverable from the taxation authority.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included with other receivables or payables in the Statement of Financial Position.

Cash flows are presented on a gross basis. The GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to the taxation authority, are presented as operating cash flows.

### **(p) Rounding of amounts**

The Company is an entity of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 issued by the ASIC relating to the 'rounding off' of amounts in the financial statements. Amounts in the financial statements have been rounded to the nearest dollars in accordance with that ASIC Corporations Instrument, unless otherwise indicated.

### **(q) Comparatives**

Where necessary, comparative information has been reclassified to be consistent with current reporting period.

### **(r) Operating segments**

The Company operated in Australia only and the principal activity is investing.

## **3 Financial risk management**

The Company's financial instruments consist mainly of deposits with banks, trading portfolios, trade and other receivables and trade and other payables.

The Company's activities expose it to a variety of financial risks: market risk (including interest rate risk, foreign exchange risk and price risk), credit risk and liquidity risk. The Board of the Company has implemented a risk management framework to mitigate these risks.

### **(a) Market risk**

The standard defines this as the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices.

#### *(i) Price risk*

##### *Exposure*

The Company is exposed to currency risk arising from its investments denominated other than in Australian dollars. The Fund retains a natural hedge of its foreign exchange risk as it holds both assets and liabilities denominated in foreign currencies. Any residual foreign exchange risk is actively managed by the Investment Manager through its treasury management framework.

The Company seeks to manage and constrain market risk by diversification of the investment portfolio across multiple stocks and industry sectors. The portfolio is maintained by the Investment Manager within a range of parameters governing the levels of acceptable exposure to stocks and industry sectors. The relative weightings of the individual securities and relevant market sectors are reviewed normally weekly and risk can be managed by reducing exposure where necessary.

### 3 Financial risk management (continued)

#### (a) Market risk (continued)

The table below analyses the Company's concentration of price risk by region.

2016	Long Exposure	%	Short Exposure	%	Net Exposure
Australia	72,539,547	69.41%	(75,097,682)	70.48%	(2,558,135)
North America	15,665,970	14.99%	(20,192,557)	18.95%	(4,526,587)
Europe	13,825,664	13.23%	(11,261,948)	10.57%	2,563,716
Rest of World	2,481,679	2.37%	-	-	2,481,679
<b>Total</b>	<b>104,512,860</b>	<b>100.00%</b>	<b>(106,552,187)</b>	<b>100.00%</b>	<b>(2,039,327)</b>

2015	Long Exposure	%	Short Exposure	%	Net Exposure
Australia	67,176,369	87.64%	(63,433,007)	87.64%	3,743,362
North America	7,118,864	9.29%	(4,867,300)	6.73%	2,251,564
Europe	2,356,720	3.07%	(2,179,390)	3.01%	177,330
Rest of World	-	-	(1,894,177)	2.62%	(1,894,177)
<b>Total</b>	<b>76,651,953</b>	<b>100.00%</b>	<b>(72,373,874)</b>	<b>100.00%</b>	<b>4,278,079</b>

The North American region includes the United States and Canada. Europe includes countries in mainland Europe and the United Kingdom.

The Company's investment sectors as at 30 June 2016 and 30 June 2015 are as below:

Sector	2016 (%)	2015 (%)
Information technology	4.72	86.79
Financials	202.46	64.77
Energy	62.58	12.12
Healthcare and biotechnology	278.57	(72.66)
Consumer staples	223.47	(22.52)
Industrials	(86.70)	(2.13)
Consumer discretionary	(568.45)	137.81
Utilities	(135.09)	10.79
Materials	114.02	(114.97)
Telecommunications services	4.42	-
<b>Total</b>	<b>100.00</b>	<b>100.00</b>

As at 30 June 2016 no individual securities represented over 5 per cent of the long or short investment portfolio.  
As at 30 June 2015 two securities represented over 5% of the long or short investment portfolio.

#### Sensitivity

The following table illustrates the effect on the Company's equity from possible changes in other market risk that were reasonably possible based on the risk the Company was exposed to at reporting date, assuming a flat tax rate of 30 per cent:

	Impact on post-tax profit/(loss)	
	2016 \$	2015 \$
Decrease 5%	71,376	(149,733)
Increase 5%	(71,376)	149,733
Decrease 10%	142,753	(299,466)
Increase 10%	(142,753)	299,466

### 3 Financial risk management (continued)

#### (a) Market risk (continued)

Post-tax profit/(loss) for the year would decrease/increase as a result of gains/(losses) on equity securities classified as at fair value through profit or loss.

At balance date, the net portfolio position was \$2,039,327 short (2015: \$4,278,078 long) therefore there is a small price risk impact on post-tax profit (2015: post-tax loss).

#### (ii) Foreign exchange risk

##### Exposure

The Company is exposed to currency risk arising from its investments denominated other than the Australian dollars. As there was a national hedge, the Investment Manager actively manages the Company's foreign exchange risk through its treasury management framework.

##### Sensitivity

The analysis is based on the assumption that the Australian dollar weakened and strengthened by 10% (2015:10%) against the foreign currencies to which the Company is exposed. The impact on post-tax profit for the year (2015: post-tax loss) would be \$9,745 higher/\$9,745 lower (2015: \$37,430 lower/\$37,430 higher).

#### (iii) Cash flow and fair value interest rate risk

The Company's interest bearing financial assets expose it to risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The risk is measured using sensitivity analysis.

The table below summarises the Company's exposure to interest rate risks. It includes the Company's assets and liabilities at fair values, categorised by the earlier of contractual repricing or maturity dates.

#### At 30 June 2016

	Floating interest rate \$	Non- interest bearing \$	Total \$
<b>Financial assets</b>			
Cash and cash equivalents	93,247,732	-	93,247,732
Trade and other receivables	-	4,179,652	4,179,652
Financial assets held at fair value through profit or loss	-	104,512,860	104,512,860
Current tax assets	-	1,534,384	1,534,384
	<u>93,247,732</u>	<u>110,226,896</u>	<u>203,474,628</u>
<b>Financial liabilities</b>			
Trade and other payables	-	(4,869,408)	(4,869,408)
Financial liabilities held at fair value through profit or loss	-	(106,552,187)	(106,552,187)
	-	<u>(111,421,595)</u>	<u>(111,421,595)</u>
Net exposure to interest rate risk	<u>93,247,732</u>	<u>(1,194,699)</u>	<u>92,053,033</u>

### 3 Financial risk management (continued)

#### (a) Market risk (continued)

At 30 June 2015

	Floating interest rate \$	Non- interest bearing \$	Total \$
<b>Financial assets</b>			
Cash and cash equivalents	77,318,497	-	77,318,497
Trade and other receivables	-	8,193,429	8,193,429
Financial assets held at fair value through profit or loss	-	76,651,953	76,651,953
Current tax assets	-	2,689,021	2,689,021
	<u>77,318,497</u>	<u>87,534,403</u>	<u>164,852,900</u>
<b>Financial liabilities</b>			
Trade and other payables	-	(9,047,727)	(9,047,727)
Financial liabilities held at fair value through profit or loss	-	(72,373,875)	(72,373,875)
	<u>-</u>	<u>(81,421,602)</u>	<u>(81,421,602)</u>
 Net exposure to interest rate risk	 <u>77,318,497</u>	 <u>6,112,801</u>	 <u>83,431,298</u>

#### *Sensitivity*

At 30 June 2016, if interest rates had increased by 75 or decreased by 75 basis points from the year end rates with all other variables held constant, post-tax profit for the year would have been \$489,551 higher/\$489,551 lower (2015 changes of 75 bps/75 bps: \$405,922 lower/\$405,922 higher on post-tax loss), mainly as a result of higher/lower interest income from cash and cash equivalents.

#### (b) Credit risk

The standard defines this as the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

Under the arrangements which the Company has entered into to facilitate stock borrowing for covered short selling, borrowed stock is collateralised by the long stock portfolio. If the stock borrowing counterparty became insolvent, it is possible that the Company may not recover all of the collateral that the Fund gave to the counterparty. The collateral on securities sold short is set at 100% (2015: 100%) of the borrowed stock.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the Statement of Financial Position and Notes to the Financial Statements.

Credit risk is managed as noted in Note 8 with respect to cash and cash equivalents, Note 9 for trade and other receivables and Note 10 for financial assets at fair value through profit or loss. None of these assets are over-due or considered to be impaired.

#### (c) Liquidity risk

The standard defines this as the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

The Investment Manager monitors its cash-flow requirements daily in relation to the investing account taking into account upcoming dividends, tax payments and investing activity.

### 3 Financial risk management (continued)

#### (c) Liquidity risk (continued)

The Company's inward cash flows depend upon the level of dividend and distribution revenue received. Should these decrease by a material amount, the Company would amend its outward cash flows accordingly. As the Company's major cash outflows are the purchase of securities and dividends paid to shareholders, the level of both of these is managed by the Board and Investment Manager.

The assets of the Company are largely in the form of readily tradeable securities which can be sold on-market if necessary.

#### *Maturities of financial liabilities*

The tables below analyse the Company's non-derivative financial liabilities into relevant maturity groupings based on their contractual maturities at year end date.

The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

Contractual maturities of financial liabilities	Less than 1 month \$	Total contractual undiscounted cash flows \$
<b>At 30 June 2016</b>		
<b>Non-derivatives</b>		
Trade and other payables	4,869,408	4,869,408
Financial liabilities at fair value through profit or loss	106,552,187	106,552,187
Total non-derivatives	111,421,595	111,421,595

Contractual maturities of financial liabilities	Less than 1 month \$	Total contractual undiscounted cash flows \$
<b>At 30 June 2015</b>		
<b>Non-derivatives</b>		
Trade and other payables	9,047,727	9,047,727
Financial liabilities at fair value through profit or loss	72,373,875	72,373,875
Total non-derivatives	81,421,602	81,421,602



#### 4 Fair value measurements

The Company measures and recognises the following assets and liabilities at fair value on a recurring basis:

- Financial assets and financial liabilities at fair value through profit or loss (FVTPL)

The Company has no assets or liabilities measured at fair value on a non-recurring basis in the current reporting period.

##### (a) Fair value hierarchy

AASB 13 requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

- quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices) (level 2), and
- inputs for the asset or liability that are not based on observable market data (unobservable inputs) (level 3).

##### (i) Recognised fair value measurements

The following table presents the Company's assets and liabilities measured and recognised at fair value at year end.

	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
<b>At 30 June 2016</b>				
<b>Financial assets</b>				
Equity securities	72,539,547	-	-	72,539,547
Equity securities international	31,593,711	-	-	31,593,711
Unlisted equity securities	-	379,602	-	379,602
<b>Total financial assets</b>	<b>104,133,258</b>	<b>379,602</b>	<b>-</b>	<b>104,512,860</b>
<b>Financial liabilities</b>				
Equity securities sold short	75,056,531	-	-	75,056,531
Equity securities international	31,454,505	-	-	31,454,505
Unlisted equity securities	-	41,151	-	41,151
<b>Total financial liabilities</b>	<b>106,511,036</b>	<b>41,151</b>	<b>-</b>	<b>106,552,187</b>
<b>At 30 June 2015</b>				
<b>Financial assets</b>				
Equity securities	66,125,105	-	-	66,125,105
Equity securities international	9,475,584	-	-	9,475,584
Unlisted equity securities	-	1,051,264	-	1,051,264
<b>Total financial assets</b>	<b>75,600,689</b>	<b>1,051,264</b>	<b>-</b>	<b>76,651,953</b>
<b>Financial liabilities</b>				
Equity securities sold short	63,391,858	-	-	63,391,858
Equity securities international	8,940,866	-	-	8,940,866
Unlisted equity securities	-	41,151	-	41,151
<b>Total financial liabilities</b>	<b>72,332,724</b>	<b>41,151</b>	<b>-</b>	<b>72,373,875</b>

## 4 Fair value measurements (continued)

### (a) Fair value hierarchy (continued)

Included within Level 1 of the hierarchy are listed investments. The fair value of these financial assets and liabilities have been based on the last sale prices at the end of the reporting year, excluding transaction costs.

The majority of the investments included in Level 2 of the hierarchy include amounts in relation to Initial Public Offerings and Placements in which the Company has subscribed to during the year. These investments have not listed on the Australian Securities Exchange as at year end and therefore represent investments in an inactive market. In valuing these unlisted investments, included in Level 2 of the hierarchy, the fair value has been determined using the valuation technique of the subscription price and the amount of securities subscribed for by the Company under the relevant offers.

There were transfers between levels 1 and 2 for recurring fair value measurements during the year, relating to the listing of the unlisted equity securities as at year end. There were no transfers in and out of level 3.

The Company's policy is to recognise transfers into and transfers out of fair value hierarchy levels as at the end of the reporting period.

### (ii) Disclosed fair values

For all financial instruments other than those measured at fair value their carrying value approximates fair value.

The carrying amounts of trade and other receivables and payables are reasonable approximations of their fair values due to their short-term nature.

## 5 Critical accounting estimates and judgements

### (a) Significant estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity and that are believed to be reasonable under the circumstances.

### (b) Critical accounting estimates and assumptions

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

## 6 Segment information

The Company has only one reportable segment. The Company operates in one industry being the securities industry, deriving revenue from dividend and trust distribution income, interest income and from the sale of its trading portfolio.

## 7 Income tax expense/(benefit)

### (a) Income tax expense/(benefit) through profit or loss

	Year ended	
	2016	2015
	\$	\$
Deferred tax on temporary differences	(47,974)	(1,188,154)
Tax on permanent differences	3,042,137	92,642
Adjustments for current tax of prior periods	12,691	9,395
	<b>3,006,854</b>	<b>(1,086,117)</b>
<i>Income tax expense/(benefit) is attributable to:</i>		
Profit/(loss) from continuing operations	<b>3,006,854</b>	<b>(1,086,117)</b>

## 7 Income tax expense/(benefit) (continued)

### (b) Numerical reconciliation of income tax expense/(benefit) to prima facie tax payable/(receivable)

	Year ended	
	2016	2015
	\$	\$
Profit/(loss) from continuing operations before income tax expense/(benefit)	13,622,111	(1,839,349)
Tax at the Australian tax rate of 30.0%	4,086,633	(551,805)
Tax effect of amounts which are not deductible (taxable) in calculating taxable income:		
Franking credits on dividends received	(475,646)	(679,201)
Foreign tax credits on dividends received	(75,123)	(12,668)
Imputation credit gross up	142,694	203,760
Over-provision in prior year	12,691	9,395
Realised gain/loss not subject to tax	(667,669)	(83,356)
Franked dividends not subject to tax	(39,263)	23,958
Foreign tax gross up on dividend income	22,537	3,800
Income tax expense/(benefit)	3,006,854	(1,086,117)

The applicable weighted average effective tax rates are as follows: 22.07% (59.05)%

The positive effective tax rate in the current year is mainly due to profits realised, net of gains from securities that are not subject to tax. The negative effective tax rate in the prior year was mainly due to losses incurred and franking credits received.

### (c) Amounts recognised directly in equity

		Year ended	
	Notes	2016	2015
		\$	\$
Aggregate deferred tax arising in the reporting period and not recognised in net profit or loss or other comprehensive income but directly debited or credited to equity:			
Net deferred tax - debited (credited) directly to equity	11, 14	241,240	346,828

## 8 Current assets - Cash and cash equivalents

	At	
	2016	2015
	\$	\$
<b>Current assets</b>		
Cash at bank	40,247,732	24,318,497
Term Deposits	53,000,000	53,000,000
	93,247,732	77,318,497

## 8 Current assets - Cash and cash equivalents (continued)

### (a) Risk exposure

The Company's exposure to interest rate risk is discussed in Note 3. The maximum exposure to credit risk at the end of the reporting period is the carrying amount of each class of cash and cash equivalents mentioned above.

Cash investments are made with the following financial institutions:

	Standard & Poor's Rating
Australia and New Zealand Banking Group Ltd	AA-
UBS AG Investment Bank	A+
National Australia Bank	AA-

## 9 Current assets - Trade and other receivables

	At	
	2016	2015
	\$	\$
Dividends and distributions receivable	461,574	127,673
Interest receivable	252,115	255,051
GST receivable	275,064	83,322
Unsettled trades	3,190,899	7,727,383
	<u>4,179,652</u>	<u>8,193,429</u>

Receivables are non-interest bearing and unsecured.

### Fair value and credit risk

Due to the short-term nature of these receivables, the carrying amounts are reasonable approximations of their fair values.

## 10 Current assets - Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are all held for trading and include the following:

	At	
	2016	2015
	\$	\$
International listed equity securities	31,593,711	9,475,584
Australian listed equity securities	72,539,547	66,125,105
Other unlisted equity securities	379,602	1,051,264
<b>Total securities</b>	<u>104,512,860</u>	<u>76,651,953</u>

The market values of all investments as at 30 June 2016 are disclosed on page 7 of the Annual Report.

Listed securities are readily saleable with no fixed terms.

Changes in fair values of financial assets at fair value through profit or loss are recorded in investment income in the Statement of Comprehensive Income.

## 10 Current assets - Financial assets at fair value through profit or loss (continued)

### (a) Investment transactions

The total number of contract notes that were issued for transactions in securities during the financial year was 4,110 (2015: 3,509). Each investment transaction may involve multiple contract notes.

The total brokerage paid on these contract notes was \$3,067,594 (2015: \$2,700,128).

### (b) Risk exposure and fair value measurements

Information about the Company's exposure to price risk and about the methods and assumptions used in determining fair value is provided in Note 3.

## 11 Non-current assets - Deferred tax assets

	2016 \$	At 2015 \$
<b>The balance comprises temporary differences attributable to:</b>		
Tax losses	23	22,746
Capitalised share issue costs	241,240	346,828
Accrued expenses	12,729	8,581
	<u>253,992</u>	<u>378,155</u>
<b>Movements</b>		<b>Total \$</b>
<b>At 1 July 2014</b>		468,314
(Charged)/credited		
- to profit or loss		21,922
- directly to equity		(112,081)
<b>At 30 June 2015</b>		<u>378,155</u>
<b>At 1 July 2015</b>		378,155
(Charged)/credited		
- to profit or loss		(18,575)
- directly to equity		(105,588)
<b>At 30 June 2016</b>		<u>253,992</u>

## 12 Current liabilities - Trade and other payables

	At	
	2016	2015
	\$	\$
Management fees payable	84,406	73,247
Performance fees payable	2,951,347	-
Unsettled trades	1,235,149	8,053,216
Interest payable	105,480	120,117
Other payables	493,026	801,147
	<u>4,869,408</u>	<u>9,047,727</u>

Trade and other payables are unsecured and are usually paid within 30 days of recognition.

Due to the short-term nature of these payables, the carrying amounts are reasonable approximations of their fair values.

## 13 Current liabilities - Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss are all held for trading and include the following:

	At	
	2016	2015
	\$	\$
International listed equity securities sold short	31,454,505	8,940,867
Australian listed equity securities sold short	75,056,531	63,391,857
Other unlisted equity securities sold short	41,151	41,151
	<u>106,552,187</u>	<u>72,373,875</u>

A short sale occurs when the Investment Manager borrows a security and sells the security on market to a third party, generating cash proceeds. The Investment Manager will reacquire the same security and return it to the lender to close the transaction. In doing so, the Company is exposed to price risk of those securities sold short.

## 14 Non-current liabilities - Deferred tax liabilities

	At	
	2016	2015
	\$	\$
<b>The balance comprises temporary differences attributable to:</b>		
Net unrealised gains on investments	96,802	196,469
Other temporary differences	59,011	3,168
	<u>155,813</u>	<u>199,637</u>

## 14 Non-current liabilities - Deferred tax liabilities (continued)

Movements	Total \$
<b>At 1 July 2014</b>	1,388,617
Charged/(credited) - profit or loss	(1,188,980)
<b>At 30 June 2015</b>	<u>199,637</u>
<b>At 1 July 2015</b>	199,637
Charged/(credited) - profit or loss	(43,824)
<b>At 30 June 2016</b>	<u>155,813</u>

## 15 Issued capital

### (a) Share capital

	Notes	30 June 2016 Shares	30 June 2015 Shares	2016 \$	2015 \$
Ordinary shares	15(b)	<b>87,120,041</b>	84,104,755	<b>86,552,644</b>	83,474,683

### (b) Movements in ordinary share capital

Details	Notes	Number of shares	\$
Opening balance 1 July 2014		84,356,386	83,214,877
On-market buy back	15(g)	(3,505,642)	(2,967,298)
Options exercised	15(e)	2,983,171	2,983,171
DRP shares issued for dividend payment	15(d)	270,840	251,654
Cost of issued capital		-	(7,721)
Closing balance 30 June 2015		<u>84,104,755</u>	<u>83,474,683</u>
Opening balance 1 July 2015		84,104,755	83,474,683
On-market buy back	15(g)	(10,000)	(9,500)
Share placement shares issued	15(f)	3,025,286	3,116,045
Cost of issued capital		-	(28,584)
Closing balance 30 June 2016		<u>87,120,041</u>	<u>86,552,644</u>

### (c) Ordinary shares

Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of and amounts paid on the shares held.

On a show of hands every holder of ordinary shares present at a meeting in person or by proxy, is entitled to one vote, and upon a poll each share is entitled to one vote.

## **15 Issued capital (continued)**

### **(d) Dividend reinvestment plan**

The Company has established a dividend reinvestment plan "DRP" under which holders of ordinary shares may elect to have all or part of their dividend entitlements satisfied by the issue of new ordinary shares rather than by being paid in cash. Shares are issued under the plan at a discount to the market price. The discount is determined from time to time and is capped at 3%. Prior year the DRP price was \$0.9292.

### **(e) Option Issue**

On 15 July 2013, as part of IPO the Company issued options to acquire ordinary shares in the Company at an exercise price of \$1.00 with expiry 31 December 2014.

Since issue total 6,808,381 options have been exercised and allotted for a total consideration of \$6,808,381. On 31 December 2014, 63,710,244 options expired.

### **(f) Share placement**

A share purchase plan was announced to the market on 13 February 2016, the offer period from 15 February 2016 to 1 April 2016. This offer to eligible shareholders was to apply for up to \$15,000 worth of ordinary shares. A total of 3,025,286 shares were issued, at the issue price of \$1.03.

### **(g) Share buy-back**

In the prior year the Company announced a 12 months on-market share buy-back program on 12 August 2014 that expired 26 August 2015. During the period, the Company had bought 3,505,642 shares at an average price of \$0.8464.

The Company renewed the share buy-back program for 12 months from 14 September 2015 and has bought back 10,000 shares at an average price of \$0.95.

### **(h) Capital risk management**

The Board of Directors will actively manage the capital of the Company. The overriding intention is to deliver value to shareholders.

To achieve this the Board monitor the monthly NTA results, investment performance, the Company's Indirect Cost Ratio and share price movements.

The Company is not subject to any externally imposed capital requirements.

## **16 Reserves and accumulated losses**

### **(a) Reserves**

	<b>2016</b>	<b>At</b>	<b>2015</b>
	<b>\$</b>		<b>\$</b>
Profits reserve	<b>6,364,468</b>		888,365

This reserve details an amount preserved for future dividend payments as outlined in accounting policy Note 2(l).



## 16 Reserves and accumulated losses (continued)

### (a) Reserves (continued)

	Notes	2016 \$	At 2015 \$
<b>Movements:</b>			
Opening balance		888,365	4,819,638
Transfer from current and retained earnings		10,627,925	-
Dividends paid	17	(5,151,822)	(3,931,273)
Closing balance		<u>6,364,468</u>	<u>888,365</u>

### (b) Accumulated losses

Movements in accumulated losses were as follows:

	2016 \$	At 2015 \$
Opening balance	(753,232)	-
Net profit/(loss) for the year	10,615,257	(753,232)
Transfer (to) profits reserve	(10,627,925)	-
Closing balance	<u>(765,900)</u>	<u>(753,232)</u>

## 17 Dividends

### (a) Dividend rate

Dividends paid and the applicable franking rates are noted in the table below.

	Dividend Rate	Total Amount	Date of Payment	% Franked
<b>2016</b>				
Ordinary shares - interim special 2016	\$0.010	\$871,201	29/04/2016	50
Ordinary shares - interim 2016	\$0.025	\$2,178,002	29/04/2016	50
Ordinary shares - final 2015	\$0.025	\$2,102,619	20/10/2015	50
<b>Total</b>		<b>\$5,151,822</b>		
<b>2015</b>				
Ordinary shares - interim 2015	\$0.020	\$1,747,948	14/04/2015	70
Ordinary shares - final 2014	\$0.025	\$2,183,325	20/10/2014	100
<b>Total</b>		<b>\$3,931,273</b>		

## 17 Dividends (continued)

### (b) Dividends not recognised at the end of the reporting period

Year ended	
2016	2015
\$	\$

In addition to the above dividends, since year end the Directors have recommended the payment of a final dividend of 3.0 cents per fully paid ordinary share (2015: 2.5 cents), 75% franked (2015: 50% franked) based on tax paid at 30%. The aggregate amount of the proposed dividend with an ex date of 4 October 2016 and a record date of 5 October 2016, expected to be paid on 20 October 2016 out of the profits reserve at 30 June 2016, but not recognised as a liability at year end, is

<b>2,613,601</b>	2,102,619
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### (c) Dividend franking account

The franked portions of the final dividends recommended after 30 June 2016 will be franked out of existing franking credits or out of franking credits arising from the payment of income tax in the year ended 30 June 2017.

2016	2015
\$	\$

Opening balance of franking account	2,316,721	145,502
Franking credits on dividends received	634,772	710,872
Tax paid during the year	4,448,648	2,952,113
Franking credits on ordinary dividends paid	(1,103,965)	(1,460,095)
Franking credits lost under 45 day rule	(159,127)	(31,671)
Franking credits on tax refund received	(2,689,020)	-
Closing balance of franking account	<b>3,448,029</b>	2,316,721

Adjustments for tax payable/refundable in respect of the current year's profits (2015: loss) and the receipt of dividends	<b>(1,445,117)</b>	(2,665,878)
Adjusted franking account balance	<b>2,002,912</b>	(349,157)

Impact on the franking account of dividends proposed or declared before the financial report authorised for issue but not recognised as a distribution to equity holders during the year	<b>(840,086)</b>	(450,561)
Franking credits available/(shortfall) for subsequent reporting years based on a tax rate of 30.0%	<b>1,162,826</b>	(799,718)

The Company's ability to continue to pay franked dividends is dependent upon the receipt of franked dividends from investments and the payment of tax.

## 18 Key management personnel disclosures

### (a) Key management personnel compensation

	Year ended	
	2016	2015
	\$	\$
Short-term employee benefits	118,721	118,721
Post-employment benefits	11,279	11,279
	<u>130,000</u>	<u>130,000</u>

Detailed remuneration disclosures are provided in the remuneration report on pages 16 to 19.

### (b) Equity instrument disclosures relating to key management personnel

#### (i) Option holdings

The numbers of options over ordinary shares in the Company that were held during the financial year by each Director of Watermark Market Neutral Fund Limited and other key management personnel of the Company, including their personally related parties, are set out below.

None of the key management personnel held options during the year ended 30 June 2016.

2015 Name	Balance at start of the year	Granted	Forfeited	Balance at 30 June 2015
<b>Directors of Watermark Market Neutral Fund Limited</b>				
Matthew Kidman	50,000	-	(50,000)	-
Justin Braitling	200,000	-	(200,000)	-
John Abernethy	-	-	-	-
Stephen Van Eyk	-	-	-	-
Robert Ferguson	1,000,000	-	(1,000,000)	-
	<u>1,250,000</u>	-	<u>(1,250,000)</u>	-

#### (ii) Share holdings

The numbers of shares in the Company held during the financial year by each Director of Watermark Market Neutral Fund Limited and other key management personnel of the Company, including their personally related parties, are set out below. There were no shares granted during the reporting period as compensation.

2016 Name	Balance at the start of the year	Net movement	Balance at 30 June 2016
<b>Directors of Watermark Market Neutral Fund Limited</b>			
<b>Ordinary shares</b>			
Matthew Kidman	50,000	14,563	64,563
Justin Braitling	683,001	30,000	713,001
John Abernethy	-	-	-
Stephen Van Eyk	48,780	66,646	115,426
Robert Ferguson	1,000,000	-	1,000,000
	<u>1,781,781</u>	<u>111,209</u>	<u>1,892,990</u>

## 18 Key management personnel disclosures (continued)

### (b) Equity instrument disclosures relating to key management personnel (continued)

2015 Name	Balance at the start of the year	Net movement	Balance at 30 June 2015
<b>Directors of Watermark Market Neutral Fund Limited</b>			
<b>Ordinary shares</b>			
Matthew Kidman	50,000	-	50,000
Justin Braitling	200,001	483,000	683,001
John Abernethy	-	-	-
Stephen Van Eyk	48,780	-	48,780
Robert Ferguson	1,000,000	-	1,000,000
	<u>1,298,781</u>	<u>483,000</u>	<u>1,781,781</u>

## 19 Remuneration of auditors

During the year the following fees were paid or payable for services provided by the auditor of the Company, its related practices and non-related audit firms:

### Pitcher Partners

#### (i) Audit and other assurance services

	Year ended	
	2016	2015
	\$	\$
<i>Audit and other assurance services</i>		
Audit and review of financial statements	<u>42,227</u>	38,866
Total remuneration for audit and other assurance services	<u>42,227</u>	38,866
<i>Taxation services</i>		
Tax compliance services	<u>17,848</u>	9,680
Total remuneration	<u>60,075</u>	48,546

The Company's Audit Committee oversees the relationship with the Company's External Auditors. The Audit Committee reviews the scope of the audit and the proposed fee. It also reviews the cost and scope of other services provided by the audit firm, to ensure that they do not compromise independence.

## 20 Contingencies

The Company had no contingent liabilities at 30 June 2016 (2015: nil).

## **21 Related party transactions**

### **(a) Key management personnel**

Disclosures relating to key management personnel are set out in Note 18.

### **(b) Transactions with other related parties**

All transactions with related entities were made on normal commercial terms and conditions no more favourable than those available to other parties unless otherwise stated.

Justin Braitting is a Director and owner of Watermark Funds Management Pty Limited, the entity appointed to manage the investment portfolio of Watermark Market Neutral Fund Limited. In its capacity as manager, Watermark Funds Management Pty Limited was paid a management fee of 1% p.a. (plus GST) on the net value of the portfolio amounting to \$925,571 (2015: \$861,539).

As at 30 June 2016, the balance payable to the Investment Manager was \$84,406 (2015: \$73,247).

In addition, Watermark Funds Management Pty Limited is to be paid, annually in arrears, a performance fee being 20% of:

- where the level of the Reserve Bank of Australia's cash-rate has increased over that year, the amount by which the Value of the Portfolio exceeds this increase; or
- where the Reserve Bank of Australia's cash-rate has decreased over that year, the amount of the increase in the Value of the Portfolio.

No performance fee is payable in respect of any performance period where the portfolio has decreased in value over that period. On the 19 May 2015, the Company announced, if the portfolio underperforms the benchmark over a financial year that underperformance is to be recouped before any entitled performance fee can be accrued.

For the year ended 30 June 2016 in its capacity as manager, Watermark Funds Management Pty Limited was paid a performance fee amounting to \$2,750,119 (2015: Nil).

No Director has received or become entitled to receive a benefit (other than those detailed above) by reason of a contract made by the Company or a related Company with the Director or with a firm of which he is a member or with a Company in which he has substantial financial interest.

Accounting and company secretarial duties are outsourced to White Outsourcing Pty Limited. Peter Roberts (resigned 27/04/2016) is a director and Matthew McShane (appointed 27/04/2016) is the Head of Operations of White Outsourcing Pty Limited which received fees net of reduced input tax credits of \$115,230 during the year (2015: \$113,127) for the services rendered pursuant to an Administrative Services Agreement entered into by the Company. As at 30 June 2016, the balance payable to White Outsourcing Pty Limited was \$16,776 (2015: \$7,830). Neither Mr Roberts nor Mr McShane received any fees as an individual. White Outsourcing Pty Limited is remunerated in accordance with the Service Level Agreement dated 25 June 2013. The agreement has no fixed term.

## **22 Events occurring after the reporting period**

Other than the dividend declared after year end, no other matter or circumstance has occurred subsequent to year end that has significantly affected, or may significantly affect, the operations of the Company, the results of those operations or the state of affairs of the Company in subsequent financial years.

## 23 Reconciliation of profit/(loss) after income tax to net cash inflow from operating activities

### (a) Reconciliation of profit/(loss) after income tax to net cash inflow from operating activities

	Year ended	
	2016	2015
	\$	\$
Profit/(loss) for the year	10,615,257	(753,232)
Fair value losses/(gains) on financial assets at fair value through profit or loss	6,317,405	(248,470)
Net exchange differences	(22,674)	(118,657)
Change in operating assets and liabilities:		
Decrease in trade and other receivables	4,013,777	2,376,046
Decrease/(increase) in other current assets	1,154,637	(2,689,021)
Decrease in deferred tax assets	136,413	93,468
Decrease in trade and other payables	(3,947,998)	(2,005,942)
Decrease in provision for income taxes payable	-	(253,697)
Decrease in deferred tax liabilities	(43,824)	(1,188,980)
Net cash inflow/(outflow) from operating activities	18,222,993	(4,788,485)

### (b) Non-cash financing activities

Dividends reinvested	-	251,654
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## 24 Earnings per share

### (a) Basic earnings per share

	Year ended	
	2016	2015
	Cents	Cents
Basic earnings per share attributable to the ordinary equity holders of the Company	12.52	(0.87)

### (b) Diluted earnings per share

	Year ended	
	2016	2015
	Cents	Cents
Diluted earnings per share attributable to the ordinary equity holders of the Company	12.52	(0.87)

Diluted earnings per share is the same as basic earnings per share. As at 30 June 2016 and 30 June 2015, the Company had no securities outstanding which have the potential to convert to ordinary shares and dilute the basic earnings per share.

## 24 Earnings per share (continued)

### (c) Weighted average number of shares used as denominator

	<b>2016 Number</b>	2015 Number
Weighted average number of ordinary shares used as the denominator in calculating basic earnings per share	<b>84,784,391</b>	86,922,158
Weighted average number of ordinary shares used as the denominator in calculating diluted earnings per share	<b>84,784,391</b>	86,922,158

**Watermark Market Neutral Fund Limited**  
**Directors' Declaration**  
**30 June 2016**

In the opinion of the directors of Watermark Market Neutral Fund Limited:

- (a) the financial statements and notes set out on pages 22 to 52 are in accordance with the *Corporations Act 2001*, including:
  - (i) complying with Australian Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements, and
  - (ii) giving a true and fair view of the Company's financial position as at 30 June 2016 and of its performance for the year ended on that date, and
- (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.
- (c) Note 2(a) confirms that the financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board, and
- (d) The Directors have been provided with the declarations required by section 295A of the *Corporations Act 2001* by Justin Braitling on behalf of the Manager, Watermark Funds Management Pty Limited, declaring that:
  - (i) the financial records of the Company for the financial year have been properly maintained in accordance with section 286 of the *Corporations Act 2001*;
  - (ii) the financial statements and notes for the financial year comply with the Accounting Standards; and
  - (iii) the financial statements and notes for the financial year give a true and fair view.

This declaration is made in accordance with a resolution of the Board of Directors.



Matthew Kidman  
Chairman

Sydney  
16 August 2016



**INDEPENDENT AUDITOR'S REPORT  
TO THE MEMBERS OF WATERMARK MARKET NEUTRAL FUND LIMITED  
ABN 45 163 980 498**

**Report on the Financial Report**

We have audited the accompanying financial report of Watermark Market Neutral Fund Limited (the Company), which comprises the statement of financial position as at 30 June 2016, the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information and the directors' declaration.

*Directors' Responsibility for the Financial Report*

The directors of Watermark Market Neutral Fund Limited are responsible for the preparation and fair presentation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 2, the directors also state that, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

*Auditor's Responsibility*

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**INDEPENDENT AUDITOR'S REPORT  
TO THE MEMBERS OF WATERMARK MARKET NEUTRAL FUND LIMITED  
ABN 45 163 980 498**

*Independence*

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

*Opinion*

In our opinion:

- a) the financial report of Watermark Market Neutral Fund Limited is in accordance with the *Corporations Act 2001*, including:
  - (i) giving a true and fair view of the Company's financial position as at 30 June 2016 and of its performance for the year ended on that date; and
  - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- b) the financial report also complies with International Financial Reporting Standards as disclosed in Note 2.

**Report on the Remuneration Report**

We have audited the Remuneration Report included in pages 16 to 19 of the directors' report for the year ended 30 June 2016. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

*Opinion*

In our opinion, the Remuneration Report of Watermark Market Neutral Fund Limited for the year ended 30 June 2016 complies with section 300A of the *Corporations Act 2001*.



S M WHIDDETT  
Partner

16 August 2016



PITCHER PARTNERS  
Sydney

**Watermark Market Neutral Fund Limited**  
**Shareholder information**  
**30 June 2016**

The Shareholder information set out below was applicable as at 31 July 2016.

Additional information required by the Australian Securities Exchange Limited Listing Rules and not disclosed elsewhere in this report, is listed below.

**A. Distribution of equity securities**

Analysis of numbers of equity security holders by size of holding:

Holding	Class of equity security		
	Ordinary shares		
	No. of Shareholders	Shares	Percentage
1 - 1000	70	34,404	0.04
1,001 - 5,000	200	616,029	0.71
5,001 - 10,000	293	2,578,596	2.96
10,001 - 100,000	1,377	49,930,061	57.31
100,001 and over	127	33,960,951	38.98
	2,067	87,120,041	100.00

There were 27 holders of less than a marketable parcel of ordinary shares.

**B. Equity security holders**

*Twenty largest quoted equity security holders*

Name	Ordinary shares	
	Number held	Percentage of issued shares
HSBC Custody Nominees (Australia) Limited	4,544,242	5.22
LIC Investments Pty Ltd <LIC Investments Unit A/C>	1,175,000	1.35
BNP Paribas Noms Pty Ltd <DRP>	1,102,330	1.27
Mr Robert Ferguson & Ms Jennifer Ferguson & Ms Rachel Ferguson <Torryburn Super Fund A/C>	1,000,000	1.15
Abbawood Nominees Pty Ltd <Abbott Family S/F No 1 A/C>	800,000	0.92
Bond Street Custodians Limited <RSALTE - D44396 A/C>	750,000	0.86
Penson Holdings Pty Ltd	700,000	0.80
Brayhope Pty Ltd <Jet Retirement Plan A/C>	684,111	0.79
Mr Stephen Richard Brown <The Adaptor A/C>	625,000	0.72
Horton Pty Ltd	494,563	0.57
C M Copeland Pty Ltd	472,232	0.54
Bond Street Custodians Limited <RSALTE - V17471 A/C>	450,000	0.52
Eliza Braitling Foundation Pty Limited	438,000	0.50
Zanacorp Financial Group Pty Ltd	437,500	0.50
Mr Willem Lasschuit & Mrs Rhonda Lasschuit <Lasschuit Inc SMSF A/C>	426,059	0.49
Sam Robert Fletcher <Fassway Investments A/C>	415,000	0.48
Mr James William Tonkin & Mrs Sharon Kathleen Tonkin <Tonkin Family S/F A/C>	401,800	0.46
Richjeca Pty Ltd <Richjeca A/C>	400,000	0.46
Wattles Nest Pty Ltd <Wattles Nest Super Fund A/C>	400,000	0.46
S & G Frisken Pty Limited <Frisken Family A/C>	348,039	0.40
	16,063,876	18.44

**C. Substantial holders**

There are no substantial shareholders.

**D. Voting rights**

The voting rights attaching to each class of equity securities are set out below:

Each share is entitled to one vote when a poll is called, otherwise each member present at a meeting or by proxy has one vote on a show of hands.

**E. Stock Exchange Listing**

Quotation has been granted for all of the ordinary shares and options of the Company on all Member Exchanges of the ASX Limited.

**F. Unquoted Securities**

There are no unquoted shares.

**G. Securities Subject to Voluntary Escrow**

There are no securities subject to voluntary escrow.