



WATERMARK

MARKET NEUTRAL FUND

NTA and Monthly Update – November 2018

Company at a Glance

ASX Code	WMK
Fund Size	AU\$72.1m
Fund Strategy	Equity Market Neutral
Share Price	\$0.81
Shares on Issue	82.2m

Net Tangible Asset (NTA) Backing

	Oct 18	Nov 18
NTA Before Tax	\$0.93	\$0.90
NTA After Tax	\$0.94	\$0.90

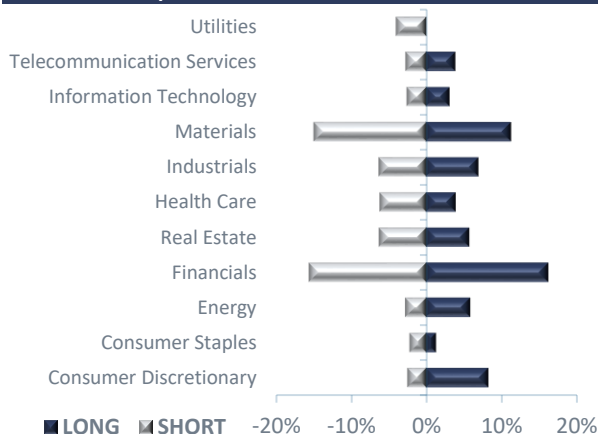
Gross Portfolio Structure

Long Exposure	88.8%	66.5%
Short Exposure	-86.4%	-67.0%
Gross Exposure	175.2%	133.6%
Cash	97.7%	100.5%

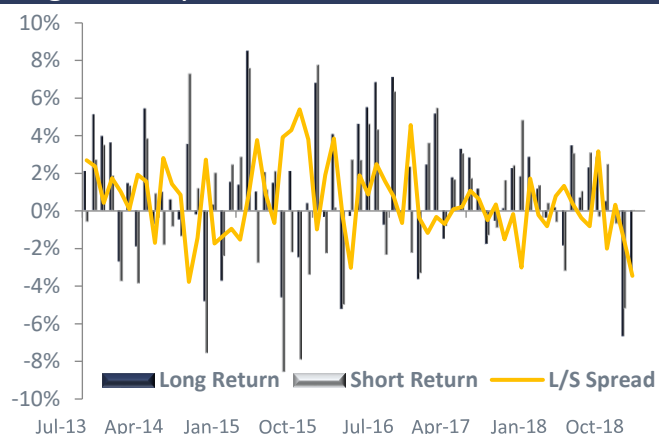
WMK Performance

	1 Mth	3 Mths	1 Yr	2 Yrs (pa)	3 Yrs (pa)	5 Yrs (pa)	S.I. (pa)
Portfolio Return (net)	-2.9%	-4.6%	-3.9%	-3.7%	-0.5%	2.6%	3.4%
RBA Cash Rate	0.1%	0.4%	1.5%	1.5%	1.6%	1.9%	2.0%
Outperformance (net)	-3.0%	-5.0%	-5.4%	-5.2%	-2.1%	0.7%	1.4%

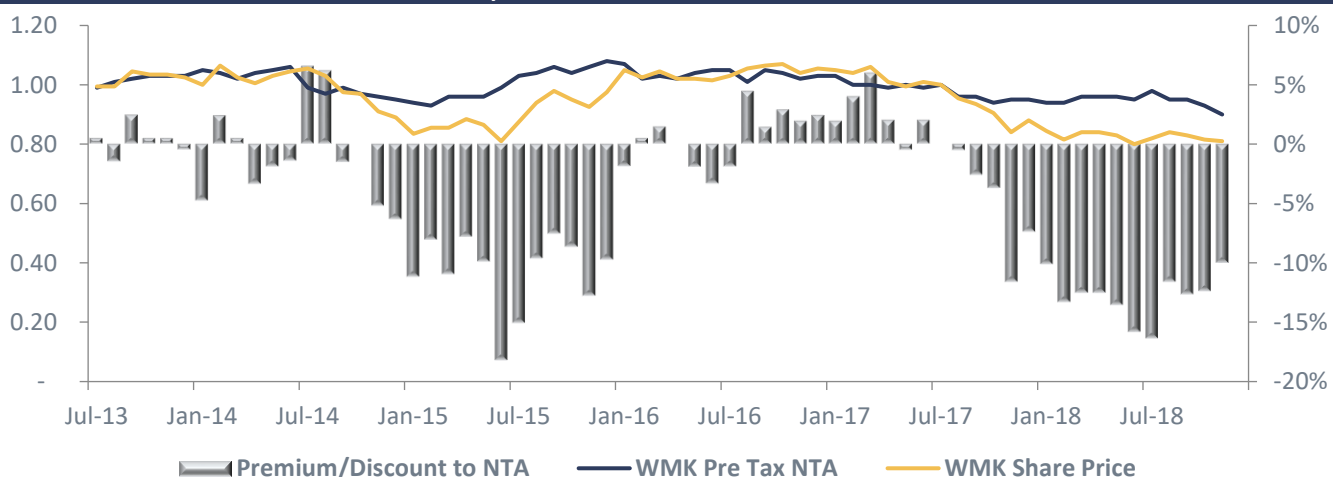
Sector Exposures



Long Short Spread



Premium/Discount to NTA History



Month in Review

The Australian share market was the worst performer amongst its developed market peers in November, falling by over 2%. Mining and Energy shares were the biggest contributors to this weakness, as prices of bulk commodities and oil tumbled through the month. The outlook for the domestic economy remains benign, with solid growth expectations and a strong labour market tempered by the weakness in the property sector, and the knock-on effects for a range of sectors such as construction and retail. Investor sentiment has turned, and capital flows into defensive sectors such as utilities and consumer staples suggest a waning appetite for risk from institutional investors.

November was a difficult month for the Fund, which fell by -2.9% after all fees. It has taken us some time to reposition the portfolio in light of developments in the share market in recent weeks, and we have been too slow in some cases to cut losses. Despite strong valuation support for high-quality investments in companies such as Aristocrat Leisure, Clydesdale Bank, Janus Henderson and James Hardie, these names continued to sell-off in the month, accounting for much of the negative performance.

We continue to position the Consumer portfolio for softening trends in discretionary spending. The Fund has a core investment in Aristocrat Leisure, reflecting the strength of the business and historic defensiveness of gaming expenditure. The company reported a solid FY18 result in November, however, the share price contracted as the company signalled plans for marketing investment in its newly acquired digital gaming division. While management has a strong track record of capital allocation and execution, the market currently has little appetite for uncertainty, particularly for a company stepping outside its core competency. Aristocrat delivered an outstanding outcome for investors with its first digital acquisition, Product Madness (2012), which we believe should be repeatable.

TMT exposures detracted from returns during the month. An investment in a New Zealand company Trade Me Group, benefitted from an indicative bid by Apax Partners to buy the business for \$6.40 per share (25% premium). Our stake in accounting software company MYOB continued to grind higher after KKR agreed to increase its indicative offer price to \$3.77, in order to progress to due diligence phase. Conversely, short positions in expensive Australian technology stocks suffered from better than expected earnings updates.

Financials also weighed on Fund returns as investors sold-off Clydesdale Bank, following its full-year result in November. Whilst the result was in line with market expectations, there are concerns around the outlook for margins, particularly in the recently acquired Virgin Money business. With a dual listing on both the London stock exchange and the ASX, Clydesdale was also dragged lower with the broader European and UK banking sector, amidst concerns over the economic impact of Brexit. Despite challenges in the near-term, we see an opportunity for the business once final approvals for the merger are obtained and the benefits of cost-out programs and revenue synergies are fully realised.

Chinese economic data continued to soften, weighing on mining shares in November. We have a modest net short bias in the sector, expecting a difficult period ahead for commodities as the Chinese property market cools in 2019. We exited our position in Lynas after the shares rallied ahead of an anticipated positive parliamentary review. The price of oil collapsed a further 20% as increasing supply from several regions met concern over the demand outlook, as the global economy slows. While we remain balanced in oil producers, our investment in Origin Energy detracted from performance.

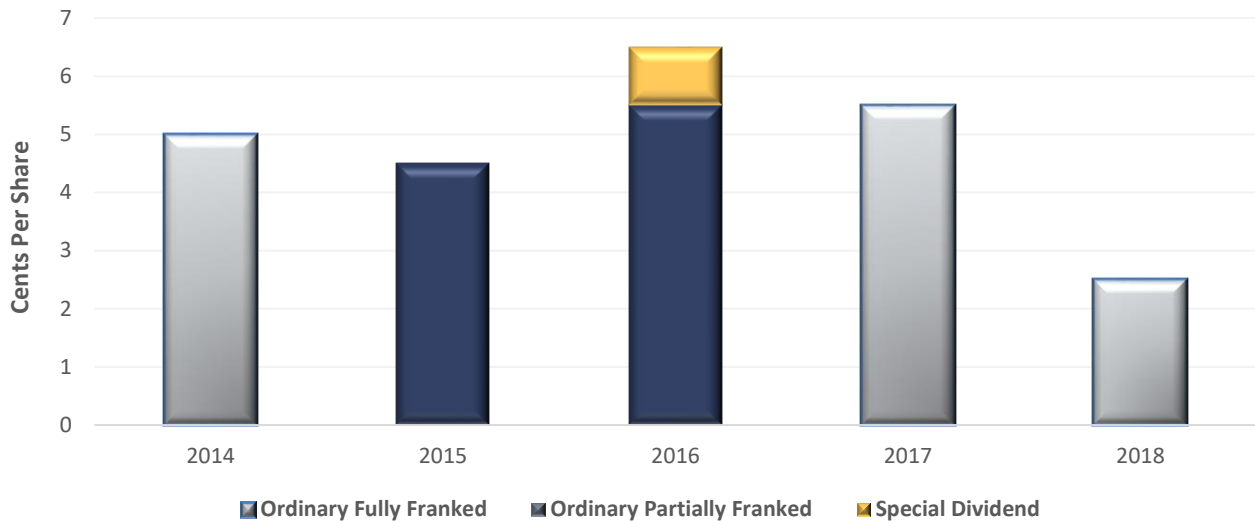
The US housing market has been growing steadily since the GFC, but at a pace that is still well below a longer term 'mid-cycle'. The continued rise in US interest rates and emerging affordability issues have resulted in a pullback in housing construction. Combined with a poor quarterly result, this led to a significant drop in the price of James Hardie shares. We have maintained our position as we believe the opportunity remains for increased penetration of their market leading product.

Australian Healthcare shares underperformed global peers, driven by selling in sector heavyweights CSL and Cochlear. Notwithstanding the recent sell-off, domestic healthcare valuations in many cases remain stretched and we expect lacklustre performance to continue as investors seek more attractive value opportunities elsewhere. The Healthcare portfolio was a positive contributor to returns in November and we retain a modest net short bias in this part of the portfolio.



Dividend History

The Board is committed to paying a consistent stream of franked dividends to shareholders, provided the Company has sufficient profit reserves and franking credits and that it is within prudent business practices. Dividends are paid on a six-monthly basis. A Dividend Reinvestment Plan is available to shareholders. Please contact Boardroom Limited for details on how to participate – 02 9290 9600; callcentre@boardroomlimited.com.au



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