

Investment Update and NTA Report

28 February 2015



Month in Review

Central bank action continued to be a major factor impacting the performance of global share markets in February. European markets were buoyed by the commencement of the ECB's quantitative easing program while speculation as to when the US Federal Reserve may begin raising rates, weighed on US shares.

On the domestic front, the RBA cut the cash rate as expected, signalling their ongoing expectation that growth in the domestic economy will be weak. This weak outlook was evident in softer employment data in January and disappointing investment expectations in business surveys. The rate cut sparked a strong rally, with the All Ordinaries rising by 6.9% for the month.

The portfolio delivered a return of 0.7% for the month. While this may look uninspiring given the strong market move, with no net exposure to the share market, returns are generated solely through stock selection. In fact it should be seen as a strong result in the context of the misfortune of having two short positions bid for in February, with Japan Post bidding for Toll Holdings and Novion Property Group merging with Federation Centres. In both cases we are convinced the short case was sound.

While fundamentals will invariably determine the success or failure of a long investment (sometimes luck plays a role), with shorts comes occasional exposure to irrational investment decisions which are not always fundamentally sound. Just consider the track record of corporate transactions - for every successful deal, history is littered with ill-conceived failures.

Every now and then we will be on the wrong side of these transactions. The first time we had one of our shorts bid for was under similar circumstances when the Japanese brewer Kirin bid \$6.5 billion for Lion Nathan in April 2009. That was a terrible transaction with Kirin overpaying and the business has struggled ever since. In our short portfolio, we can be exposed to this irrational behaviour. Sadly, the Toll profit result also announced on the day of the bid was very disappointing and the shares would have otherwise been a lot weaker.

To finish ahead for the month having carried these significant losses without any net market exposure was a solid result and indicates we also had a number of significant successes in the month of February. In particular, exposures in cyclical shares that have been out of favour in recent months saw strong gains in response to economic stimulus.

Net Tangible Asset (NTA) Backing

Month	January 2015	February 2015
NTA before tax on unrealised gains	\$0.94	\$0.95
NTA after tax	\$0.95	\$0.96
Dividend Declared*	(\$0.00)	(\$0.02)
NTA after tax and after dividend (2¢)	\$0.95	\$0.94

*The ex-date for the dividend is 26 March 2015, payable on 14 April 2015

Performance (Net of all Fees and Expenses)

Performance at 28 February 2015	1 Mth	6 Mths	Fin. YTD	1 Yr	3 Yrs pa	5 Yrs pa	Since Inception pa
WMK (net return)	0.7%	-2.0%	-8.0%	-5.0%	N/A	N/A	1.8%
RBA Cash Rate	0.2%	1.2%	1.7%	2.5%	N/A	N/A	2.5%
Outperformance (net)	0.5%	-3.3%	-9.7%	-7.5%	N/A	N/A	-0.7%

Watermark Market Neutral Fund

ASX Code	WMK
Listed	Jul 2013
Capital	\$82.6m
Market capitalisation	\$74.7m
Share price	\$0.86
NTA before tax	\$0.95
Shares on issue	87.4m
Interim Dividend (1H15)	2¢
Dividend yield	5.3%

Company Overview

The Watermark Market Neutral Fund (WMK) is a listed investment company that invests predominantly in Australian shares. The fund will maintain a market neutral structure with no greater than 10% of the company's assets exposed to the share market on a net basis at any one time. It is the Board's intention to try and deliver to shareholders a consistent and growing stream of fully franked dividends over time.

Investment Strategy

The primary goal of the investment process is the identification of mispriced securities. In a market neutral strategy the manager constructs two portfolios: a "long" portfolio of preferred shares and a "short" portfolio of less preferred shares. As the portfolios are roughly of equal size, this is a fully hedged structure aiming to minimise exposure to market movements. The fund profits to the extent the long portfolio outperforms the short portfolio plus the interest received on the fund's capital which is retained in cash.

Investment & Management Team

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Chief Investment Officer/
Portfolio Manager

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Joshua Ross
Investment Analyst

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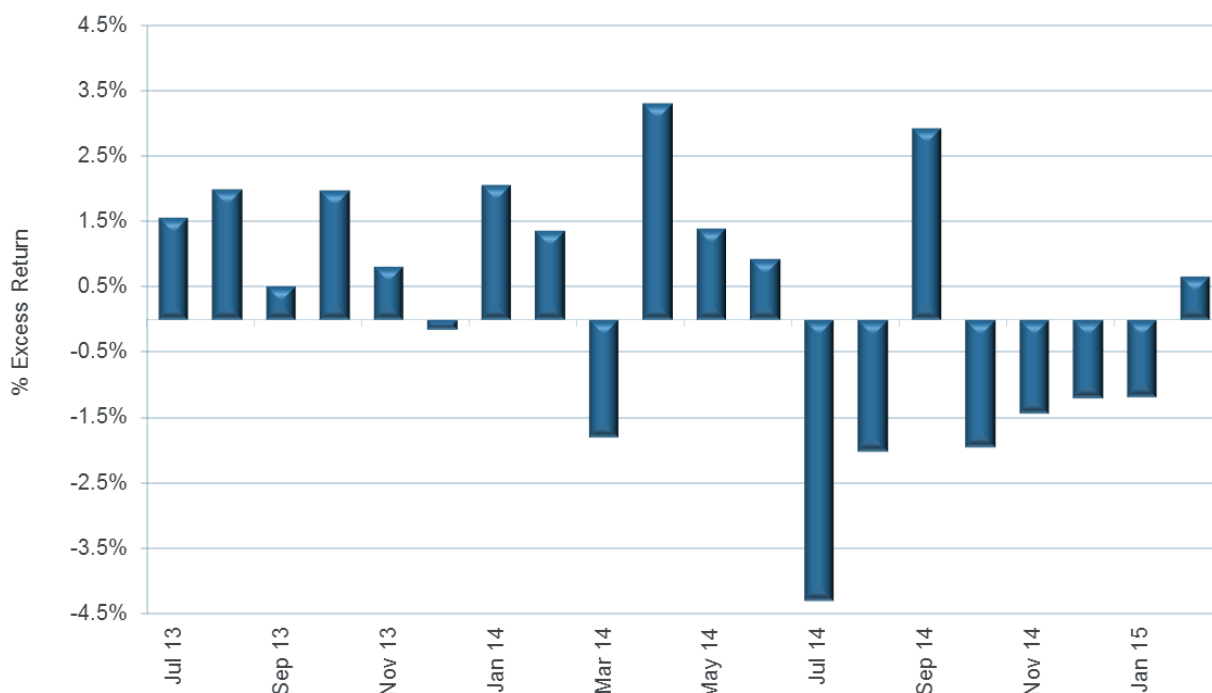
Shannon Wells
Office Manager

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Monthly Excess Returns (Gross Alpha)



Fund Attribution

In this strategy, shareholders benefit to the extent that shares in the long portfolio which the manager prefers outperform the shares in the short portfolio. In February, the Long Portfolio increased in value by 8.5%, outperforming the short portfolio which increased by 7.6%. Since inception the long portfolio has outperformed the short portfolio, resulting in a positive return for shareholders despite volatile markets.

	1 Month Return (%)	3 Month Return (%)	6 Month Return (%)	Financial YTD Return (%)
	Portfolio ¹	Portfolio ¹	Portfolio ¹	Portfolio ¹
Long Portfolio	8.5%	11.6%	2.6%	6.0%
Short Portfolio	7.6%	13.4%	4.4%	13.4%
Cash	0.1%	0.6%	1.0%	1.1%
Total	0.8%	-1.3%	-1.2%	-7.0%

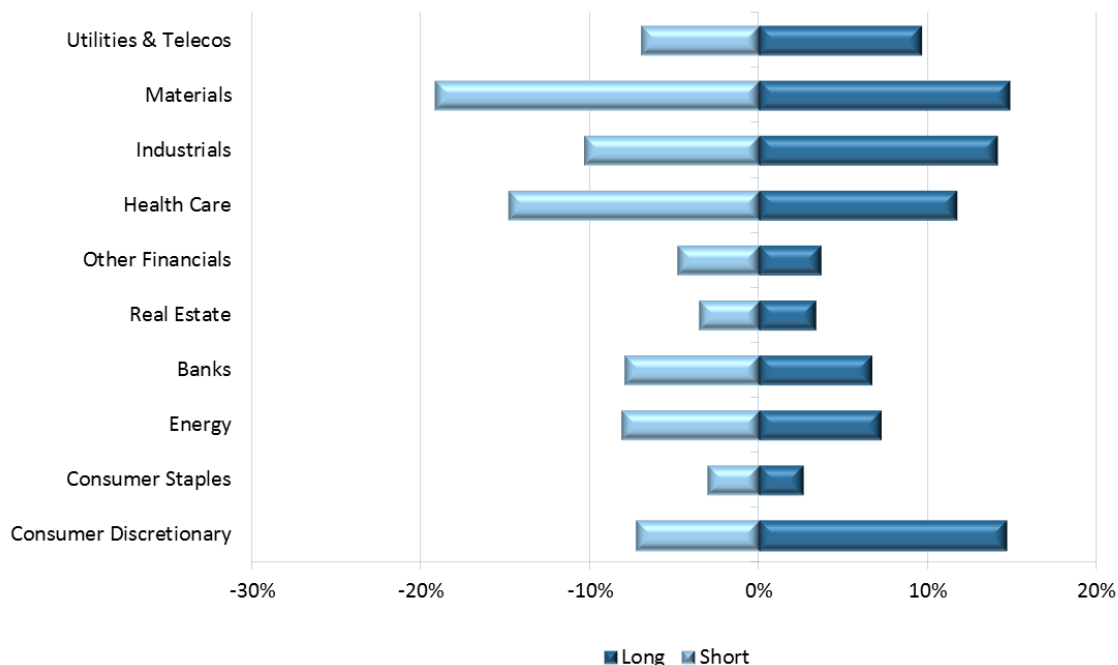
¹ The "Portfolio" column displays the return achieved in the period from the Investment Portfolio (long) and from the Borrowed Securities portfolio (short) separately. A negative return for the short portfolio is a good outcome and adds to performance. The Total Portfolio performance, representing the underlying return achieved on Shareholder's Funds is a weighted return of the long and short portfolios as well as cash.

Gross Portfolio Structure

Investment Type	31 January 2015		28 February 2015	
	\$m	%	\$m	%
Listed Securities - Long	77	94%	73	88%
Listed Securities - Short	-76	-93%	-72	-87%
Net Exposure	1	1%	1	1%
Cash	81	99%	82	99%
Capital	82	100%	83	100%

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Sector Exposures



Dividend History

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

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