



WATERMARK

MARKET NEUTRAL FUND

NTA and Monthly Update – March 2017

Company at a Glance

ASX Code	WMK
Fund Size	AU\$90.0m
Fund Strategy	Equity Market Neutral
Share Price	\$1.06
Shares on Issue	87.1m
Dividend (HY17 Interim)	3 cents
Dividend Yield (annualised)	5.7%

Net Tangible Asset (NTA) Backing

	Feb 17	Mar 17
NTA Before Tax	\$1.03	\$1.03
NTA After Tax	\$1.03	\$1.03
Dividend Declared (3¢)	(\$0.03)	(\$0.03)
NTA After Tax \$ Dividend (3¢)	\$1.00	\$1.00

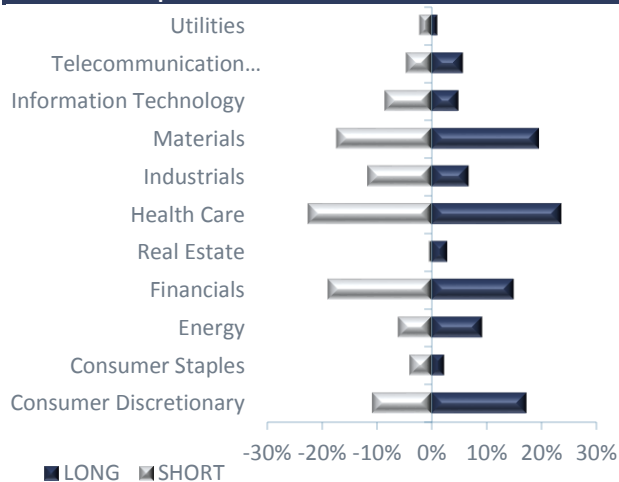
Gross Portfolio Structure

Long Exposure	112.7%	108.1%
Short Exposure	-116.8%	-107.9%
Gross Exposure	229.6%	216.0%
Cash	104.1%	99.8%

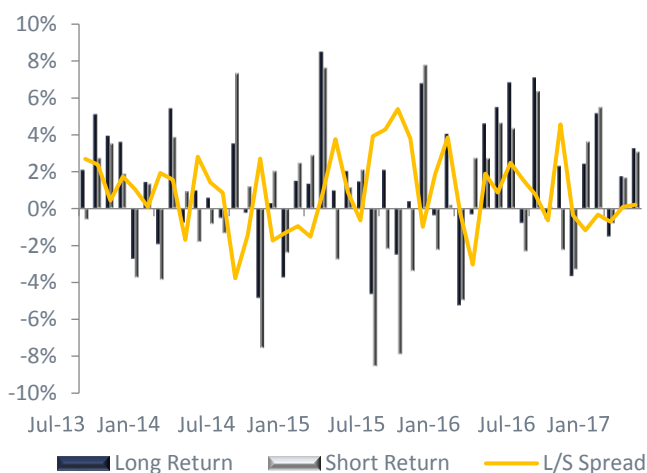
WMK Performance

	1 Mth	6 Mths	FYTD	1 Yr	S.I. (pa)
Portfolio Return (net)	0.0%	-2.3%	0.2%	3.6%	6.8%
RBA Cash Rate	0.1%	0.8%	1.2%	1.6%	2.2%
Outperformance (net)	-0.1%	-3.1%	-1.0%	2.0%	4.6%

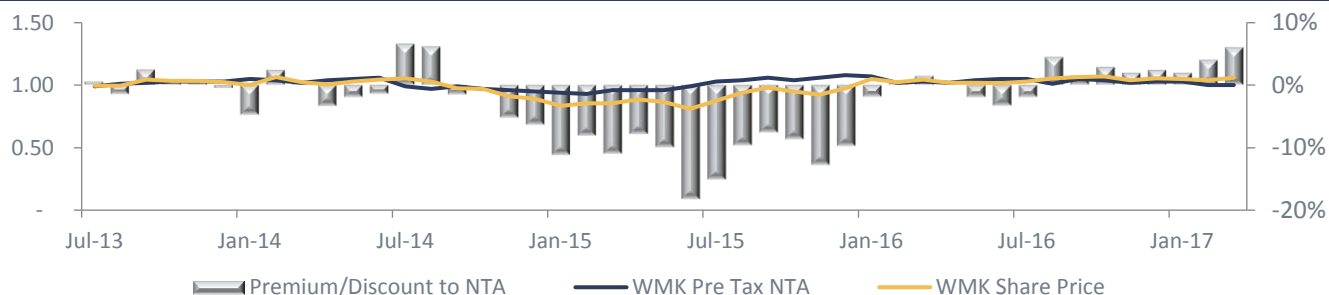
Sector Exposures



Long Short Spread*



Premium/Discount to NTA History





Month in Review

Global equity markets moved higher in March, showing continued resilience in the face of growing geopolitical risks including numerous challenges for the Trump administration in executing its pro-growth policy agenda and the looming prospect of a new populist government in France. Economies in Europe and the US continue to show signs of continued (albeit modest) growth, providing Central Banks with confidence to push ahead with plans to wind back stimulatory measures and lift interest rates.

The Australian share market also performed strongly, flirting with a post-GFC high but again falling short. Gains were widespread across sectors, driven by an improved earnings outlook and confidence in a resilient global economy. Confidence in the outlook for the domestic economy was not enough to prompt a rate rise from the RBA, which continues to walk a fine line between providing support for the fragile industrial economy while managing overheated east-coast property prices. They will be assisted in this endeavour by APRA, who announced the introduction of macro-prudential controls as an attempt to limit credit growth for property investors.

The Fund was flat again in March. Modest gains in most sectors were offset by losses focused in the healthcare portfolio, where broad-based momentum across the sector along with some company-specific developments, gave rise to losses on several core shorts. News was better in the resources and real estate sectors, which provided the strongest contribution to returns. At an individual security level, the strongest performers were Iluka Resources, Brickworks, Westpac and Star Entertainment, all on the long side of the ledger, while a short position in a copper miner also performed well.

A major theme across the consumer sector has been the outperformance of discretionary over staples retailers. The fund's long positions in casinos (Star Entertainment and Melco Resorts) have performed well following sell downs last year, over concerns around Chinese VIP trends. Within staples, the market continued its reappraisal of the value of Unilever following the bid from Kraft-Heinz while Heineken benefited from a relaxation of anti-Mexican rhetoric from the US administration.

Valuation has been the primary driver of positioning across industrial sectors. A divergence of infrastructure valuations was successfully exploited through a new investment in Sydney Airport, which has performed well with the recovery in the share price, as investors' concerns over the risk posed by a second major airport in Sydney have abated. Gains in capital goods positions were largely offset by weakness in automotive, while in transport the long in Qantas (versus short in international peers) was an additional source of returns, reflecting the undervaluation of Qantas versus its offshore competitors.

The domestic healthcare sector outperformed the broader index in March. Notable outperformers were Ansell, Sirtex and Primary Healthcare, all rallying on scant news. We continue to see downside risk to these businesses. Many domestic healthcare companies remain at or near stretch-valuation levels, providing the basis for short theses supporting several core positions and a net short exposure across the domestic healthcare sector. Better value is on offer through Ramsay Healthcare, which remains a core long position for the Fund. Offshore we prefer long exposures in innovator companies and selling businesses with relatively lower product differentiation and higher exposures to drug pricing pressures by payers (i.e. diabetes, immunology).

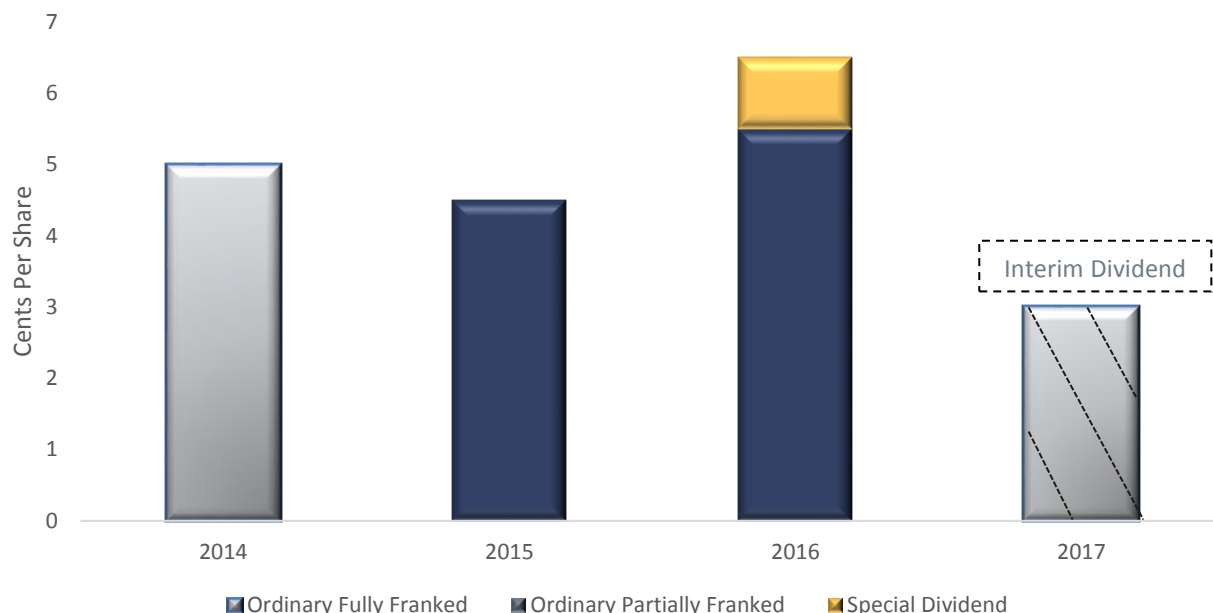
Positive momentum also continued across financial sectors, where banks and asset managers all performed strongly. The Fund retains a balanced exposure to the major Australian banks and is net short their Canadian peers. There are many parallels between the major Canadian banks and our domestic banking sector. Both have benefitted in recent years from exposure to the booming resources sector and from buoyant residential property markets. While the Australian banks undertook remedial action in 2015 to strengthen their capital positions (and were de-rated as a result), the Canadian regulator has been less proactive, leaving the banks undercapitalised and poorly provisioned for a rise in bad and doubtful debts. With the share prices of Canadian banks at all-time highs and the regulator hinting at action in respect of capital, we believe the Canadian banking sector is in a similar position to our domestic industry in early 2015.

Mining companies were amongst the weakest performers in March, with prices of many commodities looking vulnerable at current levels and record margins for miners likely to be unsustainable in the medium-term. We will look to build on short positions across the mining sector in the coming months, balanced by investments in producers of more reasonably-priced commodities such as nickel and potash. The Energy sector saw plenty of action though the month, with concerns over rising inventories and US supply-growth leading to a 10% decline in the price of Oil. We have used this weakness to build upon investments in the sector, in particular adding to ENI & Hess Corp.



Dividend History

The Board is committed to paying an 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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