



Monthly Update – October 2018

**Fund at a Glance**

Fund Size	AU\$245m
Strategy FUM	AU\$317m
Fund Inception Date	August 2012
Fund Strategy	Equity Market Neutral
Application/Redemption	Daily
Management Fee	1.5%
Performance Fee	20%
Benchmark	RBA Cash Rate

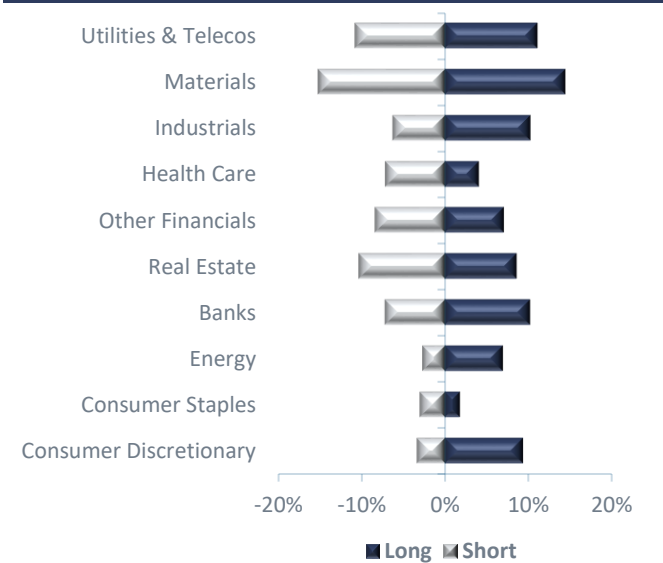
**Return Characteristics<sup>1</sup>**

Positive Months	68%
Beta	-0.2%
Sharpe Ratio	1.1
Sortino Ratio	3.5
Standard Deviation (annualized)	6.6%
No. Long Positions	72
No. Short Positions	71
Gross Exposure	176%
International Exposure (% of Gross)	10%

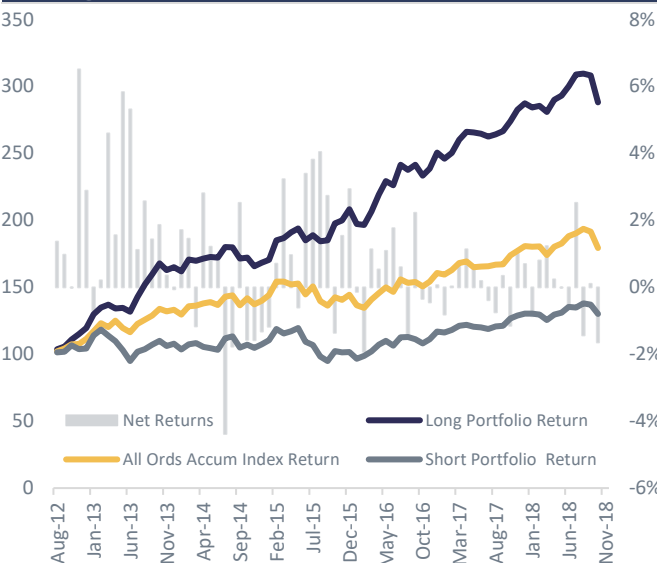
**Performance**

	1 Mth	1 Yr	2 Yrs (pa)	3 Yrs (pa)	4 Yrs (pa)	5 Yrs (pa)	SI (pa)
WMNT (net return)	-1.7%	1.9%	0.7%	3.1%	5.6%	4.8%	9.7%
RBA Cash Rate	0.1%	1.5%	1.5%	1.6%	1.8%	1.9%	2.1%
<b>Outperformance</b>	<b>-1.8%</b>	<b>0.4%</b>	<b>-0.8%</b>	<b>1.5%</b>	<b>3.8%</b>	<b>2.9%</b>	<b>7.6%</b>

**Sector Exposures**



**Long/Short Spread<sup>2</sup>**



**Gross Portfolio Structure**

Investment Type	September 2018		October 2018	
	\$m	%	\$m	%
Listed Securities - Long	218.6	88.5	226.6	92.5
Listed Securities - Short	-201.8	-81.7	-203.4	-83.0
<b>Net Exposure</b>	<b>16.8</b>	<b>6.8</b>	<b>23.0</b>	<b>9.4</b>
Cash	230.2	93.2	222.0	90.6
<b>Capital</b>	<b>247</b>	<b>100</b>	<b>245</b>	<b>100</b>

## Month in Review

Simmering concerns over a range of geopolitical and macroeconomic issues boiled over in October, sending share markets around the world tumbling to their worst monthly performance in several years. While the root causes behind the sell-off in risk assets originate predominantly offshore, the local share market was not immune and fell by over 6% in the month. Data from the bellwether US economy continues to be strong, with little to suggest that rate hikes from the Federal Reserve have had the desired effect of relieving pressures in the labour market. It is clear investors are increasingly of the opinion that this could be as good as it gets and are de-risking portfolios accordingly.

The Fund delivered a net return of -1.7% in the month. Historically the Fund has performed well during 'risk-off' events, although with no net exposure to the share market, this is by no means guaranteed. Stock specific performance and sector tilts drive returns in a market neutral strategy and both detracted moderately in October.

We have struggled for some time against the momentum of a bull-market, adding far less value on the short side than in previous years. Valuations for expensive growth companies that would normally provide shorting opportunities have stretched ever further, while M&A activity has been elevated in a market awash with cheap liquidity. This has given rise to a particularly difficult environment for short-sellers such as Watermark. Pleasingly, alpha generation on the long side has been consistently strong and we have avoided any material drawdown in the value of the Fund during this period. We are confident that market conditions in the coming months will better suit our investment style and that our fully hedged position will stand investors in good stead.

Our investment in MYOB bucked the technology sell off, receiving a takeover offer from KKR at a 25% premium. The company has undergone heavy investment spend over the past two years delivering a cloud offering with capabilities akin to competitor Xero. With this investment largely spent, earnings and free cash flow growth will begin to emerge. We are not surprised at the timing of the bid, especially considering previous owner Bain Capital has been looking to exit.

Global Healthcare shares performed broadly in-line with major global bourses in October, marked by solid performance in pharmaceutical shares, as investors sought refuge in more 'defensive' and 'value' exposures. Australian healthcare shares fell sharply, underperforming for most of the month before staging a late recovery to finish slightly behind the broader market. The Healthcare portfolio was down moderately in October, our shorts delivered robust performance however these were offset by outsized declines in offshore investments. Losses were largely isolated to Fresenius Medical, which fell sharply after the company surprised investors with an early guidance downgrade and Baxter, International which delivered disappointing September quarter results. We made minor changes to the portfolio in the period and continue to see domestic healthcare valuations as stretched despite the sell-off.

The Consumer portfolio also detracted from performance. Tabcorp held an investor day in October where the company confirmed that, while momentum remains strong in the Lotteries division, structural pressures in wagering remain a drag on the business, where additional investment is required. An investment in Super Retail detracted following a slightly softer trading update and the resignation of long-serving CEO Peter Birtles. Anecdotal feedback is that the trading environment for many consumer-facing companies softened in October as housing sector woes became front-page news. We will be maintaining a sharp eye on this sector as the key Christmas trading period approaches.

In Financials, issues stemmed principally from investments in two European banks. Clydesdale Bank is dual-listed on the London stock exchange and the ASX and was dragged lower with the broader European banking sector, despite significant upside resulting from its merger with Virgin money. We are still very excited by the outlook for CYBG in coming years - the benefits to flow through from the merger are significant and following receipt of advanced accreditation the company is over-capitalised and should return capital to shareholders. In simple terms CYBG is cheaper than the major banks and will be able to grow profits by close to 30% in the next 3 years, while the majors are unlikely to see profits grow in years ahead. European banks have been sold-off on concerns over political instability in Italy and the ongoing Brexit saga, as well as money laundering scandals in Denmark and the Netherlands, which impacted an investment in Danske.

## Monthly Net Performance (%)

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2012	-	-	-	-	-	-	-	1.36	0.97	0.00	6.51	2.88	<b>12.14</b>
2013	-0.71	0.21	4.60	1.55	5.83	5.31	1.11	2.57	1.43	1.86	0.35	-0.06	<b>26.57</b>
2014	1.71	1.45	-1.17	2.80	1.21	0.84	-4.38	-1.77	2.52	-1.57	-1.58	-1.32	<b>-1.51</b>
2015	-1.18	0.70	3.23	0.96	-0.61	3.39	3.82	4.04	2.73	-1.36	1.53	2.93	<b>21.92</b>
2016	-0.14	-1.93	1.13	0.53	1.08	1.76	0.60	-1.46	2.23	-0.34	-0.46	0.07	<b>3.03</b>
2017	-0.81	0.02	0.76	1.13	0.61	0.19	-0.39	-0.75	0.34	-1.14	1.00	0.69	<b>1.62</b>
2018	-0.86	0.80	1.23	0.23	-0.01	-0.61	2.52	-1.44	0.10	-1.65			<b>0.25</b>



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<sup>1</sup> Return Characteristics are for the period since inception. The Fund's inception date is August 2012.

<sup>2</sup> The Fund makes a profit where the long portfolio outperforms the short portfolio, after the payment of fees. Portfolio returns are before fees and costs.

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