



## NTA and Monthly Update – October 2018

### Company at a Glance

ASX Code	WMK
Fund Size	AU\$74.7m
Fund Strategy	Equity Market Neutral
Share Price	\$0.82
Shares on Issue	82.4m

### Net Tangible Asset (NTA) Backing

	Sep 18	Oct 18
NTA Before Tax	\$0.95	\$0.93
NTA After Tax	\$0.95	\$0.94

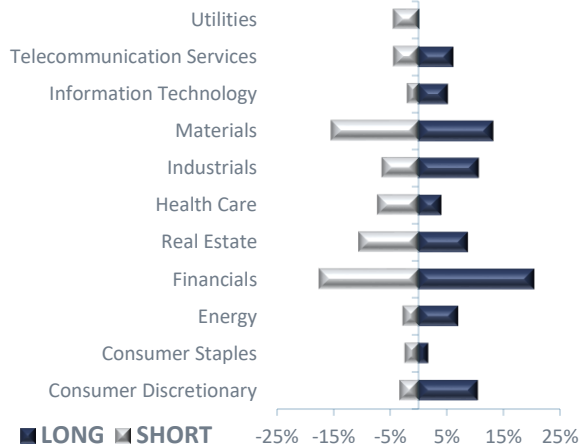
### Gross Portfolio Structure

	Sep 18	Oct 18
Long Exposure	92.3%	88.8%
Short Exposure	-89.5%	-86.4%
Gross Exposure	181.8%	175.2%
Cash	97.2%	97.7%

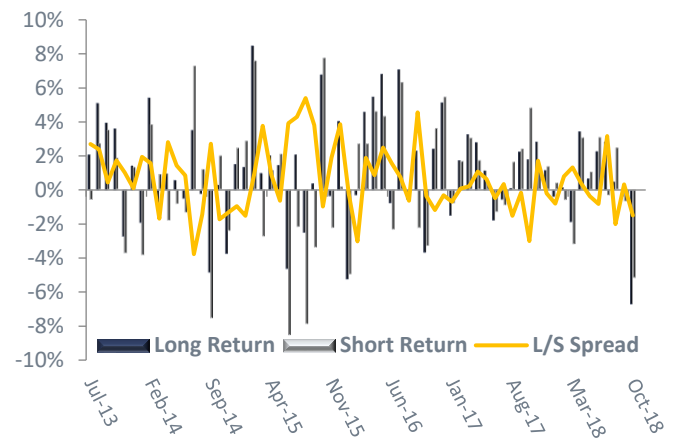
### WMK Performance

	1 Mth	3 Mths	1 Yr	2 Yrs (pa)	3 Yrs (pa)	5 Yrs (pa)	S.I. (pa)
Portfolio Return (net)	-1.9%	-3.7%	0.1%	-2.7%	1.0%	3.3%	4.0%
RBA Cash Rate	0.1%	0.4%	1.5%	1.5%	1.6%	1.9%	2.0%
<b>Outperformance (net)</b>	<b>-2.0%</b>	<b>-4.1%</b>	<b>-1.4%</b>	<b>-4.2%</b>	<b>-0.6%</b>	<b>1.4%</b>	<b>2.0%</b>

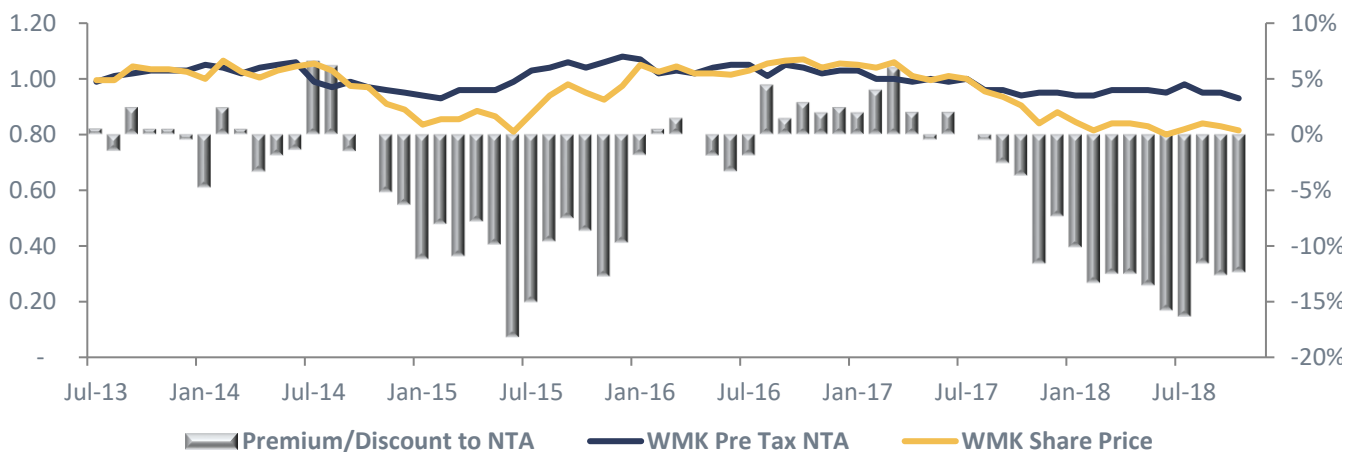
### Sector Exposures



### Long Short Spread



### Premium/Discount to NTA History



## 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 -1.9% 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 feel confident that prevailing market conditions in the coming months will better suit our investment approach 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 a 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. Specifically, investment 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.

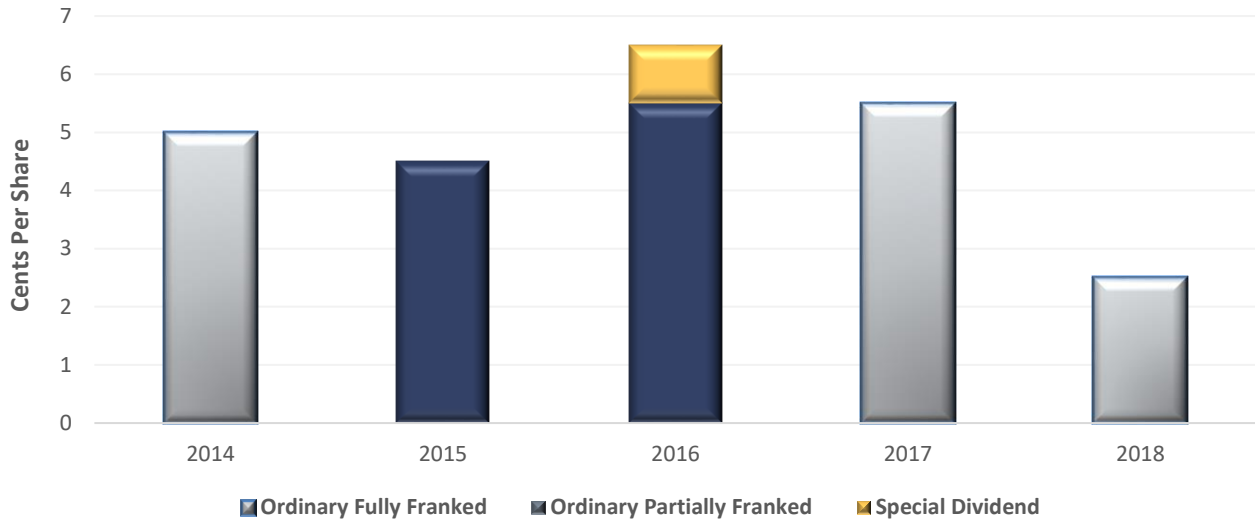
The Consumer portfolio also detracted from performance. Tabcorp held an investor day in October, where the company confirmed that while momentum remains strong in the Lotteries division, structural pressures in wagering remain a drag on the business and announced a need for reinvestment in that division. 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 the month of 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.

The Financials portfolio was a modest detractor from returns in the month, with issues stemming 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.



## 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](mailto:callcentre@boardroomlimited.com.au)



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