WATERMARK ABSOLUTE RETURN FUND
Monthly update– March 2021

APIR ETL8732AU
APIR ETL5025AU

WATERMARK FUNDS MANAGEMENT

FUND AT A GLANCE

Fund Inception **Ord/B Class**	May 19/26 Mar 21
Fund Strategy	Variable Beta
Benchmark	RBA Cash Rate
WARF ORD.UNIT ENTRY PRICE	**$1.079**
WARF ORD.UNIT PRICE/EXIT	**$1.076/1.073**
WARF B CLASS UNIT PRICE/EXIT	**$1.023/1.003**

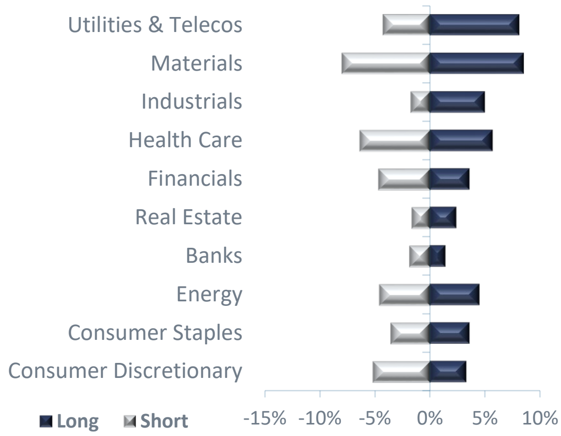
PORTFOLIO CONSTRUCTION

No. Long Positions	94
No. Short Positions	67
Gross Exposure	90%
Net Exposure	6%

GROSS PORTFOLIO STRUCTURE

Investment Type	%
Listed Securities – Long	47.8
Listed Securities – Short	-42.2
Cash	94.4
Capital	100

SECTOR EXPOSURES



TOP CONTRIBUTORS	TOP DETRACTORS
ALG	MGR
LVH	TCL
TLS	CWY

MONTHLY NET PERFORMANCE (%)

	1 Month	3 Months	FYTD	Inception (pa) *
WARF	-1.1	3.5	9.2	10.0
RBA Cash Rate	0.0	0.0	0.1	3.5
Outperformance	**-1.1**	**3.5**	**9.1**	**6.5**

*WARF est. May 2019, historic returns from ALF:ASX- same variable beta strategy est. in 2004

KEY RISK INDICATORS

Beta	Volatility	Information Ratio
0.13	**5.56**	**0.77**

MONTH IN REVIEW

Australian equities were largely flat in March with the All Ords up 0.02%. The *Consumer Discretionary* sector led up 6.9%, although this was largely a recovery from a late February sell-off. The worst performing sectors were Materials and Technology, down 5.0% and 3.0% respectively. Following similar trends in recent months, rising bond yields again weighed on long-duration growth assets like *Technology.*

The Watermark portfolio finished the month down -1.1% (net of fees) a partial unwind of the strong +3.9% return delivered in February. The March quarterly return was +3.5%. This unwind was most evident in our short position in the *Consumer Discretionary sector,* which saw several names retest February highs. The best performer in March, *Ardent Leisure,* benefited from the US vaccine rollout and domestic travel stimulus. *Telstra* was also a strong performer as key defensive shares caught up having underperformed in recent months.

MARKET OUTLOOK

Share markets around the world are looking over-bought and vulnerable to a set-back in the June quarter. We would expect a correction of 10-15% in the months ahead before the final leg up in this long bull market begins in the second half of the year.

All the major price signals for shares, bonds and currencies are indicating a pull back is imminent. The USD as the key reflation indicator appears to have turned the corner and will put risk assets under pressure as it rallies.

If we look at technical and sentiment indicators, we get the same message. Market breadth and participation is narrowing, with fewer names leading the rally. Sentiment indicators (bull/bear ratio) are also at multi-decade highs as is retail investor participation. Most of the bubble sectors are looking like they may have turned also, a red flag for shares more broadly, with- *Bitcoin, ARK, Clean Energy;* and *Tesla* all struggling here.

At the same time, we are transitioning through peak stimulus as fiscal spending tapers with final cheques paid and the Biden administration looking at new taxes to fund the pandemic spending. While we are unlikely to see changes to accommodative monetary policy settings any time soon, capital markets have taken charge in recent months, pushing rates higher increasing funding costs for lending institutions. This upward pressure on rates will continue as the recovery unfolds.

On the sector front, rotation between sectors and factors has been a feature of this recovery in recent quarters. *Defensive* shares which have been the laggard, have caught up in recent months as bond yields have backed up. More recently, *growth* and *technology* sectors have also recovered leaving all sectors overbought and susceptible to a broader correction.

SECTOR OUTLOOK

After a momentous beginning to the year- Buy Now Pay Later (*Afterpay* and *Zip*) saw deep selling late in February and into March. These high valuation shares remain highly sensitive to bond yield gyrations which played out late in February. Concerns have also emerged over *Paypal* and now potentially *Square* entering the space. We are more cautious on the sector now reflecting increased competition.

Computershare (CPU) was the best performer in the ASX50. We maintain a long position given its exposure to interest rates. We consider it one of the best ways to get upside exposure to short term rates and defence against inflation.

A more stable yield curve in March and improving reopening sentiment saw *Real Estate* (+5.6%) and *Utilities* (+6.8%) perform strongly over the month. Whilst bonds remain supportive in the very short term we think that risk remains of rising real yields negatively impacting these sectors. This is particularly so after the bounce off the bottom these oversold sectors had in the month.

We remain balanced in long and short positions in *technology* where we are focussed on stock selection. This is to avoid volatility arising from valuation concerns. Our key pick in the tech sector is *Life360*, a family safety application, which is set to benefit from and reopening USA and children returning to school in July/August.

In the broader *industrial* sectors- *AGL Ltd* a key short, announced its intension to split into *New AGL* and *Prime Co* the less attractive generation business. While this is probably in the best interests of shareholders longer term, it will add an additional layer of costs which will weigh on earnings- we have retained our short position.

Elsewhere in *utilities* we took up positions in *APA* and *AusNet* as these shares had underperformed with all the excitement in *cyclical* shares. We have also added *Contact Energy* to the portfolio, the dual listed gen-trader in NZ. The shares have struggled with the dry weather in NZ and a re-weighting of its shares in key green energy ETF's, providing an opportunity for us.

Elsewhere in *defensives* we have added to *Telstra.* COVID has impacted roaming revenues which should recover as boarders open up again. Historically we have also seen a nice uplift in revenues accompanying a generational shift in platform technology- we would expect to see this again with the roll out of 5G.

It is hard to find any value amongst *cyclical industrial* companies. We are adding to contractors, they have not participated in the cyclical rally despite strength in the mining sector. We have taken profits in *Media* and *Building Materials*.

The *healthcare* names continue to struggle given the dual headwinds of a stronger Australian dollar and the defensive nature of the sector. We are long emerging domestic names in imaging *(IDX)* and IVF *(MVF and VRT)* and short the international names. The IVF sector is particularly interesting, birth-rates are back up and pricing has improved as competition has abated.

The *Consumer* sector is continuing to benefit from a higher pool of household savings and a redirection of spending away from services to durable purchases. Our channel checks suggest this has continued into April. Having said that, share prices have been volatile as the market grapples to understand which sales are sustainable and which are transient.

We continue to see the Australian *e-commerce* sector as overvalued, having benefited from atypical trading conditions. As the market normalises, we expect growth rates to mean-revert. A consistent theme in recent announcements has been a ramp-up in marketing costs in an attempt to keep the sales momentum going, this obviously will come at a cost.

Trading activity in the *Consumer Discretionary* sector has probably peaked in our view. While companies may continue to deliver very strong trading results in the near-term (with more earnings upgrades), investors will look forward to profits moderating from here.

In the *Consumer Staples* sector, FMCG companies struggled in 2020 as everyone chased discretionary names and are now looking interesting. While demand for these essential items has remained resilient through the pandemic, supply chains have been disrupted as consumption has shifted from out-of-home to at-home. As these companies re-engineer their operations, we expect profits to recover. We are already seeing this play out for *United Malt* and *Bega*.

On the short-side, the *supermarkets* are looking over-valued. Our
channel checks suggest the risk of a price war is real and that we should expect to see more action on that front in coming weeks.

MONTHLY NET PERFORMANCE (%) *

YEAR	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
FY04								0.3	1.1	0.2	0.0	1.8	**3.4**
FY05	1.0	-0.3	3.7	2.3	3.6	2.0	0.3	1.0	-0.7	-4.9	-0.4	3.9	**11.7**
FY06	2.0	2.2	3.9	-2.3	3.1	3.1	1.3	1.6	5.3	2.7	-1.0	0.9	**25.0**
FY07	-3.1	4.4	1.8	6.3	2.5	2.0	2.8	-1.7	2.8	1.1	2.2	1.8	**25.0**
FY08	-1.0	4.1	2.5	0.8	-0.1	-1.4	-11.7	-8.3	1.4	4.4	1.5	-7.1	**-15.1**
FY09	-1.1	5.3	-5.2	-16.0	-6.3	3.2	2.5	3.1	16.2	7.3	10.1	7.1	**24.5**
FY10	9.3	11.2	6.0	0.1	0.5	-0.5	-2.3	1.9	3.5	-1.7	-5.7	-1.9	**20.8**
FY11	2.9	-3.8	2.4	0.1	2.7	10.8	2.2	1.7	3.6	2.0	-1.2	-1.3	**23.6**
FY12	-4.0	-6.7	-8.3	6.5	-1.3	1.0	5.0	4.8	3.8	0.9	-2.3	0.8	**-1.0**
FY13	3.8	4.2	0.0	-1.2	6.7	3.0	2.7	1.2	3.0	2.2	1.6	2.9	**34.2**
FY14	3.9	3.6	2.9	3.7	-0.2	-0.1	0.4	3.1	-1.3	2.4	1.1	0.6	**21.8**
FY15	-3.6	-2.4	1.4	-1.2	-2.5	-1.1	-1.2	1.0	3.0	0.8	-0.5	3.1	**-3.5**
FY16	3.8	4.6	1.9	-2.1	0.6	2.6	0.4	-2.6	1.8	-1.0	1.7	1.8	**13.9**
FY17	-0.3	-0.6	3.9	-0.5	-0.9	-0.2	-0.7	-0.1	0.2	1.2	0.8	-0.5	**2.3**
FY18	0.2	-1.9	-0.4	-3.1	1.3	0.1	-0.6	0.7	0.9	0.9	0.0	-0.6	**-2.4**
FY19	3.0	-2.0	0.2	-2.0	-2.9	-1.4	0.5	0.7	-0.9	-2.3	-0.6%	**1.1**	**-6.6**
FY20	**2.1**	**1.5**	**-0.5**	**1.6**	**-0.4**	**-0.1**	**0.7**	**-1.1**	**-2.4**	**0.9**	**-0.7**	**-1.2**	**0.3**
FY21	**1.2**	**1.1**	**0.1**	**1.4**	**2.8**	**-1.1**	**0.8**	**3.9**	**-1.1**				**9.2**

**WARF est. May 2019, historic returns from ALF:ASX- same variable beta strategy established in 2004.*

MANAGING YOUR INVESTMENT

To view details of your investment such as your transaction history and distribution payments, please register via the secure portal (investorserve.com.au) operated by Boardroom Pty Limited.

The Fund is priced monthly, on or around the 6th business day of each month. Boardroom Limited, who manage the unit registry for the Fund, will accept applications up until 2pm on the last day of the month and redemption requests up until 2pm on the 10th business day of each month.

WARF Application and Redemption forms can be found on our website wfunds.com.au, once completed please return to watermark@boardroomlimited.com.au.

Investors should refer to the Product Disclosure Statement when applying or redeeming from Watermark Absolute Return Fund. (ETL8732AU PDS & ETL5025AU)

For further information about the InvestorServe portal or queries regarding your holding, please contact Boardroom Limited 1300 005 027 (in Australia) +61 2 8023 5474 (international) or email watermark@boardroomlited.com.au.

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