



The Leading Edge

QUARTERLY REPORT • September 2019

Level 23, Governor Phillip Tower, Sydney NSW 2000

TEL (02) 9252 0225 • info@wfunds.com.au • www.wfunds.com.au

This report has been prepared by Watermark Funds Management Pty Limited.

This report is for distribution only under such circumstances as may be permitted by applicable law. It has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein nor is it intended to be a complete statement or summary of the securities, markets or developments referred to in the report. The report should not be regarded by recipients as a substitute for the exercise of their own judgement. Any opinions expressed in this report are subject to change without notice. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. Watermark Funds Management Pty Limited is under no obligation to update or keep current the information contained herein. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realised.



Justin Braiting
Portfolio Manager

Message from the CIO

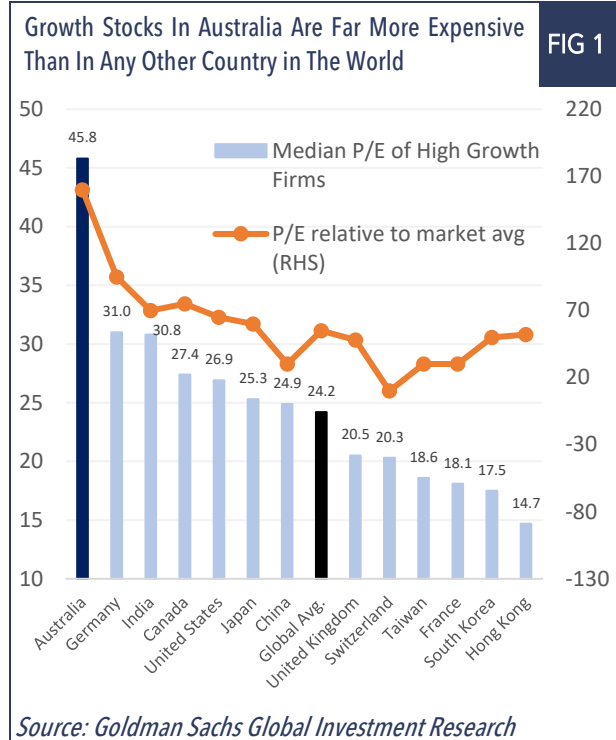
From mid-year, as global growth slowed materially, investors moved into the safety of bonds pushing yields to unprecedented lows. Deflationary forces were pervasive with commodities and bond yields falling in tandem.

Local financial markets were caught in this downdraft with Australian Commonwealth Government Bonds plumbing new lows of just 1%. Yields on one-third of the world's stock of sovereign bonds shifted back into negative territory while gold broke sharply higher. The message coming from the bond market was clear, with yield curves inverting, recession was a real and present danger.

Central Banks the world over were quick to get the message including our own RBA, pivoting from a tightening stance to interest rate cuts in short order. The reversal in monetary policy sent share markets higher with growing confidence the 'Fed put' was back in place.

Rarely have we seen such divergence in price signals coming from bond and equity markets - shares were suggesting clear skies ahead while bonds were priced for a recession. The deflationary impulse peaked in August before thawing in trade tensions, and the prospect of a deal saw bonds sell off and money move back into risk assets.

Concurrently, we witnessed a large reversal in share market leadership. Extremely low bond yields had pushed growth and defensive securities to extreme levels. We have seen this manifest in our own share market as Technology shares reached dot com levels. Figure 1 shows we are home to the world most expensive growth names.



Along with record bond prices, positioning in this barbell strategy had become extreme, so when bonds reversed, we saw money pour out of defensives and Tech, back into cyclicals and value. This trend has continued into the fourth quarter of the year.



While global growth continues to slow with Q3'2019 likely to be the bottom, investors are buying cyclical shares in anticipation of a resumption in growth next year,

confident that policy makers have acted pre-emptively, cutting rates sufficiently to avoid recession.

Most international markets have been trading lower in a bear market for the best part of 2 years. Shares in the US and Australia are now toying with prior peaks, threatening to break out and move higher. This is likely to be led by cyclical parts of the share market with key indices (S&P Industrials; US/Euro Banks; SOXX; Russel; DJ Trans) recently making new highs. European and EM Indices also look to have reversed bear market trends as the US Dollar peaked following the US Fed announcement that it was returning to Quantitative Easing.

Share markets globally may well move to new highs in the months ahead, though I suspect the upside is limited, the cycle is very mature and valuations are very stretched. While there may be one more leg up in this cycle, bulls should temper their enthusiasm as lingering recession risks for 2020/2021 will restrain the strength of any rally.

The Australian share market will inevitably participate in any move higher, but there are good reasons to believe our market may underperform. Firstly, the Australian market is a mature defensive market - a key reason why it has outperformed this year as money has moved into defensive assets. Secondly, Australia will be a funding source as money flows back into emerging markets; these inflows contributed to the outperformance of Australian shares in 2019. Thirdly, valuations in our market have been pushed to extremes, the growth basket of shares in Australia is amongst the most overvalued globally.

Finally, if our market is to fully participate, Australian bank shares which have been trading lower for three years need to regain their mojo. Bank shares are leading offshore markets higher as they respond to higher bond yields; there is no such relationship for the Australian banks as they have a different asset mix and funding structure. Furthermore, the full-year bank results that have just been released have been very disappointing with no loan growth and retail margins under pressure from lower interest rates.

Australian banks seem to be going the way of European banks where returns have shrunk along with ultra-low interest rates policies. The Westpac Capital raise has also put capital adequacy back on the agenda. With this backdrop, it is hard to see the banks participating in any rally.

The cyclical parts of the market offer the best prospects in the months ahead, domestic industrial shares, mining and

energy. Our exposure to any advance is likely to be modest given where valuations stand. We would hope though to at least match any market return through stock selection where we have returned to form so far this financial year.

PORTFOLIO REVIEW

Basic Industries

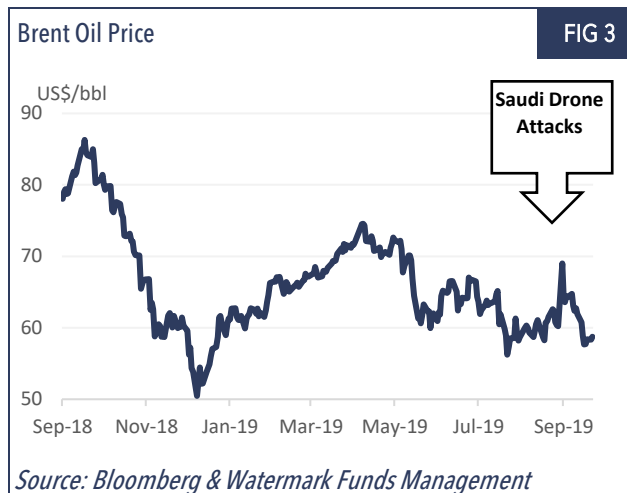
Weak economic data and continued trade tensions weighed on the broader commodity sector in September. Nickel, was the exception, rallying strongly after the Indonesian government brought forward a proposed ore and gold export ban. The end of financial year reporting season showed robust earnings and mostly sound balance sheets for mining companies, which are generally in their strongest position for several years. Capital management was a key theme for iron ore and coal miners, which bestowed shareholders with outsized dividends. In the gold sector, price rises are fuelling the expansion of exploration budgets.

Oil continued its downtrend, with ample supply and weak demand. This trend reversed temporarily in mid-September following a drone attack on a Saudi Arabian oil facility. This resulted in the shutdown of the world's largest oil processing facility. However, the Saudis have been quick to bring supply back online and release reserves. Prices have since fallen, with the market focussed for now on poor demand drivers and building inventories.

The Resources portfolio was net short into August as markets topped and commodities began to weaken. We expect to see further weakness into the December quarter and have maintained our short positioning. We are constructive on gold given the global risks. We remain cautious of base metals and iron ore however, with many commodities starting to find cost support.

Oil Markets

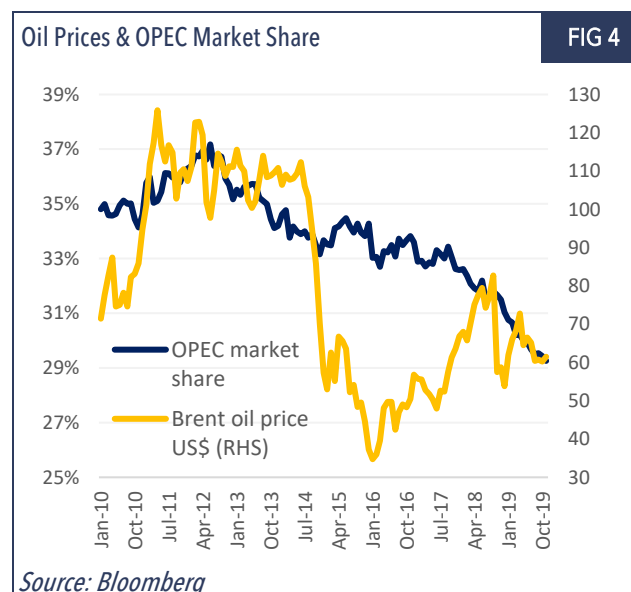
Oil markets have had a volatile 2019, pushing higher at the start of the year on the back of solid growth expectations only to fade as demand forecasts proved too optimistic. Oversupply concerns from US shale oil also dragged on the market, although this was partially offset by reduced production from Iran and Venezuela. Globally, the world produces roughly 85Mb/d (Million barrels of oil per day) supplied largely from OPEC (Organisation of Petroleum Exporting Countries) - 32Mb/d (Saudi Arabia - 11Mb/d, Iraq - 4.5Mb/d, Iran - 2.3Mb/d, Russia 11Mb/d and the USA 12Mb/d).



Globally, the world produces roughly 85Mb/d (Million barrels of oil per day) supplied primarily from OPEC - 32Mb/d (Saudi Arabia - 11Mb/d, Iraq - 4.5Mb/d, Iran - 2.3Mb/d, Russia 11Mb/d and the USA 12Mb/d).

OPEC

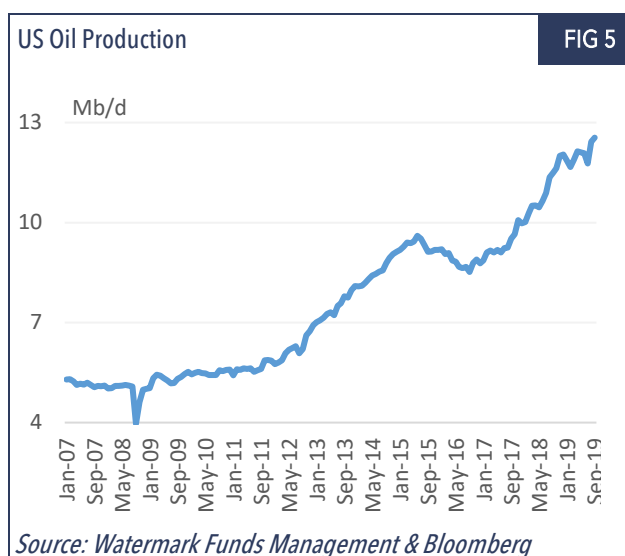
OPEC has traditionally served as the market moderator, co-ordinating policies for member countries to ensure a stable market and what it perceives as a fair return on its investments. Collectively OPEC has supplied 35-40% of global production since the early 90's. It will generally cut production during periods of lower pricing, giving up market share. It is also worth noting that OPEC has been losing market share over the past few years; however, this is primarily due to the rapid increase in US production. Most recently, OPEC has committed to cuts (ex-Iran and Venezuela) of 1.2Mb/d vs Oct 2018 levels to support the market further.



Next year we expect markets to be oversupplied and OPEC to cut production by around 1.2Mb/d to help maintain market balance.

US Shale Oil

Over the past nine years, a major shift in global oil supply has occurred due to the emergence of US shale oil production, which has rapidly increased since 2012. This has satisfied 70% of the growth in global oil demand over this period and set the USA on a path of oil independence.



Shale oil is extracted from layers of rock with very low porosity (as opposed to sandstone which has higher porosity). It has been made possible through technological developments in drilling (horizontal wells), stimulation (fracking) and prices over US\$55/bbl. In 2018 the US recorded the largest ever annual increase in oil production by any country, with a rise of 2.2Mb/d.

In 2019 we expect the US to grow production by around 1.8Mb/d, facilitated by new pipelines allowing for better transportation to end markets. Into 2020 this should slow to c.1Mb/d, particularly if oil prices remain subdued.

Due to the low porosity, shale oil production tends to fall rapidly, so extended wells (capital) and stimulation (expense) are required to maintain production levels. To date, the US shale sector has failed to produce sustainable economic returns and with the recent falls in oil price, capital has been constrained and drill rigs have been parked up. Some forecasters point to this resulting in a shortfall, but there has also been a surge in horizontal drilling which should support production next year.

Demand

Oil consumption is correlated to GDP and trade growth. Generally, 1% of GDP growth would translate to around a 0.5% increase in oil consumption. As GDP growth accelerates over 3.5%, oil intensity tends to increase while GDP growth under 2.7% generally sees oil intensity fall away quickly. Trade growth also impacts oil demand (air and sea freight, etc.) which has been one of the more significant detractors in 2019. Since September 2018, the China-US trade war has impacted GDP and trade expectations, removing c.0.8Mb/d of demand growth. Most growth forecasts have fallen from 1.5Mb/d to 0.8Mb/d, which is the lowest level of growth since 2011.

The largest consumers of oil are the USA (20Mb/d), China (14Mb/d), India (5Mb/d), Japan (4Mb/d) and Russia (4Mb/d). Since 2000 China has accounted for 35% of the growth in global oil demand. In the year to date, China's imports equate to an increase of 0.9Mb/d however most agencies are only forecasting 0.4Mb/d, which could prove to be a positive surprise. Changes to shipping fuel standards may also provide demand support into next year.

Pricing

We continue to look for softer pricing and downgrades to company earnings forecasts. Positive surprises are possible as a result of Chinese demand, Middle East shocks and changes to fuel standards however, we believe these will tend to fade as supply continues to lift. We anticipate oil prices trading between US\$50-65/bbl over the near term.

TMT/Healthcare

The TMT and healthcare portfolios made a modest contribution to returns in the quarter, with very low net exposure and a clear defensive bias towards quality and value. The FY19 reporting season was a difficult one to navigate in respect of Australian technology stocks, such as Wisetech, Afterpay, Appen, Altium and Xero (WAAX). While most reported results were in line or slightly below expectations, investors looked through weaker earnings and outlook statements, using the early August sell-off in the technology sector as an opportunity to 'buy the dip', sending prices rallying by 10-20%.

The performance of telecommunications shares has been somewhat idiosyncratic. Telstra shares gave up half of their 2019 gains in the September quarter as bond yields bounced and in light of lacklustre FY19 results, which also flagged downgrades to FY20 EBITDA forecasts. This is a result of weaker assumptions for the mobile market and more competition in the enterprise segment. TPG has been caught up in its anti-trust case with the ACCC. The trial now has concluded, and we are expecting a ruling from the judge between November and February. There are strong arguments for the merger with Vodafone to be allowed to proceed. In New Zealand, shares in Spark reached new highs, with the new CEO providing assurance on the company's dividend and a more upbeat outlook for FY20. This allayed concerns around a market slowdown, which were inferred in the first-half results. On the flipside, Chorus shares remain caught up in regulatory limbo as its administrative framework continues to be worked out by the NZ authorities, resulting in analysts cutting revenue assumptions during the quarter.

In media, debate centred around the weakness in advertising across the board (television, radio, out of home and digital) and whether this is just a flash in the pan or the beginning of a cyclical slowdown. In the case of oOh!media, the softness was enough to trigger a management downgrade on profit expectations for the year, causing its shares to collapse 35% in one day. News Corp shares continued to outperform their peers, driven by a decent set of results and continued focus on the narrative around simplification of the business (e.g. strategic review of North America Marketing). It is worth noting the exceptional performance of REA Group and

Domain shares in anticipation of a strong spring recovery in the residential property market.

Among healthcare names, CSL was one of the big winners of the earnings season, posting very strong FY19 results and FY20 guidance on the back of a tight IG market, more than offsetting moderating growth in its speciality products. Cochlear was penalised for losing market share to Advanced Bionics in 2H19 due to the lack of an MRI compatible cochlear implant. This has since been remediated with a new device that will hopefully recover that market share in FY20. Resmed has continued to re-rate higher, underpinned both by solid trading conditions in its US market as well as global re-pricing (higher) of med-tech names.

Perhaps one of the more interesting segments of Healthcare in the third quarter of 2019 has been smaller companies. As large and midcap companies have re-rated higher, investors have to reach further down liquidity/risk spectrum to find value and compelling stories. Paradigm Biopharmaceuticals is a notable example from this part of the market. Paradigm shares have doubled in value as a result of strong Phase 2B clinical data and the US FDA clearing its expanded access IND for a phase III trial in ex NFL players. Similarly, shares in Opthea multiplied by a factor of 5x on the announcement of a positive clinical outcome of its Phase 2B trial in patients with wet age-related macular degeneration (AMD).

Overall, the TMT / Healthcare portfolio is conservatively positioned for a topping market. We remain concerned that excessive monetary accommodation is stoking financial asset bubbles and pushing investors further out on the risk curve. Our long portfolio remains focused on either defensive businesses with solid earnings outlooks or businesses that we fundamentally like where we have value support. On the flip side, the short portfolio has a mix of extremely expensive shares and bad companies prone to disappoint.

Fineos

In August, we participated in the IPO of Fineos a provider of core software systems to the Life, Accident & Health (LAH) insurance industry. Fineos today has over 50 insurers as customers across eight countries, including 6

of the top 10 insurers in Australia and the USA. Fineos ticks many boxes as a high-quality business model: sticky customers, recurring revenue stream, high incremental margins, low capital intensity, all in the context of a growing sector.

The shares were priced at \$2.50 on their debut entry to the ASX but quickly traded up 20% to \$3.00 reflecting a healthy level of demand for a quality business with secular tailwinds.

The company was founded in 1993 by its current CEO Michael Kelly, who remains its largest shareholder post-IPO. In 2014 the company embarked on a heavy investment phase to broaden its focus from claims to a comprehensive product suite covering all core systems of LAH insurance, from policy management to claims payments, including billing, absence, and providers among others. Since then the business has spent €90 million in building this full portfolio, but it was only in 2018 that this development began to be monetised. Today, all modules are cloud-ready and have been deployed live with a customer. While the on-premise Claims module generates the majority of present revenue, sales of new modules and shifting existing customers to the cloud represents an attractive opportunity (cloud pricing is established at around 2x existing maintenance fees).

For context, the LAH industry spends around USD 100 billion annually on IT (hardware and software), and most of that spend goes to maintaining old, on-premise solutions. These legacy systems are often a hodgepodge of antiquated software. They are written in old, customised code which is very hard to update or flex. The data remains siloed across different applications, making sharing, collaboration and analysis quite difficult, while processing has to happen in a time-consuming batch form instead of real-time, which hinders effective and timely decision making for customers.

Given the importance of these systems, which are mission-critical to the operation, insurers have been slow and reluctant to replace them. But much like in adjacent sectors (banking, fund and wealth management, property & casualty insurance, among others) the transition from old legacy on-premise systems to agile, modular, cloud-deployed solutions is starting to gain traction driven by a need to accelerate speed to market, increased

compliance requirements and the need to remain cost-competitive in a mature and price-sensitive market.

We believe Fineos can produce c.15-20% annual revenue growth for the next five years driven by a combination of new customer acquisitions and growing share of wallet within the existing client base. Many of Fineos' clients use a limited number of the modules available or are multi-nationals that have only just deployed Fineos in one or few jurisdictions or in only one business line (individual or group LAH)- hence the multi-year growth opportunity.

High and sustained growth rates combined with moderating opex growth means the business can grow EBITDA at c.25-30% annually, resulting in significant equity accretion over the same period.

More recently, management has shown positive commercial momentum with three large deals signed in Q4 FY19, another four smaller customers signed in the first two months of FY20, and a pipeline of opportunities of over three times the forecast revenue for FY20. The new contracts signed tend to provide good visibility, typically over five years, although customer relationships tend to be longer than that as customer churn is very low (2% in FY18 and 0% in FY19). As a result, by the end of August management had 89% of the FY20 prospectus revenue already in the order book and closing deals, de-risking the year ahead.

The tricky part with many of these early-stage companies is that although they grow fast and generate cash, they tend to reinvest that cash into sustaining and widening that competitive advantage vis-à-vis peers. So cash flow break-even tends to be a few years out, which can make them volatile to swings in the market (esp. discount rates). At the time of the IPO, we estimate Fineos was priced at 5.5x EV / FY20 Sales which compared favourably with the US and Australian peers trading at 7.2x and 9.5x respectively. Even today, after a 20% appreciation, the shares still look attractive for long-term holders considering the growth profile and the duration of that growth.

Financials

The Financials portfolio had a solid quarter. We participated in the IPO of Sezzle during July and saw the shares move quickly to around 80% above the issue price. Sezzle currently operates in North America, where it offers a product that is similar to Afterpay and has approximately one-quarter of the number of Afterpay customers. We see both companies as attractive exposures to the emerging 'Buy Now Pay Later' trend in the US with significant growth ahead of them.

An investment in IOOF Holdings performed well in the period, with APRA losing its case against the company and its executives. This has revived expectations that its acquisition of ANZ's platforms business will be approved, which will be highly accretive to IOOF's earnings. We took an opportunity to initiate this investment following the release of the company's financial results, which saw its shares fall as a result of its ~\$240m remediation charge. Since September, IOOF has recut the ANZ deal and extended the timeline for competition.

Another key contributor over the quarter was EML, a company we wrote about in our June quarterly. Its share price has appreciated 45% through to the end of September. EML delivered a solid result in August, beating expectations across all divisions. With a diversified earnings (largely offshore) base that is seeing synchronised growth across all divisions, we see solid prospects for earnings growth and expect that investors will be willing to pay a higher multiple for those earnings.

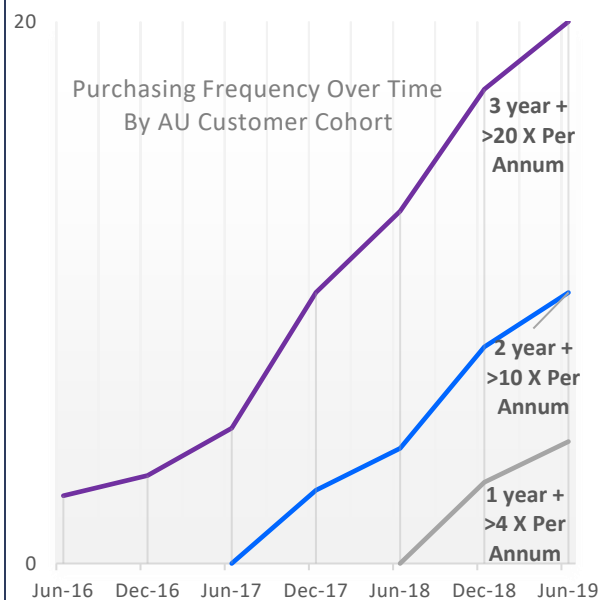
Afterpay

We have been long-term supporters of the Afterpay success story. New information in FY19 results indicates that the frequency of usage is increasing at a much faster rate than previously expected. We have since remodelled Afterpay's global gross transaction volume (GTV) with the Australia annual frequency profile.

We now believe Afterpay can beat their 2022 sales target of \$20bn GTV by at least 70% on a conservative set of assumptions and has the potential to even double guidance in a favourable US/UK scenario.

Afterpay's Australia Frequency Experience

FIG 6



Source: Company Data (Afterpay)

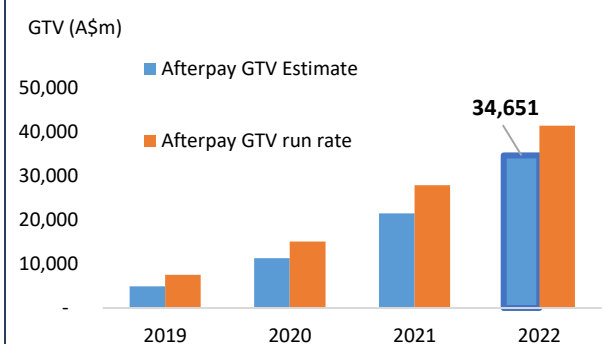
Frequency Model

The thesis is centred on behavioural trends noted in Afterpay's mature Australian cohorts who are now transacting using Afterpay more than 20x a year – a number which is still growing. We have extrapolated the behaviour of earlier customers across the whole portfolio. The results show a 70% upside to Afterpay's guidance and >40% upside to consensus GTV in 2022.

For the analysis, we forecast frequency moving upward from 20x a year in year 3 to 25x in year 5, then remaining constant at 25x a year thereafter. See frequency profile in Fig 7 (note the frequency is averaged for a usage run rate).

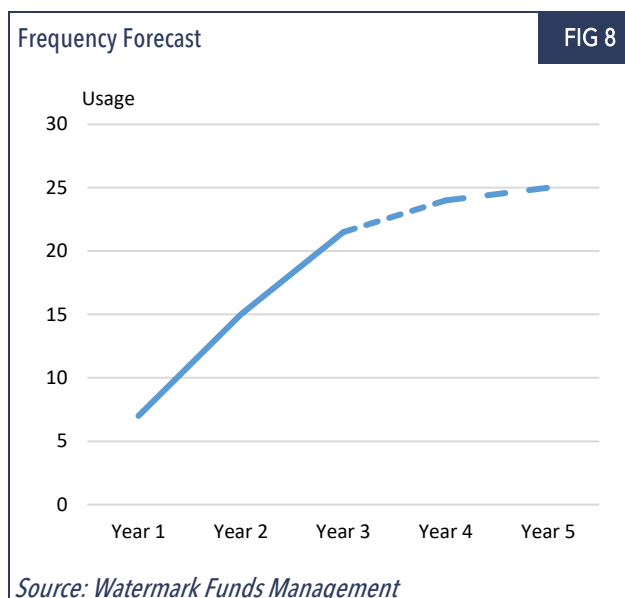
Watermark GTV Forecast: Estimate \$34B GTV in FY22

FIG 7



Source: Watermark Funds Management

This is our frequency profile based on APT's chart.



Assumptions

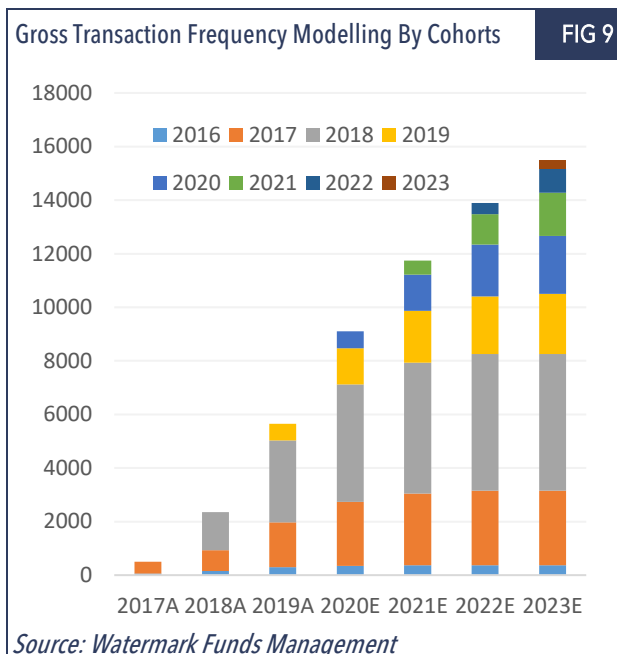
Beyond our frequency changes, our analysis is based upon a conservative set of assumptions:

1. Australian additions decline.
2. The rate of US customer additions stays flat going forward (realistically it is increasing).
3. The rate of UK customer additions stays flat going forward (realistically it is increasing).
4. Basket size remains flat at \$150 (it increased over 2019), there is also upside from Afterpay's new variable payment upfront option which allows for larger basket size.
5. While we don't include churn, we think this is more than captured within our conservative additions forecasts.
6. We only expect a slight tick up in frequency before it moderates.

As such, we see an additional upside to our GTV forecast based on the level of conservatism, particularly around customer addition rates.

Output

Below is our modelling by country and cohort - we simply grow usage in all markets using the frequency trends observed in Australia (Fig 9).



Implications

The impact of this frequency change on GTV is significant. For instance, even if Afterpay didn't add any new customers in ANZ in 2020, it would still see an uptick in ANZ sales of 50% - merely from older cohorts increasing frequency.

These results took us by surprise. It sees Afterpay beat its FY2022 target by more than 70%. This is with the rate of customer additions flatlining in the US and UK (we consider this unlikely). We also understand consensus sits at around \$24bn in FY22, and this sees >40% upside to consensus volumes.

Beyond this, we also believe that Afterpay has the potential to beat the net transaction margin guidance of 2% due to the scalability of its GTV.

Consumer/Industrial

The Consumer and Industrial sectors delivered strong returns in the September quarter. The largest contributors to performance came from core holdings in small-cap consumer shares. The performance was driven by three investments in BWX Limited (BWX), Baby Bunting (BBN) and PointsBet Holdings (PBH).

The largest detractors from performance came from our short portfolio, in particular, a basket of 'expensive defensives'. Given the rate cut environment, the hunt for yield drove investors into defensive interest rate proxies such as supermarkets. However, with the US Fed signalling a pause in its easing cycle in late September, we have subsequently added to these short positions in anticipation of a cyclical rally.

Overall, the Consumer portfolio retains a neutral stance. Typically markets deliver higher-than-average returns when the Fed has finished easing. However, in this case we are late in the economic cycle and are therefore cautious on being overly optimistic. In term of tilts within the sector, we are long cheap cyclicals such as Star Entertainment, Qantas and Webjet. The travel sector is offering good value currently as companies have been indiscriminately sold on the back of a series of travel disruptions including Brexit, the Hong Kong riots and the collapse of two travel companies in Europe. Importantly for the sector, these disruptions are likely to be temporary, and in some cases, defer spending to future periods. History has shown that a snap-back of deferred corporate travel often drives stronger than average trading performance post-disruption.

BWX

BWX was listed on the ASX in November 2015 at \$1.50 per share. Since then it has traded as high as \$8.06, on the back of strong industry tailwinds, several accretive acquisitions, and solid organic growth. It was amazing to see the share trade below its IPO price earlier in 2019 at levels as low as \$1.34 per share. While today's share price is not strictly comparable to the IPO price given the new shares issued to fund acquisitions, even after adjusting for these, the share price touched \$3.87, a fraction of historic highs. Adding to the intrigue, the stock had 2x% short interest when trading at its lowest point.

Winding the clock forward, BWX has been one of our best performing investments in FY20 to date. Our average entry price was \$2.23, and we remain holders today. Below we detail why we decided to build a position and what still excites us about the outlook for the business.



Firstly, and most importantly, equity in BWX's core brands remained untainted. These brands are the core competitive advantage for the business and where most of the value resides. Our principal aim in analysing the company was to establish whether we could get comfortable with the ongoing strength of the brands. Speaking with numerous retailers of BWX brands, we were able to establish that despite BWX reporting slowing revenues at the company level, retailers were still reporting strong sales growth and market share expansion at the customer level. This told us that much of the lost revenue in 2019 was due to destocking of the supply chain and was temporary in nature. BWX's brands remain strong today, as evidenced by new demand from retailers in Australia and offshore, further broadening distribution.

The second indicator of opportunity was the view that most of the disruption to FY19 earnings was internally driven and fixable. The business had undergone the distraction of a failed private equity bid, the resignation of CEO and CFO, and was midway through a complicated upgrade of internal systems. The culmination of these issues resulted in a drop in profit margins driven by a

range of issues, including cost duplication, poor inventory management, and the hang-over of a business that was dressed up for sale. While it was difficult to get comfortable on all of these issues, there was enough evidence to suggest the issues were largely transient, and that peak disruption occurred before BWX's interim result in February 2019.

The third reason for driving our decision to own BWX shares was the appointment of David Fenlon as CEO. David is widely respected in the Australian Health & Beauty industry as the former CEO of Blackmores Australia. He has the reputation of a team builder and culture driver. Given BWX's brands weren't broken, internal execution was the key focus for the incoming CEO. While much of the recent share price strength has been driven by David communicating his plans for the business, further share price growth will be driven by his ability to execute. We will continue to watch this closely.

Finally, sectoral tailwinds in the natural healthcare space remain very strong. Australia is arguably a global leader in natural skincare as consumer demand for a healthy lifestyle has driven the emergence of numerous boutique brands. Despite a growing consumer preference for natural skincare, the category until recently has been focussed on the speciality pharmaceutical channel only. Growth of the category into mainstream mass-market retail presents growth potential domestically. Importantly for BWX and its global reach, key international markets such as the US and UK are less progressed than Australia in the switch to natural skincare. Speaking to industry sources, we see a handful of US mass-market retailers that are currently working on building out this category. For example, Target will roll out a 'Clean Beauty' concept to all 1870 stores in January 2020. BWX's US brands, Andalou and Mineral Fusion, are well placed to participate in this market opportunity. If management can successfully execute rollout to US mass retailers, we see significant upside to today's share price.

Performance Review

The September quarter was a strong one for fund performance, with all Watermark funds posting solid gains. This was especially pleasing in light of varied market conditions and elevated volatility for the All Ordinaries Accumulation Index. Our broadly neutral portfolio settings are intended to protect the funds when markets fall, while allowing us to create value through security selection and thematic tilts.

As discussed earlier, major policy reversals from central banks triggered pronounced changes to investors' positioning in the quarter, as investors pivoted away from defensive and growth-oriented exposures, back to value and cyclical parts of the market. We have been tilted towards more defensive exposures for much of 2019, which explains in part why our portfolios managed to keep pace with buoyant markets in July, despite having no net exposure. This also left the Funds well positioned to withstand the drawdown in markets during August. Unfortunately, this same tilt caused the fund to underperform in September as investors rotated away from defensive settings. We have since adjusted our exposures across the portfolio, to align better with the macroeconomic outlook we have set out earlier in this newsletter.

Thematic tilts and adjustments to the Funds' net market exposure can have a meaningful impact on returns, however it is the value that we can add through security selection that will ultimately determine whether we meet our return targets for the Funds. Pleasingly, there was broad contribution across multiple sectors in the period, coming from both sides of the ledger. Financials, Consumer and Information Technology, were the most notable contributors in the quarter, with strong returns coming from several of the core positions outlined in the portfolio review.

Quarterly Performance by Sector

Sector	Portfolio
TMT	0.31
Healthcare	0.33
Consumer	1.48
Industrials	0.15
Basic Industries	-0.23
Financials	1.34

*Portfolio data is for Australian positions in Watermark Market Neutral Trust.

Fund at a Glance - September 2019

ASX Code	ALF
Fund Size	AU\$265.0
Fund Strategy	Variable Beta
Share Price	\$0.97
Shares on Issue	240.2m
Net Exposure	-7.5%

Net Tangible Asset (NTA) Backing

	Aug 19	Sep 19
NTA Before Tax	\$1.18	\$1.18
NTA After Tax	\$1.17	\$1.17
Dividend Declared	-	(\$0.025)
NTA After Tax & Dividend	\$1.17	\$1.145

Gross Portfolio Structure

Long Exposure	68.0%	83.6%
Short Exposure	-74.8%	-91.2%
Gross Exposure	142.9%	174.8%
Cash	106.8%	107.5%

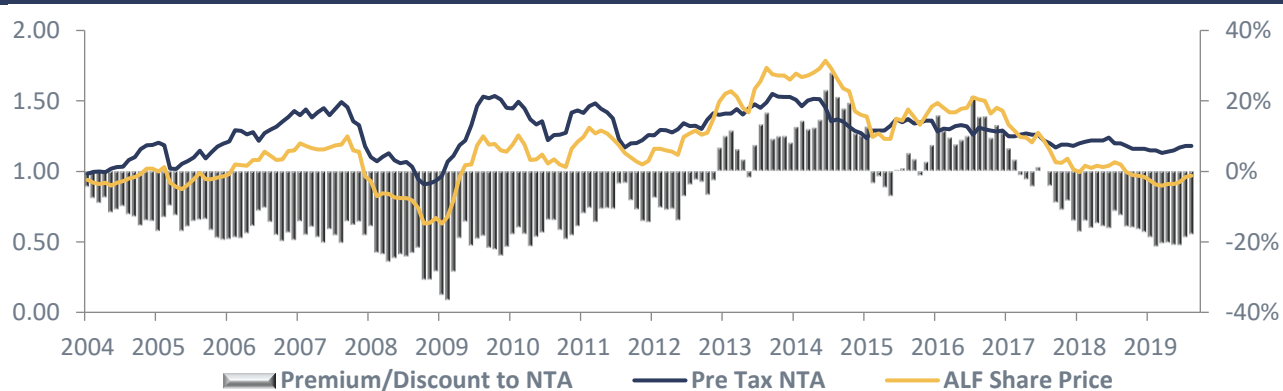
ALF Performance

	1 Mth	3 Mths	1 Yr	3 Yrs (pa)	5 Yrs (pa)	7 Yrs (pa)	S.I. (pa)
Portfolio Return (net)	0.1%	3.1%	-5.3%	-2.5%	1.5%	6.5%	10.5%
All Ords Accum Index	2.1%	2.8%	12.1%	11.7%	9.7%	11.0%	9.3%
Outperformance (net)	-2.0%	0.3%	-17.4%	-14.2%	-8.2%	-4.5%	1.2%

Net Equity Exposure



Historical Premium/Discount to NTA History





Fund at a Glance – September 2019

Fund Size	AU\$58m
Strategy FUM	AU\$132m
Fund Inception Date	August 2012
Fund Strategy	Equity Market Neutral
Application/Redemption	Daily
Management Fee	1.5%
Performance Fee	20%
Benchmark	RBA Cash Rate

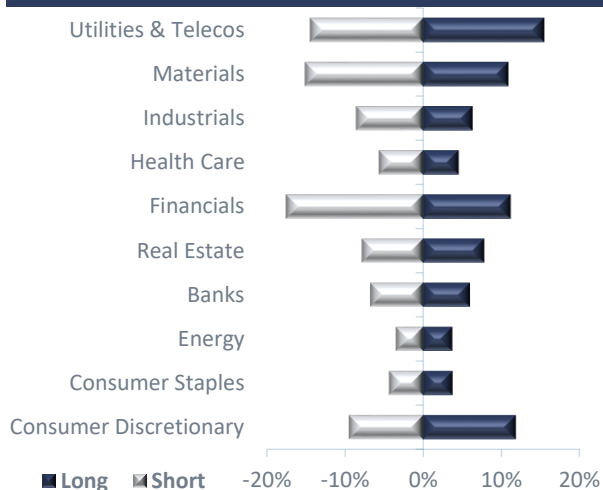
Return Characteristics

Positive Months	66%
Portfolio Beta	-0.1%
Sharpe Ratio	0.9
Sortino Ratio	2.6
Standard Deviation	6.6%
No. Long Positions	74
No. Short Positions	74
Gross Exposure	179%

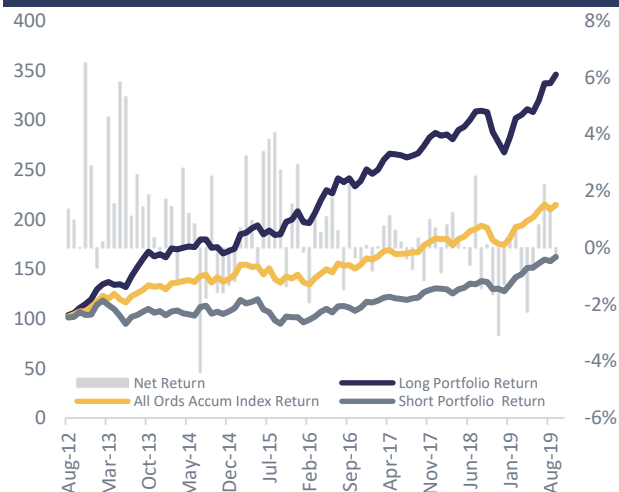
Performance

	1 Mth	1 Yr	2 Yrs (pa)	3 Yrs (pa)	5 Yrs (pa)	7 Yrs (pa)	SI (pa)
WMNT (net return)	-0.4%	-5.2%	-1.4%	-0.8%	3.4%	7.7%	7.8%
RBA Cash Rate	0.1%	1.4%	1.4%	1.5%	1.7%	2.0%	2.0%
Outperformance	-0.5%	-6.6%	-2.8%	-2.3%	1.7%	5.7%	5.8%

Sector Exposures



Long/Short Spread



Monthly Net Performance (%)

Cal. Yr	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2012	-	-	-	-	-	-	-	1.36	0.97	0.00	6.51	2.88	12.14
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	26.57
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	-1.51
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	21.92
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	3.03
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	1.62
2018	-0.86	0.80	1.23	0.23	-0.01	-0.61	2.52	-1.44	0.10	-1.65	-3.08	-1.30	-4.11
2019	0.22	0.69	-1.00	-2.27	-0.78	0.80	2.21	1.38	-0.41				0.77



Fund at a Glance - September 2019

Fund Size	AU\$37m
Strategy FUM	AU\$302m
Fund Inception Date	May 2019
Fund Strategy	Variable Beta
Application/Redemption	Monthly
Benchmark	RBA Cash Rate

Return Characteristics

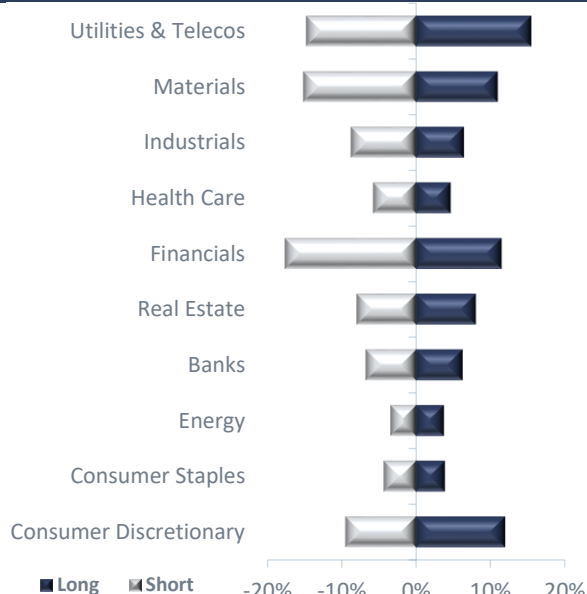
No. Long Positions	74
No. Short Positions	74
Gross Exposure	182%
Net Exposure	-7.8%

Unit Price **\$1.0339**

Performance

	1 Mth	3 Mths	1 Yr	2 Yrs (pa)	3 Yrs (pa)	4 Yrs (pa)	SI (pa)
WARF (net return)	-0.5%	3.2%					3.4%
RBA Cash Rate	0.1%	0.3%					0.4%
Outperformance	-0.6%	2.9%					3.0%

Sector Exposures



Gross Portfolio Structure

Investment Type	\$m	%
Listed Securities - Long	32.2	86.9
Listed Securities - Short	35.0	-94.6
Net Exposure	-2.9	-7.8
Cash	39.9	107.8
Capital	37	100

Managing your Investment

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 and redemption requests up until 2pm on the 10th business day of each month, giving investors the opportunity to review the latest unit price before deciding to apply for, or redeem units. Redemption proceeds will ordinarily be paid within 5 days of the cut off. Investors should refer to the Product Disclosure Statement for the Watermark Absolute Return Fund for details on applying for and redeeming units in the Fund.

For any queries regarding your unit holding, please contact the unit registry managed by Boardroom Limited at watermark@boardroomlited.com.au; or 1300 737 760.

Notes

Notes

Level 23, Governor Phillip Tower, Sydney NSW 2000

TEL (02) 9252 0225 • info@wffunds.com.au • www.wffunds.com.au