



Watershed Income Portfolio

Investment Profile

The Watershed Income SMA is a concentrated portfolio of listed debt, hybrid securities and ETF's or LIT's aiming to generate an income return of 2% above the UBS Bank Bill Index net of fees.

A separately managed account, or SMA, is a professionally managed portfolio whereby the investor receives beneficial ownership of the underlying securities.

The Watershed Income portfolio has a bias towards floating or variable rate fixed interest securities to minimise interest rate risk.

The portfolio should be viewed as defensive with minimal capital volatility and is not expected to generate any long term capital growth.

Key Portfolio Features	
Inception	30 Aug 2010
Benchmark	UBS Bank Bill Index
Authorised Investments	Listed Bonds Hybrid Securities Listed Debt
Number of Securities	10-20
Cash Allocation	2-20%
Investment Horizon	At least 2 years

The Portfolio is designed for investors who...

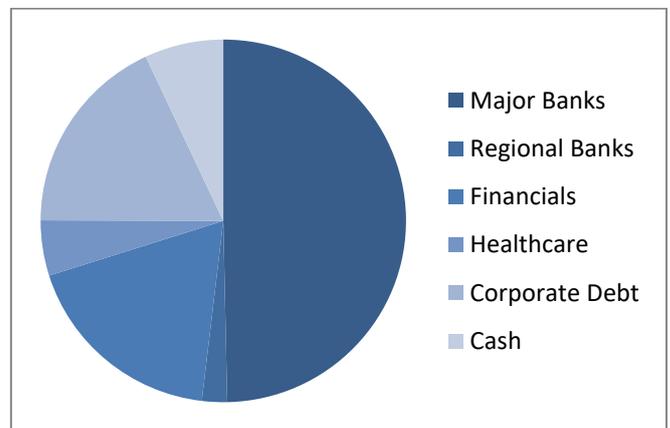
- Seek higher than market, stable, tax-efficient income returns
- Have a medium-term investment horizon and are not expecting any capital gains from their investment

Portfolio Structure

No.	Company Name	ASX Code
1	MCP Master Income Trust	MXT
2	NAB Preference Shares	NABPB
3	ANZ Convertibles	ANZPD
4	ANZ Capital Notes	ANZPE
5	CBA Preference Shares	CBAPD

GICS Sector by Issuer

Major Banks	49.66%
Regional Banks	2.22%
Financials	18.24%
Healthcare	4.93%
Corporate Debt	17.97%
CASH	6.98%
TOTAL	100%



Performance

Net Performance (%)	1m	3m	6m	1yr	2yr	3yr	4yr	5yr	Inception *
WFM Income Portfolio	0.60%	0.93%	1.63%	5.87%	4.75%	7.08%	4.60%	4.54%	5.76%
WFM Including Franking	-	-	-	7.05%	6.05%	8.46%	5.96%	5.88%	7.11%
UBS Bank Bill Index	0.17%	0.52%	1.00%	2.02%	1.88%	1.90%	1.98%	2.13%	
Relative Performance	0.43%	0.41%	0.63%	5.03%	4.17%	6.56%	3.98%	3.75%	

*Inception - August 2010



Quarter in Review

Performance Summary

The Watershed Income SMA continues to provide a high income level with low capital volatility. The portfolio returned positive 0.93% in the March quarter after a 0.70% return in the December quarter despite 10%-20% corrections seen across global share makerts.

The Watershed Income SMA has performed very strongly over the longer term, with performance of **7.11%** since inception including franking.

Portfolio Adjustments

Trimmed: NABPD

Sold: WBCPG

Bought: MQGPD (new issue)

Quarterly Performance Attribution

Top Contributors	Key Detractors
MQGPD	MXT
MQGPC	
AMPPA	

Market View

The US Federal Reserve 'Pivot' (we would call it a monumental backflip) caused an incredible rally in global bond markets this quarter. The Fed has moved from Quantitative Tightening (shrinking its balance sheet and withdrawing liquidity from financial markets) and progressive rate increases to a flat rate outlook (markets are now actually pricing a 25bps cut this year) and have outlined progressively ceasing QE from May to September.

Bond markets in Australia rallied significantly as well, with markets now pricing in two 25bps cuts, taking the official cash rate to just 1%. Despite a very soft housing market, we think that this is overly bearish.

Sector Positioning

The portfolio positioning has adjusted slightly over the quarter with approximately 75% exposed to hybrid and listed corporate debt securities, 7% in cash and 18% in senior secured loans via the Metric Credit Partners Listed Investment Trust. We were expecting to progressively introduce government bond exposure to the portfolio over the course of 2019 as the Fed "normalises rates" but this window closed very quickly over March Quarter. If global growth continues to stabilise over the course of the year we should get a far better entry level.

There were a few changes to the portfolio this quarter. WBCPG was sold to fund the higher margin new issue, WBCPI, which listed in December. We also participated in the new Macquarie issue.

Macquarie Group Capital Notes 4 (MQGPD) listed on the 28th March experiencing strong demand given the attractive 415bps margin above the 3 month bank bill swap rate. This represents the highest new issue margin since the CGFPB offer in Feb 2017 (to which we received and still hold an allocation) which in part reflects the longer duration of 7.5 years to the September 2026 optional call date. We also view the repositioning to partial franking as a positive in light of the ALPs proposed dividend imputation policy. Macquarie is expected to pay distributions franked at 45% for the medium term (given large exposure to international operations – 67% of FY18 income). Partial franking will boost cash income. MQGPD began trading at a premium to the issue price, currently \$102.50 from the \$100 issue price.

The portfolio closes the quarter with a slightly elevated cash weight of just under 7%. As always we continue to look out for attractive new issuance, mis-pricing within the sector and continue to review the macro-economic outlook and interest rate outlook to determine overall sector positioning. However it should be noted that there are no Tier 1 Hybrids callable until March 2020 when MBLPA and NABPC reach their optional call dates, so further supply could be limited in the short term which is favourable for existing pricing in this ultra low interest rate environment.