

Watershed Emerging Leaders Portfolio

Investment Profile

A Professionally Managed Portfolio of Australian Shares

The Watershed Emerging Leaders Portfolio is a separately managed account, or SMA, actively managed by Watershed Funds Management. SMAs are professionally managed portfolios of direct shares whereby the investor receives beneficial ownership of the underlying securities.

Investment Objective

The objective of the Watershed Emerging Leaders Portfolio is to provide investors with long-term capital growth and some tax effective income from a concentrated portfolio of stocks listed outside of the ASX 100. The Portfolio aims to outperform the ASX Small Ordinaries Accumulation Index over the medium to longer term (three to five years) by 2-3% per annum, by undertaking rigorous bottom up stock analysis and active portfolio management.

Key Portfolio Features	
Inception	6 Aug 2013
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Authorised Investments	ASX listed companies not in the ASX 100
Number of Stocks	15-30
Cash Allocation	2-40%
Tracking Error	5% to 9% per annum
Investment Horizon	At least 3 – 5 years

The Portfolio is designed for investors who...

- Seek long term capital growth & some tax-effective income
- Have a longer -term investment horizon of at least three years and accept the risk of significant price fluctuations.

Performance

Net Performance (%)	1m	3m	6m	1yr	3yr	5yr	7yr	Inception*
WFM Emerging Leaders SMA	-1.77%	4.72%	13.85%	25.89%	11.19%	11.97%	14.12%	13.99%
S&P/ASX Small Ords Accum	-2.14%	3.43%	12.23%	30.43%	9.43%	10.17%	10.36%	9.42%
Relative Performance	0.37%	1.29%	1.62%	-4.54%	1.75%	1.80%	3.76%	4.57%

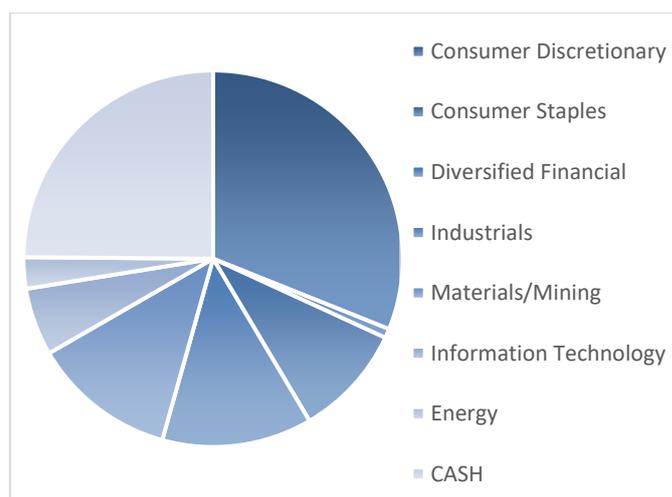
*Inception - August 2013

Performance Fee Disclosure The table above sets out the investment performance returns (AFTER investment management fees, but BEFORE administration fees and taxes) for the portfolio. The performance returns have been calculated on a daily basis taking into account brokerage costs, and are accumulated for the period shown. Returns are shown as annualised if the period is over 1 year, or as total returns otherwise.

Portfolio Structure

No.	Company Name	ASX Code
1	City Chic Collective	CCX
2	IGO Limited	IGO
3	PWR Holdings	PWH
4	Mineral Resources	MIN
5	Baby Bunting Group	BBN

GICS Sector	
Consumer Discretionary	31.10%
Consumer Staples	0.80%
Diversified Financial	9.62%
Industrials	12.81%
Materials/Mining	12.30%
Information Technology	5.81%
Energy	2.69%
CASH	24.87%
TOTAL	100%





Quarter in Review

- The Watershed Emerging Leaders SMA had a strong quarter outperforming the index through reporting period and also the markets first decline in nearly a year during September. The portfolio returned 4.72% for the quarter, outperforming the index by 1.29%
- The portfolio remains well ahead over all longer term time periods except the 1 year, falling behind the strong gains in the market rebound.

Portfolio Adjustments

During the quarter we made the following changes:

New: CNQ (Spin off from SRL)

Sold: CNQ, APT, BIN (takeover), NXL

Quarterly Performance Attribution

Top Contributors	Key Detractors
PWH	MIN
CCX	APX
IGO	WOR

Market Summary

The September quarter began strongly with the full year FY21 reporting period leading the market higher before traditional September market weakness unwound some of the earlier gains. The Small Ordinaries still climbed 3.43% during the quarter after retracing 2.14% in September.

The reversal was driven largely by an outperformance of value stocks over growth stocks primarily due to the uptick in global bond yields in the wake of more hawkish Federal Reserve commentary signalling the near term start to tapering of their massive asset purchasing program (QE).

The worst performing sector in the Small Ordinaries index during the quarter was materials (due to the fall in the iron ore price) followed by technology, whereas the best performing sectors were the more cyclical sectors in Energy and Communications.

Portfolio Positioning

The portfolio has had several changes during the quarter including some very positive corporate activity for two of the bigger holdings in the portfolio.

The first is integrated waste management and recycling company Bingo Industries (BIN) which was removed from official listing after being taken over by a subsidiary of the Macquarie Infrastructure Fund. The takeover included a price of \$3.45 per share plus a special dividend of 11.7cents. This was a pleasing outcome for a company with a strong portfolio of assets that could not be replicated in the waste management and recycling industry. The price represented a 33% increase to the January volume weighted average price (when the proposal was first announced). While this had been flagged for a while, the scheme was only implemented on August 5 and the listed stock was removed from the ASX on August 6.

The second is a fully script takeover offer for Afterpay (APT) by global payment giant Square (SQ.NAS) listed on the Nasdaq. We see this takeover as an ideal fit for both companies utilising each other's technology, as well as merchant and client base, and sold the position in full for \$130 after the announcement. The portfolio is mandated to hold a stock that moves into the S&P/ASX 100 index for up to 24 months before divesting to capture momentum and maximum upside. Afterpay has been the single best investment in the portfolio to date after been introduced from IPO at \$1 a share.

We also sold the small holding in CleanTeq Water (CNQ), a spin-off from battery play Sunrise Energy (SRL) which provides water treatment services for a number of use cases. This split allows SRL to concentrate on its battery materials project via its Sunrise Project, a fully integrated mine to sulphate facility for Nickel and Cobalt, vital components for battery technology.

And finally we sold underwhelming technology play Nuix (NXL) after internal chaos lead to an internal reshuffle and several downgrades to prospectus forecasts, a big faux pas for any newly listed company. While we remain positive on the underlying technology driven by the Nuix Engine, a powerful analytics software used by major government departments, fortune 500 companies, law firms and police departments, it will take the market some time to get comfortable management can deliver what was set out in the prospectus and hit financial targets.

The portfolio is now underweight technology for the first time in several years which we expect to play out well with bond yields moving higher, unwinding some of the valuation gains of higher growth stocks. The portfolio remains materially overweight consumer discretionary which has been a big beneficiary of increasing household savings. And finally, the portfolio still has a meaningful cash position it is seeking to deploy when valuations aren't as elevated, with several stocks on our watchlist.