



WATERSHED

FUNDS MANAGEMENT



FUTURE PLANNERS

Financial Services

Watershed Income Portfolio

Quarterly Report December 2014

Investment Profile

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

The portfolio has a bias towards listed bond exposure and highly-rated, 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.

All issuers must have an investment grade credit rating.

Key Portfolio Features	
Inception	30 Aug 2010
Benchmark	UBS Bank Bill Index
Authorised Investments	Listed Bonds Hybrid Securities Listed Debt
Number of Stocks	10-15
Cash Allocation	0-20%
Investment Horizon	At least 1 year

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

Performance

Gross Performance (%)	1m	3m	6m	1yr	2yr	3yr	Inception *
WFM Income Portfolio	0.61%	1.87%	-0.51%	3.68%	5.07%	5.82%	6.72%
WFM Including Franking	0.71%	2.18%	0.12%	4.93%	6.50%	7.17%	8.07%
UBS Bank Bill Index	0.25%	0.69%	1.36%	2.69%	2.78%	3.18%	
Relative Performance**	0.36%	1.18%	-1.87%	0.99%	2.29%	2.64%	

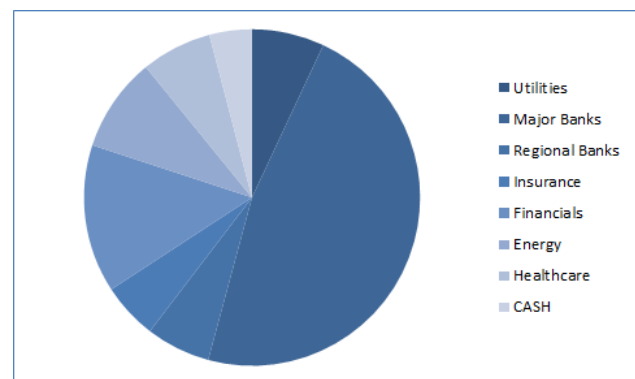
*Inception since August 2010 **Excludes franking

Portfolio Structure

No.	Company Name	ASX Code
1	NAB Preference Shares	NABPB
2	Origin Notes	ORGHA
3	ANZ Notes	ANZPD
4	ANZ Convertibles	ANZPE
5	APA Group Notes	AQHHA

GICS Sector by Issuer

Utilities	6.97%
Major Banks	47.23%
Regional Banks	6.19%
Insurance	5.41%
Financials	14.23%
Energy	9.08%
Healthcare	6.79%
CASH	4.09%
TOTAL	100%





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Quarter in Review

Performance Summary

- The Watershed Income SMA rose by **1.87%** during the quarter, as the sector recovered from a weak September quarter. The UBS Bank Bill Index rose by **0.69%**.
- Over the past year the Watershed Income SMA rose by **3.68%** beating the UBS Bank Bill Index (**2.69%**) by **0.99%**.
- If franking is included in these calculations, the Watershed Income SMA returned **4.93%** over the past year, giving outperformance of **2.24%**, and achieving the portfolio benchmark of **2%** over the cash rate.

Portfolio Adjustments

During the quarter we:

Took up the issues of: Bendigo Bank Convertible Preference Shares, Macquarie Capital Notes and CBA Perls VII.

Monthly Performance Attribution

Top Contributors	Key Detractors
WBC Prefs	RHC Note
APA Note	ORG Note
CBA Perls	CBA Prefs

While the US Federal Reserve has now officially stopped their money printing Quantitative Easing (QE) program, last year saw Japan launch an even larger QE program (relative to GDP) and the European Central Bank looks like initiating a bond buying program of between \$600bn and \$1 trillion Euros early in 2015. This has seen global Bond Yields fall to almost historically low levels.

Another way of looking at this is that Bond Prices are historically very expensive. Despite this, the US is the only major developed economy likely to raise official interest rates off the current emergency levels, which means that we will remain in a low interest rate environment in 2015, both globally and domestically.

In Australia the cash rate is 2.5% (term deposit rates are just over 3%) and the 10 year government bond yield is 2.65% (another historic low). Below is a chart of the 10 year bond yield over the past thirty years.



Consequently we see no value in global or domestic bonds and a great deal of risk in global high yield markets and comparatively view the domestic hybrid and listed debt market (current portfolio running yield 6.31%) as very attractive.