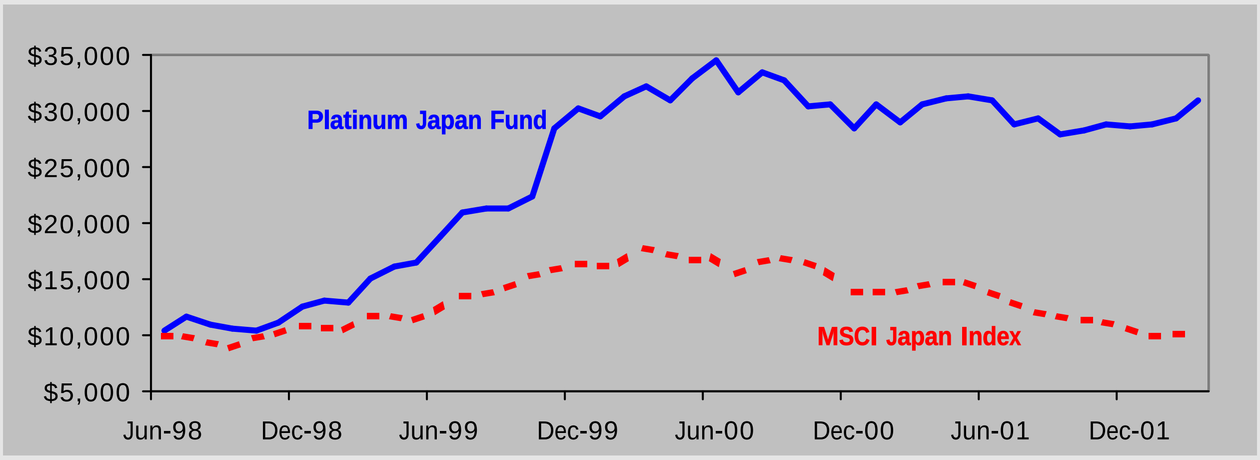
The Platinum Japan Fund

Performance

REDEMPTION PRICE: $1.8893

VALUE OF $10,000 INVESTED SINCE INCEPTION (1 JULY 1998 – 31 MARCH 2002)



The Japanese stockmarket witnessed significant volatility this quarter. During January, the market took a sharp fall of almost 7% as the post-September 11 rally in global markets faded, and people returned to a more pessimistic view of world economic growth. In such a scenario, Japan is seen as particularly exposed due to its weak consumer spending environment and this led to foreign selling of the market. The so-called "Sell Japan Trade" of short Nikkei Index, JGB (Japanese Government Bonds) and Yen became popular once again amongst hedge funds. However February and March saw a sharp reversal as global economic indicators finally signalled a degree of recovery in world growth and helped the Topix to finish 2.6% higher over the quarter. The market recovery was also aided by the Japanese government, which instituted new short-selling rules in the lead-up to the Japanese financial year-end, and this forced many foreign investors to cover their short positions. Meanwhile Korea continued to be a very different story, with the market powering ahead by 24%. The market had been rallying strongly since September on strong domestic growth but this was given added impetus by signs of a recovery in exports. In addition, local investors began to pour into the market as historically low interest rates and a fear of being left out of the action forced their hand.

The Fund managed to perform well during the quarter rising by 8.3% in A$ terms, while the MSCI Japan Index fell 2.6% in A$ terms. This performance was once again driven by our Korean holdings, with Lotte Confectionery, LG Chemical, Samsung Corporation and Seoul Broadcasting leading the way, with gains of 85%, 95%, 68% and 37% respectively. Among our Japanese holdings we managed to avoid any serious declines, although our position in the consumer finance company Aiful was hurt by rising bad debts as the economy continued to slow. We remain optimistic on the stock because of the diversification of its customer base. NTT, a recent poor performer for the Fund, managed to show some signs of renewed life and closed 18% higher. The Fund also benefited in a relative sense from our hedging back into Australian dollars, as that currency appreciated by 4.5% against the US$ over the quarter. The Fund's one year record now stands at +1.7% versus the MSCI Japan Index of –28.3%. Over three years, the compound return has been 27.9% versus -4.3% for the index.

Changes to the Portfolio

DISPOSITION OF ASSETS

Region	Mar 2002	Dec 2001
Japan	65%	64%
Korea	25%	24%
Cash	10%	12%
Shorts	16%	16%

The major change to the portfolio was in our currency position, where we eliminated our hedged position in the Korean Won (raising exposure from 0% to 25%) and also increased our exposure to the yen by 10% to 25%. At the time, our view was that with expectations of a global recovery becoming more pervasive, the pressure would come off the yen and by implication its major trading competitor. However after a short lived move up the yen appears to be headed back toward its recent lows. The remainder of our currency position remains as a hedge into the Australian dollar, which has started to see some strength buoyed by cyclical recovery and a stronger gold price.

Our Japanese positions were unchanged in an aggregate sense but we repositioned toward cyclical and domestic stocks. We added names such as Sekisui Chemical (house building and chemicals), Kirin Brewery and Komatsu. These additions were financed by trimming some of our larger holdings and completely removing Toshiba. Whilst the removal of Toshiba was somewhat premature we remain wary of the company's lack of focus and high debt levels.

With such dramatic price action in Korea and with many of our stocks hitting what we believe is fair value we have started to migrate toward better relative value. Our core positions in companies such as Samsung Corporation and Lotte Confectionery, remain unchanged but we have trimmed around 20% of the exposure. This money has been moved into smaller stocks which would be regarded as higher beta plays or more sensitive to the economic cycle. These stocks are typically valued cheaply, sub 10x PE but some on 2-4x PEs, and at some stage, are likely to be swept up in the continuing bull market. We have also added Kangwon Land (see story below).

In terms of short positions, we have hedged 5% of the Fund's Korean position and 10% of the Japanese position with index futures. We have also taken a number of short positions in technology stocks like Advantest, Sharp and Tokyo Electron, which appear very expensive on an international basis. We have also taken a "pairs trade" by buying NTT and shorting NTT Data, its listed subsidiary against it. Both companies have similar growth profiles but NTT Data is priced in excess of 2x the valuation of its parent.

BREAKDOWN BY INDUSTRY

Categories	Examples of Stocks	Mar 2002	Dec 2001
Thematic	Fujirebio, Noritake, TOC Corp	13%	14%
Cash Generators	Citizen Watch, Air Liquide Japan, Enix Corporation	13%	8%
Restructuring	NTT, MEI, Yamaha Motor	10%	18%
Hidden Assets	Nippon Broadcasting, Toyo Tec, Tenma	7%	9%
Growth Stocks	Towa Corporation, Aiful Corporation	7%	9%
Other	Makita Corporation, Alpine Electronics	14%	6%
Korea	LG Chemical, Korea Telecom, Samsung Corpoation	25%	24%
Cash/Margin Deposits		10%	12%

Commentary

During the quarter, a lot of media attention was given to the Japanese government's changes to the rules governing short-selling of securities. Many cynically regarded this as an exercise in market manipulation just ahead of the financial year-end (31 March) and we would agree. This point is best made when one realises that the main measure of the "Anti Deflation" package announced by the Finance Minister was the imposition of stricter rules on short selling. The demonising of foreign investors as being responsible for the economic problems of Japan highlights how far the authorities are from embracing the right solutions to their problems. But then again, this is perhaps not so surprising considering the results of a recent poll which found that 65% of Japanese are against structural reform as proposed by Prime Minister Koizumi. On the subject of Koizumi himself, the prime minister's approval rating continues to be eroded by the successive scandals engulfing his government and the damp squib of structural reform. It seems that Japan is destined once again for another vicious cycle of apathy, delayed crisis response and political ruction before any new hope can emerge.

Across the water, it is refreshing to speak of the good things happening in Korea. We have discussed the positive structural case for Korea many times in the past, and it is good to see our analysis rewarded. What we are seeing now is a "blowoff" phase as local cash which had remained anchored to the sidelines floods into the market. In many instances brokers are repeating back to us the positive cases on our stocks and raising target prices well above our expectations. In this environment our instinct is to become cautious however we are still positive for the following reasons. We believe it is rare for such a positive structural change in an economy to be fully played out in the equity market in just one year. It is likely that the benefits to corporates accrue over a number of years and that equity prices broadly track this timeframe (although at times such as these they can get over enthusiastic in there role as discounters of the future). Also consider that the local investor is only really just getting started and has a mere 3% of his wealth in stocks. Structural change will most likely mean lower interest rate and risk premiums which are both good for equities. Furthermore, we continue to find cheap valuations in a broad range of stocks with many still on sub 10x PEs. We would think valuations of 15x for the market are appropriate.

One Korean stock which we think still shows great value is Kangwon Land. This company operates a casino complex approximately four hours by road, in the mountains east of Seoul. At present, the company is operating out of a temporary facility (comprising 30 gaming tables, 480 machines, and 200 hotel rooms) until the main casino is opened at a cost of US$850 mn later this year. In mature markets, casinos are generally uninteresting businesses, exhibiting stable, property-like characteristics, with high dividend yields. However, we believe Kangwon Land is much more interesting for the following reasons.

1) Until 2006 legislation will provide the company with a monopoly to cater for Korean casino gamblers. There are other casinos in Korea but these are small and only foreigners are allowed to gamble. Gambling options for Koreans are limited to horseracing with poker machines still illegal.

2) When the main complex is completed, Kangwon Land will become the premier tourist destination in Korea which seriously lacks such quality resorts. The new complex will not only quadruple casino capacity but will be a fully integrated resort destination much along the lines of Malaysia's Resorts World. It will offer 1,600 hotel rooms, 1,000 condominia, an eighteen-hole golf course, a theme park and ski slopes.

3) The Korean consumer is having a wonderful time on the back of full employment and falling interest rates. Asset markets are also enjoying boom times. It is likely that the effect of this new level of wealth will filter through to discretionary expenses such as gambling. The idea of spending more on leisure will be further encouraged as the government enforces a reduction in the working week from six to five days, allowing more time for citizens to spend their leisure dollars (or Won).

4) Koreans demonstrate a particular propensity to gamble. The turnover on the Korean futures exchange is currently $US5.5 bn/day and most of this is retail. Compare this with Tokyo at $US3.7 bn and the CME (S&P and Nasdaq) in the US at $US18 bn, most of which is institutional.

The risks involved in the story mostly surround licence conditions and attendant tax rates levied on the casino. These are valid threats but we would point out that both the company's monopoly status and tax rates are dealt with and enshrined in legislation, meaning any change would require a very solid consensus. In addition, the government retains a 36% stake in Kangwon Land and is unlikely to act to the detriment of its own "golden goose".

The valuation is attractive with the trailing PE ratio being 17x which falls to under 10x when the main casino is opened. Foreign ownership, while rising, is also quite low compared to the other 'large cap' stocks in the market. We would expect that, as has been the case in Australia, the stock will continue to perform very well up until the opening of the main casino later this year.

Outlook

The low level of interest rates and a surprisingly resilient US consumer seem to be stabilising world economic activity. However, we remain sceptical that the excesses of the previous economic cycle, manifested in the technology bubble, have been purged, and as a result, business returns and hence capital expenditure are likely to remain subdued. This means that current hopes for a strong economic rebound will end up petering out and equity markets are likely to experience a further period of lacklustre performance. Consequently, Japan is unlikely to find salvation in an export recovery. We are unlikely to become bullish on the Japanese market in a more general sense until the stand-off between the politicians and the Bank of Japan over the bad loan problem is resolved. At present, the BOJ is refusing to provide additional monetary easing to end deflation until the underlying structure of the economy is overhauled, part of which will necessitate the closure of many companies. As for the politicians' part, they are still too concerned with preserving jobs, including their own. Hence, necessary major change at the macro level is not occurring, notwithstanding some positive developments at the corporate level.

Jim Simpson
Portfolio Manager