Platinum Japan Fund

Jacob Mitchell Portfolio Manager

Disposition of Assets

REGION	JUN 2012	MAR 2012
Japan	89%	91%
Korea	4%	3%
Cash	7%	6%
Shorts	8%	10%

The Fund also has an 11% short position in Japanese Government Bonds.

Source: Platinum

Portfolio Position

Changes in the quarterly long portfolio composition:

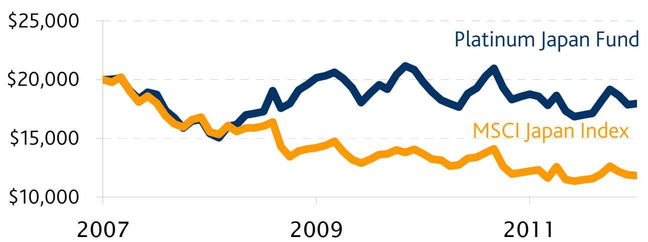
Sector Breakdown

SECTOR	JUN 2012	MAR 2012
DOMESTIC	52%	52%
Retail and Services	19%	18%
Financials	14%	14%
Telco, IT and Internet	12%	10%
Real Estate and Construction	7%	10%
EXPORT	41%	42%
Tech/Capital Equipment	19%	19%
Autos and Machinery	16%	15%
Alternative Energy	5%	5%
Commodities	1%	3%
Gross Long	93%	94%

Source: Platinum

Value of $20,000 Invested Over Five Years

30 June 2007 to 30 June 2012



Source: Platinum and MSCI. Refer to Note 2, page 5.

Performance

Over the past 12 months, the Fund fell 4.2% underperforming the MSCI Japan Index (A$) benchmark by around 1%, and over the past quarter the Fund fell 6.3%, in line with the benchmark.

The quarter witnessed an unwind of last quarter's conspicuous yen weakness as euro woes drove investors back to the yen as the Bank of Japan (BOJ) displayed little urgency in achieving its 1% inflation target. This reluctance by the BOJ is aimed at pressuring the politicians to cut the fiscal deficit so that its own buying of government debt (money printing), doesn't lead to a loss of confidence in the Japanese Government Bond (JGB) market by Japanese households.

Against this backdrop, our best performing stocks included mid-sized consumer orientated entities (Calbee, AIN Pharmaciez and Pal) and large domestic 'defensives' such as telecommunications (KDDI and NTT Docomo). The worse performers were at the export end of the market, that is a reversal of last quarter's action in a pattern that the Fund's investors would be all too familiar with.

One of our recent performers, Calbee, is Japan's leading snack-food company with 60% market share in potato chips. Snack-food businesses have interesting characteristics, the most attractive of which is the need for very fine direct replenishment networks that create significant barriers to entry for dominant incumbents. To illustrate, think of the number of point of sales points that need to be serviced to place a packet of Smiths Crisps within easy reach of the consumer and how hard it would be to cover this cost with a narrow, untested product offering.

As a low profile initial public offering (IPO) with weak sell-side support, what initially caught our interest was that the CEO was previously the head of Johnson & Johnson in Japan (foreign multi-national experience is a positive), that he had been enticed to join Calbee with performance-linked compensation (including options, still relatively rare in Japan), and further, Pepsi was a 20% shareholder. Calbee's profit margins, were and still are, significantly below global peers (7% versus a more typical 15%), especially adjusted for its dominant position. We adjudged that this was a function of a family-run, paternalistic tolerance of inefficient manufacturing and forgiving distribution practices, not uncommon in Japan, however, we also had the sense that a mandate for change had been granted. We suspect the family ultimately wants to sell their stake and, hence, profits are now being prioritised. The company's results since we purchased our holding have confirmed this thesis and the market valuation of the business has increased significantly, though, given the uniqueness of the franchise, there is more money to be made.

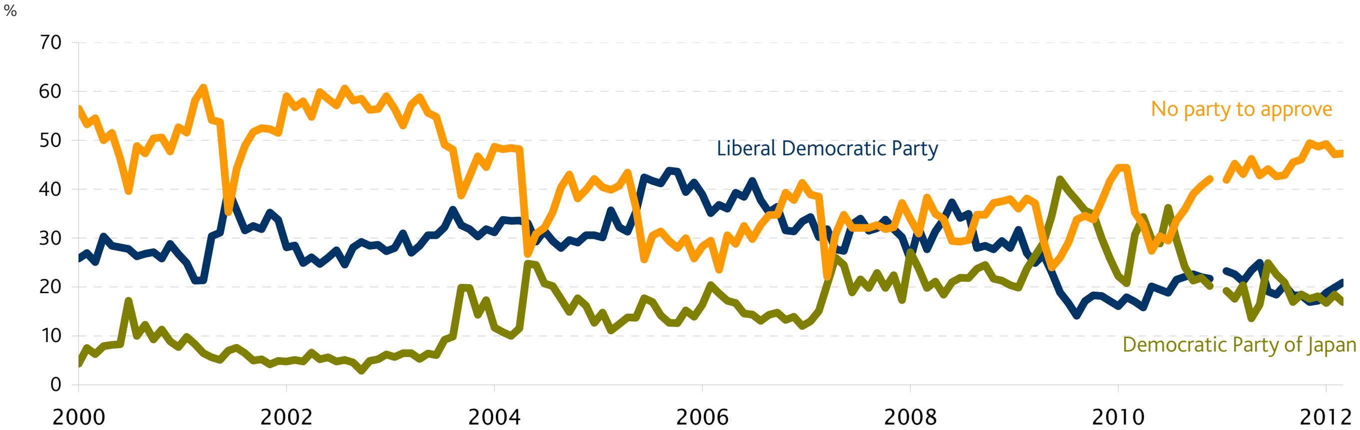
Changes to the Portfolio

Changes to the portfolio were minor in nature. Whilst the search for new ideas is ongoing, when we benchmark current candidates against existing investments we see little reason to change. Our preference for owning the US dollar over the yen also remains unchanged. Whilst additional easing from the BOJ would accelerate yen weakness, there is sufficient deterioration of the terms of trade to support a gradual decline in the currency. We also find it interesting that even at this extremely over-valued level of the exchange rate and atmosphere of gloom, that Japanese inflationary expectations are rising against a global backdrop of declines.

Commentary and Outlook

Japanese manufacturing is under extreme pressure with the viability of companies such as Sony; Sharp, Panasonic, NEC; Renesas, Mazda, Mitsubishi Motors and Nippon Sheet Glass up for question. These companies, and by no means is this an exhaustive list, employ over 800,000 Japanese workers or 1.3% of the total workforce. The currency alone cannot be blamed for their collective predicament, that is, much is self-inflicted, the result of inflexible management and corporate tribalism that has prevented constructive domestic mergers and capacity rationalisation. This is the primary reason we have generally avoided this type of company. Nevertheless, the strong yen is certainly not helping their predicament and a tipping point is approaching.

Japanese Cabinet Approval Rating



Source: NHK

Against this backdrop, it is not surprising that a political vacuum has re-emerged with both major parties unpopular (see chart above). However, until the Japanese people elect an effective anti-establishment leader, current policy gridlock is unlikely to change. As we wrote last quarter, Hashimoto, mayor of Osaka, in some ways fits the bill for this role. The question is whether he can make the transition to the national stage, tap into this disenchantment and then actually overcome bureaucratic inertia.

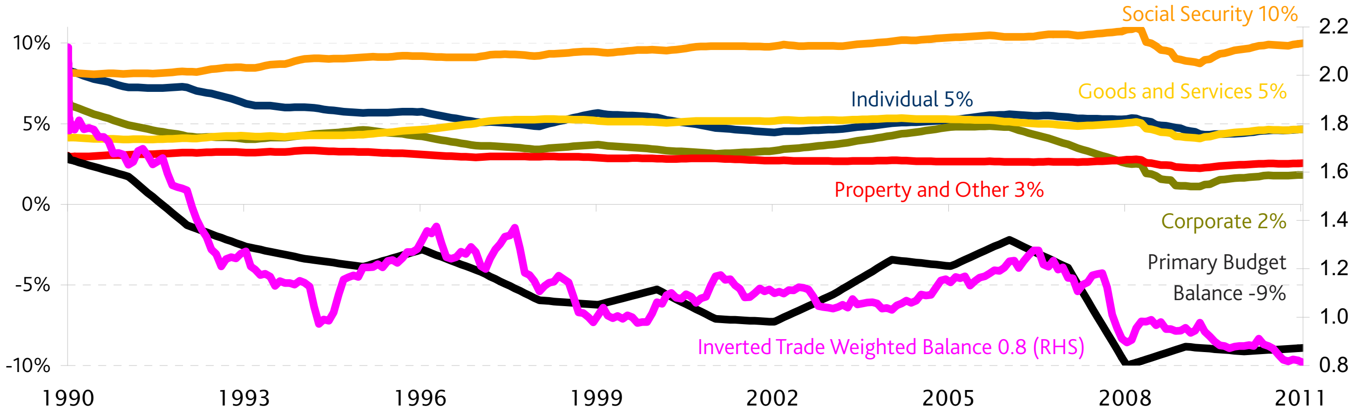
In keeping with a narrow bureaucratic prescription, the lower house of the Japanese government has actually passed a bill to raise the consumption tax from 5% to 8% in April 2014 and 10% in October 2015. The bill still needs upper house approval before becoming law. Prima facie, this is a small step in the right direction, though in isolation, is problematic. Policy makers should also consider cuts to social security transfer payments, corporate reform, trade and labour market deregulation and a lower exchange rate if the aim is to lift the nominal GDP growth above funding cost and achieve sustainable deleveraging of the economy.

To put the enormity of the challenge in context, the consumption tax hikes will raise an additional ¥10 trillion in tax revenue versus current total tax revenue of ¥143 trillion and a fiscal deficit of ¥47 trillion. That is, the Japanese government's current $600 billion per annum funding gap will reduce to $450 billion after the full effect of the tax hikes in 2015 – this could be described as an improvement, but…

The fiscal deficit is highly correlated with yen appreciation (and the yen has appreciated against every currency and over almost all time periods) as the large exporters are the key source of corporate tax revenues and as export profits diminish with yen strength, the corporate tax take declines and the fiscal deficit expands (see chart over). Given China's structural issues and Europe's damaged credit multiplier, global demand is now highly dependent on North America's continued recovery in the face of potential fiscal retrenchment. Against this backdrop, it is difficult to see how Japan can close the fiscal deficit without direct action by the BOJ to target a lower exchange rate and spur exports. Recent acceleration in euro weakness further exacerbates the issue.

Whilst the macro-economic outlook remains uncertain, the good news is that we invest in companies and not countries. From a stock picking perspective, Japan remains a prospective market, valuations are reasonable and the strong companies continue to get stronger.

Japanese Tax to GDP



Source: Macquarie Research

Notes

1. The investment returns are calculated using the Fund's unit price and represent the combined income and capital return for the specific period. They are net of fees and costs (excluding the buy-sell spread and any investment performance fee payable), are pre-tax, and assume the reinvestment of distributions. The investment returns shown are historical and no warranty can be given for future performance. You should be aware that historical performance is not a reliable indicator of future performance. Due to the volatility of underlying assets of the Funds and other risk factors associated with investing, investment returns can be negative (particularly in the short-term).

   The inception dates for each Fund are as follows:
   Platinum International Fund: 30 April 1995
   Platinum Unhedged Fund: 31 January 2005
   Platinum Asia Fund: 4 March 2003
   Platinum European Fund: 30 June 1998
   Platinum Japan Fund: 30 June 1998
   Platinum International Brands Fund: 18 May 2000
   Platinum International Health Care Fund: 10 November 2003
   Platinum International Technology Fund: 18 May 2000

2. The investment returns depicted in this graph are cumulative on A$20,000 invested in the relevant Fund over five years from 30 June 2007 to 30 June 2012 relative to their Index (in A$) as per below:
   Platinum International Fund - MSCI All Country World Net Index
   Platinum Unhedged Fund - MSCI All Country World Net Index
   Platinum Asia Fund - MSCI All Country Asia ex Japan Net Index
   Platinum European Fund - MSCI All Country Europe Net Index
   Platinum Japan Fund - MSCI Japan Net Index
   Platinum International Brands Fund - MSCI All Country World Net Index
   Platinum International Health Care Fund - MSCI All Country World Health Care Net Index
   Platinum International Technology Fund - MSCI All Country World Information Technology Net Index
   (nb. the gross MSCI Index was used prior to 31 December 1998 as the net MSCI Index did not exist).

   The investment returns are calculated using the Fund's unit price. They are net of fees and costs (excluding the buy-sell spread and any investment performance fee payable), pre-tax and assume the reinvestment of distributions. It should be noted that Platinum does not invest by reference to the weightings of the Index. Underlying assets are chosen through Platinum's individual stock selection process and as a result holdings will vary considerably to the make-up of the Index. The Index is provided as a reference only.

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