Platinum Japan Fund

Jacob Mitchell Portfolio Manager

Disposition of Assets

REGION	SEP 2011	JUN 2011
Japan	87%	89%
Korea	3%	2%
Cash	10%	9%
Shorts	14%	13%

The Fund also has a 14% short position in Japanese Government Bonds.

Source: Platinum

Portfolio Position

Changes in the quarterly long portfolio composition:

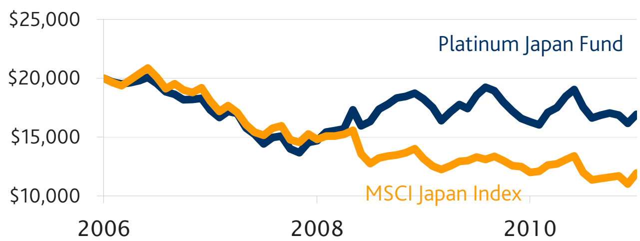
Sector Breakdown

SECTOR	SEP 2011	JUN 2011
DOMESTIC	49%	43%
Retail and Services	19%	14%
Telco, IT and Internet	12%	10%
Financials	11%	12%
Real Estate and Construction	7%	7%
EXPORT	41%	48%
Tech/Capital Equipment	15%	14%
Autos and Machinery	11%	13%
Commodities	10%	13%
Alternative Energy	5%	8%
Gross Long	90%	91%

Source: Platinum

Value of $20,000 Invested Over Five Years

30 September 2006 to 30 September 2011



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

Performance

Over the past 12 months, the Fund rose 3.9%, outperforming the MSCI Japan Index (A$) benchmark by 4.4%, and over the past quarter the Fund fell 0.6%, underperforming the benchmark by 3.7%. For the quarter, the benchmark rose 3.1% in A$ terms and fell 10.7% in Yen terms.

Japan could not escape the downdraft in global markets, driven by sovereign concerns in the euro zone, policy tightening in China and a US slowdown. However, in times of global market distress, Japan is perceived to offer a relative "safe haven" status which has contributed to Japan's recent bout of equity outperformance versus other global markets. In some-ways this reflects a corporate and household sector that has spent a good part of the last 20 years deleveraging. Japan's sovereign position is not great with a 2010 government deficit to GDP of 8.1% and a net government debt/GDP of 116.3%, the highest in the OECD, whilst the country runs a trade surplus, the very strong external position offsets sovereign risk. However, a serious global recession would threaten the trade surplus and ultimately expose Japan's Achilles' heel; a dysfunctional government sector.

Looking a little more closely at attribution, our best performers were domestic stock exposures, especially retail and telecoms, not surprising given the defensive nature of their earnings. Our commodities and autos exposure detracted from Fund performance on global economic slowdown concerns.

Changes to the Portfolio

We have made some incremental changes in portfolio composition as we expect that the macro headwinds that we have often discussed, and have not surfaced, will persist.

Long positions

We have introduced some new longs, in the foods, retail and capital goods sectors. One in particular, Nikkiso, should benefit from increased demand for its niche industrial pumps and stable growth opportunities for their dialysis machines in Asia. Significant latent demand exists in China for dialysis treatment as improved medical coverage and treatment options cover a larger portion of the population. Their joint venture with Weigao group in China is expected to begin local production of dialysis machines from 2012 and targets a 40% market share. There are estimated to be 100,000 dialysis patients in China currently but the latent potential could be as high as 1.5 million, some five times as large as the current Japanese market. We think the earnings growth prospects for this company are both substantial and under-appreciated by the market.

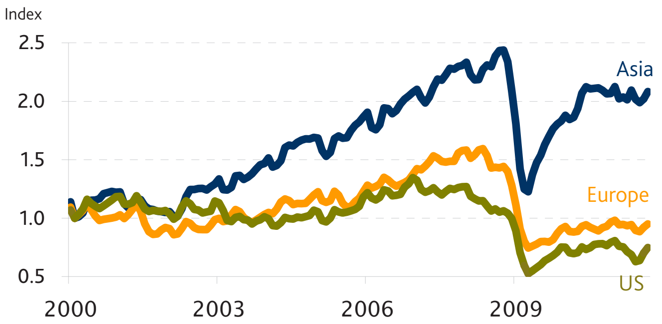
Short positions

We have initiated shorts in names where we believe growth stories have become stale or the earnings risks have not been fully priced in. These stocks represent companies that, while displaying solid earnings, are either not immune to a cyclical slowdown in emerging markets or have exposure to a depreciating Euro/Yen exchange rate. Stock prices have moved well-ahead of their underlying fundamentals and become priced for perfection. Market consensus in Japan at times can be quite slow to discount such turning points, which rewards a more nimble and contrarian approach.

Currency

Unfortunately Japan's safe haven status was also conferred on its currency, which appreciated against most currencies over the quarter. Despite raising our Yen exposure from 35% to 41% over the period, the opportunity cost of not having the Fund fully exposed to Yen accounted for 7% of lost performance relative to the benchmark. The impact of the strong currency is clearly evident in the limited recovery in Japan's exports to Europe and the US (see chart over). Given the issues facing the euro zone, Japan will find it hard to weaken its currency without resolute policy action – something that painfully eludes Japan's political and bureaucratic class.

Japan Exports by Destination



Source: Bloomberg

Commentary and Outlook

Fears of further financial contagion and sovereign risks emanating from the euro zone continue to dominate headlines. It was not so long ago that global markets feared financial catastrophe from Japan which had dragged its feet on cleaning up its banking system. In sharp contrast to the recent falls in global stock markets, led by worries over banks, the stocks of Japanese megabanks have performed in line with the Topix. Whilst affected by a cyclical slowdown and the after affects of the Tohoku earthquake, we do not believe that asset quality is a concern. In a world where sector correlations are close to their highest levels ever, worries about Japans' banks are conspicuous by their absence. Further, in typical pre-emptive Japanese fashion, the megabanks recapitalised twice in the last three years in anticipation of Basel 3 requirements.

The reason for this preparedness is that Japan has spent much of the past 20 years dealing with the deflationary aftermath of its own credit crisis. During the time, when much of the excesses of credit expansion in Western economies were created, Japanese banks were still repairing their own balance sheets. Unwilling and unable to participate in the global credit boom, Japanese banks have now been spared the worst of the bad debts. Japanese banks have limited exposure to euro zone loans.

Japanese megabanks now have one of the lowest loan to deposit ratios globally. Non-performing loan ratios remain below 2%, barely moving even through the GFC. Tier one capital adequacy ratios, a key indicator of bank health, have improved from 7% levels in 2007 to 12% currently. Importantly, the quality of capital has improved: the ratio of deferred tax assets within tier one capital has now dropped from around 30% in 2005 to less than 10% currently, and the proportion of equity holdings in tier one capital has dropped from around 65% in 2005 to 30% currently. In short, Japanese banks have now rebuilt their capital bases and are cautiously emerging after nearly two decades of problems.

Japanese real estate is also showing the first tentative signs of a cyclical recovery after a difficult few years. The key Tokyo market is seeing office vacancy rates peaking out, indicating that the market is able to comfortably absorb new supply. Despite continued falls in existing tenant rents, asking rents for new buildings have fallen to reasonable levels. Real estate transaction volumes are rising and cap rates falling, indicating relatively healthy demand for centrally located prime properties.

Having lived in Japan for most of the past 20 years one could see how government policy plays an outsized role in low growth environments. Many economic reforms have tended to be half hearted and ill-conceived, as they cut across numerous vested interests. Still, Japan has embraced aggressive reforms when needed, most notably during the Koizumi years, which resulted in the longest period of GDP growth in the post-war period (69 months from February 2002 to October 2007). A strong global economy contributed, but it was the resolution of bad debts at the banks in 2003 that allowed domestic growth to accelerate.

There are two key barometers of progress in Japan that are worthy of investor focus. Firstly, merger and acquisition (M&A) activity is slowly gathering momentum and secondly, electoral reform has gained some attention. We will be looking closely at these issues in coming months as they provide the keys to unlocking higher profit share and implementation of pro-growth economic policies.

On the M&A side, Nippon Steel and Sumitomo Metal Industries have agreed to merge by October 2012, subject to Fair Trade Commission (FTC) approval. This has been brought about by a shift to a more pragmatic anti-trust policy, with the FTC now taking into account global market shares of combined entities rather than domestic share. We regard this as a positive step as we believe that large cap corporate Japan needs to gain scale efficiencies in order to better compete globally.

Japan politicians have put-off electoral redistribution to reflect underlying population shifts. The end result is a chronic over-representation of rural and under-representation of urban seats in both the lower and upper house of Japan Parliament. Vote value disparity, which measures the magnitude of this gap, reached a maximum of 5.126 to one (meaning the value of one vote in the least populous prefecture was equal to over five votes in the most populous) in the most recent upper house election and the lower house election was a large 2.524 to one gap.

This has not gone unnoticed and numerous lawsuits challenging the validity of the election results have been ruled on by the High Courts. In March, the Supreme Court of Japan deemed the current lower house distribution as unconstitutional and will require reforms to correct the disparity. The courts have not gone as far as nullifying the election results but have been clear that enacting proposals to correct these disparities will be required before the next general elections (which must be called before August 2013).

The implications of redistricting on economic policy are potentially significant. The current system clearly favours voters in rural seats, particularly increasingly elderly farmers on fixed pensions. These constituencies benefit from deflation and closed agricultural markets and are major barriers to structural reforms. Urban voters, who are generally more in favour of open markets and pragmatic pro-growth policies, should see increased representation. We expect this should result in a focus on more aggressive economic reforms and pro-growth policies designed to reflate the Japanese economy.

Leon Rapp
Japanese Investment Analyst

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$20,000 invested in the relevant Fund over five years from 30 September 2006 to 30 September 2011 relative to their Index (in A$) 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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