

# Platinum International Technology Fund



Alex Barbi Portfolio Manager

## Disposition of Assets

REGION	JUN 2015	MAR 2015
Asia and Other	28%	28%
North America	26%	30%
Europe	15%	12%
Japan	9%	9%
Russia	2%	1%
Africa	2%	2%
Cash	18%	18%
Shorts	3%	3%

Source: Platinum. Refer to Note 3, page 4.

## Performance

(compound pa, to 30 June 2015)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum Int'l Tech Fund	1%	20%	23%	12%	9%
MSCI AC World IT Index	-2%	33%	27%	17%	-3%

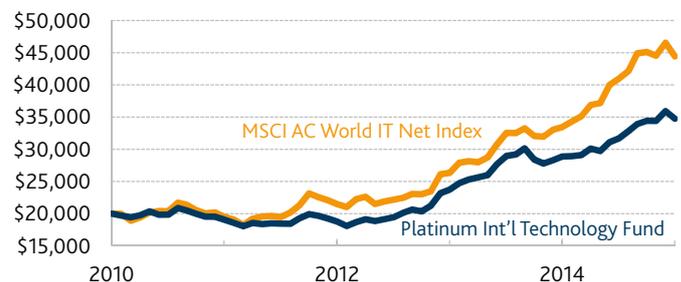
Source: Platinum and MSCI. Refer to Note 1, page 4.

During the quarter the Fund was up 1% while the MSCI AC World Information Technology Index (A\$) was down 2%. For the six months year to June the Fund's return was 10%, compared to 8% for the Index.

Smaller capitalisation holdings outperformed larger companies this quarter and contributed positively to performance for the period. Some of the stronger performers were our Hong Kong-listed and US-listed Chinese companies (H-shares and American Depository Receipts or ADRs, respectively), such as **Youku Tudou** (+96%), **Sina** (+67%), **SouFun** (+40%) and **ZTE** (+33%) (see the Platinum Asia Fund report for detail).

## Value of \$20,000 Invested Over Five Years

30 June 2010 to 30 June 2015



Source: Platinum and MSCI. Refer to Note 2, page 4.

As mentioned in our previous reports, the Fund's investment philosophy is based on portfolio construction independent from the global benchmark, and our recent high exposure to Chinese and other Asian stocks in particular may result in its performance diverging from that of the Index.

We have been holders of several Chinese telecom, Internet and e-commerce stocks on the basis of their relative undervaluation compared to Western peers and their potential for secular growth. We were glad to see some of these holdings appreciate strongly this quarter as other investors also recognised the attractive valuation gap and the potential for further upside. So firm was the recognition that in some cases even the promoters themselves have started buying back shares in the companies they had listed only few years ago. Similarly, some undervalued companies are also being privatised by founders at a modest premium to market valuation, with the idea of re-listing them at a much higher valuation on the Chinese A-share market.

## Changes to the Portfolio

In India we exited our position in **Bharti Airtel** as we believe that competition in wireless services will intensify once Reliance Jio Infocomm launches its new 4G network, with a serious possibility of them also entering into an alliance with existing or other new players.

In Europe we reduced the Fund's exposure to **ADVA Optical Networking** after the stock surged to more expensive valuation levels, and we added to our **Ericsson** position after a 16% stock price correction since April. This gave us the opportunity to increase our holding in a company which we consider to be the best positioned leader in next generation wireless networks.

**Altera**, a semiconductor company specialised in Programmable Logic Devices, was taken over by Intel for a pleasing 46% premium to the entry price we first paid less than a year ago.

As we expect interest rate normalisation to happen first in the US, and with no signs of impending monetary tightening in Australia, the Fund's exposure to the Australian dollar remains low (7%). Major currency exposures as at 30 June include the US dollar 57%, the Hong Kong dollar 11% and the Euro 10%. The Fund's exposure to Japanese stocks remains close to fully hedged into US dollars.

## Commentary

2015 is on track to be a very strong year for mergers and acquisitions (M&A). So far this year, according to Dealogic, total global M&A transactions reached US\$2.19 trillion, an increase of 31% on 2014 and the second highest level after the first half of 2007. While Technology was only the third busiest sector after Health Care, and Oil and Gas, it reported the highest number of deals with 4,074 transactions. Within Technology the semiconductor industry was the busiest.

NXP Semiconductors acquired Freescale Semiconductor to create a US\$40 billion leader in industrial and automotive components. Altera was taken over by Intel for US\$17 billion to further entrench its dominance in data centre. Broadcom was acquired by Avago for US\$37 billion to achieve higher penetration in the market for connectivity components (Wi-Fi etc.).

Some commentators pointed to this renewed enthusiasm for M&A at relatively high prices/valuations as a sign of a new Tech bubble in the making. In fact, when JDS Uniphase combined with SDL in a US\$41 billion merger in 2000 the NASDAQ bubble had just started deflating (JDS Uniphase now has a market valuation of only US\$3 billion).

While these deals are admittedly consummated at high prices, there are some differences compared to 15 years ago.

Firstly, in 2000 global M&A volume was a huge 10% of total global market capitalisation while in 2014 the ratio was a more moderate 5%. Secondly, about half of the acquisitions were completed by issuing new stocks at a time when the NASDAQ Composite Forward P/E ratio was a hefty 40 times and the 10-Year Treasury Notes were yielding just under 7% – corporates were more inclined to issue equity than borrowing cash. Today, instead, debt seems more attractive, with the same P/E ratio at 20 times and the 10-Year Treasury Notes at 2.4%. That obviously does not justify paying crazy prices for dubious businesses while leveraging the balance sheet to levels which may be less than optimal once interest rates start reverting.

So why are all these deals happening right now?

It is interesting to observe that this flurry of activity is developing at a critical point in the consumer electronics cycle. Many data and estimates point in the direction of a growth slowdown and maturity reached by many key consumer electronics end-markets. For example, after years

of double digit growth, global smartphone revenues are expected to grow by only 1% this year and to slightly decline in 2016<sup>1</sup>. Similarly, PC revenues are expected to decline by 7% this year and by 3% in the next, while tablets revenue growth also seems to have reversed (-8% in 2014 and -6% in 2015)<sup>2</sup>.

While Emerging Markets are left with plenty of people in need of their first smartphone, the richest countries are almost approaching saturation level, and they will follow more moderate upgrade/replacement cycles rather than the boom of the past eight years (the first iPhone was introduced in 2007).

In light of this trend, the semiconductor industry is likely to enter a period of more subdued growth. Some analysts even suggest that the traditional multi-year supply-based cycles brought on by (often irrational) capacity additions mis-timed demand cycles, and that generating big revenue swings on a yearly basis may become a thing of the past. This may also explain why many players are taking over sub-scale rivals or companies with interesting products to complement their existing portfolios. Consolidation in some cases may well be the logical solution to a more difficult environment.

That of course does not mean the end of innovation in electronics, as surely some new and more complex devices and applications will be invented, requiring more complex, powerful and efficient semiconductors. Phones and computing devices also require continuous integration of components previously designed and assembled separately, to reduce production costs and meet the requirements of cheaper and more commoditised end products. We may end up only upgrading our smartphones, but these may well become thinner, larger, lighter, or have very different screens, more efficient batteries and many more new functions. Let's think for example about the number of sensors included in a modern smartphone. The Samsung Galaxy S launched in 2010 had three sensors embedded in it (accelerometer, proximity sensor and compass). The Galaxy S5 released in 2014 has ten sensors! In addition to the original three, Samsung added sensors to capture gesture, heart rate, ambient light, a barometer, a 3-axis gyroscope, a finger-print sensor and another one to detect if the cover is open or closed!

<sup>1</sup> Source: IDC.

<sup>2</sup> Source: Gartner.

Furthermore, the trend towards collection of data and connectivity is not limited to personal phones, but is expanding to new devices such as "wearables" (smart watches, fitness bands, activity monitors) and home appliances (think about the concept of "smart-home" where thermostats, TVs, air-conditioning units, alarms, etc. all become connected and remotely monitored and controlled). Think also to industrial or agricultural applications (managing the logistics of containers, pallets, supply chains, farming machinery, utility grids, etc.) or the increased semiconductor content in motor vehicles with the idea of assisted and self-driving cars now gradually becoming a reality.

It is not so fanciful to imagine a proliferation of applications and smart end-points which ultimately will build what is known as the "Internet of Things" (IoT) – the development of the Internet in which everyday objects have network connectivity, allowing them to send and receive data.

The numbers are mind-boggling. In their Visual Network Index forecasts Cisco Systems predicts that globally there will be 11.5 billion mobile devices and connections by 2019, up from 7.4 billion in 2014. A large part of these (3.2 billion) will be Machine-to-Machine (M2M) connections.

## Outlook

While the semiconductor industry may enter a more mature phase, according to Gartner, revenue growth expected for the semiconductor end-markets in the period from 2014 to 2018 will see industrial applications grow by a solid 8.3% per annum, followed by automotive at a respectable 6% per annum. In contrast, consumer applications will only grow by 2% per annum.

Looking at semiconductors by type, the strongest growth will be in non-optical sensors (+10.9%), followed by non-volatile memory (NAND) (+9.5%) and optoelectronics (+8.5%).

The Fund has already identified and invested in some of the areas described above through a few highly specialised, small market capitalisation stocks. Moreover, some of our largest companies are also investing heavily in the same interesting areas. More specifically, they will benefit from the strong growth expected in NAND (**Samsung** and **Intel**) and in the gradual but ubiquitous deployment of the Internet of Things (**Cisco**, **Samsung** and **Intel**).

## Notes

1. The investment returns are calculated using the relevant 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: 28 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

(NB: The gross MSCI Index was used prior to 31 December 1998 as the net MSCI Index did not exist.)

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 2010 to 30 June 2015 relative to its benchmark 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

The investment returns are calculated using the relevant 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 benchmark 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.

3. Invested position represents the exposure of physical holdings and long stock derivatives.

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