

MLC-Platinum Global Fund

QUARTERLY INVESTMENT MANAGER'S REPORT

PERFORMANCE

Fund Size: \$731.8m	Last quarter	Last 12 months	5 years (compound pa)	Since inception (compound pa)
MLC-Platinum Global Fund	1.1%	27.6%	11.2%	10.8%
MSCI All Country World Net Index (A\$)	9.0%	27.7%	14.4%	7.8%

Fund returns are after fees and expenses and assume the reinvestment of distributions. Portfolio inception date: 30 June 1994.

Source: MLC Investments Limited and Platinum Investment Management Limited for Fund returns, and FactSet Research Systems for MSCI index returns.

Past performance is not indicative of future performance. The value of an investment may rise or fall with changes in the market.

The Fund returned 1.1% over the quarter and 27.6% over the year.¹

The global economic picture is still one of strong recovery. The pace of consumer and manufacturing activity in Europe (which had been lagging the US and China) accelerated over the quarter, while company surveys monitoring activity in retail, capital equipment, housing and automobiles point to the US economy being 'red hot'. Overall, we expect the global recovery to continue, albeit naturally slowing from its current pace.

Investors are alert to any situations that may derail the recovery and two events received a lot of focus in this regard. The first was the Chinese government's attempts to lower commodity prices by slowing the build-out of some of its infrastructure projects and then announcing they would sell a portion of their strategic stockpiles of copper, aluminium etc. to increase supply. The second event was the messaging from the US Federal Reserve (Fed) that due to the strength in the economy and labour market, they would bring the timing of their first interest rate increase slightly forward.

¹ References to returns and performance contributions (excluding individual stock returns) in this MLC-Platinum Global Fund report are in AUD terms, unless otherwise specified. Individual stock returns are quoted in local currency terms and sourced from FactSet Research Systems, unless otherwise specified.

These small steps toward policy normalisation generally drove profit taking in the more economically sensitive stocks and saw buying demand return for high-growth/high-priced names. This trend was evident in the portfolio, with our technology and growth holdings performing better than our cyclical holdings.

The standout contributor to the Fund's performance was **Li Ning** with the stock rising 88% over the quarter. Li Ning is a Chinese sportswear brand that carries the name of its founder Li Ning, a famous Chinese gymnast who is the equivalent of China's 'Michael Jordan' in terms of national recognition. The revitalisation of the brand has been a product of six years of hard work, both in developing its own direct-to-consumer distribution and re-establishing its fashion credibility via the development of retro sub-brand China Li Ning and collections with leading international designers. The fruits of these efforts are coming through, with Li Ning sales now growing at 60% p.a.

The most notable detractor from performance was German steel and industrial conglomerate **ThyssenKrupp**. The company is implementing major restructuring, with the strategy to sell multiple divisions in the coming years, a process that will be greatly helped if industrial activity and steel prices remain strong. The stock fell 23% over the quarter, as investors worried that China's move to cool commodity prices would impact steel prices and demand for their product.

DISPOSITION OF FUND ASSETS (NET INVESTED POSITIONS) ^

Region	30 Jun 2021	31 Mar 2021
Asia	32.5%	32.1%
North America*	26.9%	19.3%
Europe	15.6%	13.8%
Japan	14.0%	13.1%
Australia	3.1%	3.2%
Other	0.9%	1.0%
Cash	7.0%	17.5%

^ The geographic disposition of assets (i.e. other than "cash") shows the Fund's exposures to the relevant countries/regions through its long securities positions and long securities/index derivative positions, as a percentage of its portfolio market value.

* As at 30 June 2021, the Fund had a -0.5% short position against the Nasdaq E-Mini Future Sep 21. The Fund's -8.2% short position against the Nasdaq E-Mini Future Jun 21 was closed during the quarter.

Source: Platinum Investment Management Limited.

TOP 10 HOLDINGS ^

Company	Country	Industry	Weight
Samsung Electronics Co	South Korea	Info Technology	5.3%
Micron Technology Inc	US	Info Technology	4.4%
Microchip Technology Inc	US	Info Technology	3.8%
Ally Financial Inc	US	Financials	3.7%
ZTO Express Cayman Inc	China	Industrials	3.5%
UPM-Kymmene Oyj	Finland	Materials	3.2%
MinebeaMitsumi Co Ltd	Japan	Industrials	3.0%
Glencore PLC	Australia	Materials	3.0%
Lixil Group Corp	Japan	Industrials	2.9%
China Overseas Land & Inv	China	Real Estate	2.7%

^ As at 30 June 2021. The table shows the Fund's top ten positions as a percentage of its portfolio market value taking into account its long securities positions and long securities derivative positions. Numerical figures are subject to rounding adjustments.

Source: Platinum Investment Management Limited.

NET SECTOR EXPOSURES ^

Region	30 Jun 2021	31 Mar 2021
Industrials	21.9%	22.4%
Financials	18.6%	17.5%
Materials	18.5%	17.2%
Information Technology	15.6%	15.1%
Consumer Discretionary	6.9%	6.0%
Health Care	5.5%	5.3%
Real Estate	3.3%	3.6%
Communication Services	3.2%	3.6%
Energy	0.0%	0.0%
Other	-0.5%	-8.2%
TOTAL NET EXPOSURE	93.0%	82.5%

^ The table shows the Fund's net exposures to the relevant sectors through its long securities positions and long securities/index derivative positions, as a percentage of its portfolio market value. Index positions (whether through ETFs or derivatives) are only included under the relevant sector if they are sector specific, otherwise they are included under "Other". Numerical figures are subject to rounding adjustments.

Source: Platinum Investment Management Limited.

NET CURRENCY EXPOSURES ^

Currency	30 Jun 2021	31 Mar 2021
United States Dollar (USD)	28.7%	27.2%
Chinese Renminbi (CNY)	16.9%	17.1%
Japanese Yen (JPY)	14.8%	11.5%
Euro (EUR)	13.8%	16.8%
South Korean Won (KRW)	7.8%	7.5%
Indian Rupee (INR)	4.7%	4.4%
Australian Dollar (AUD)	3.7%	4.1%
UK Pound Sterling (GBP)	3.1%	2.8%
Hong Kong Dollar (HKD)	3.1%	2.5%
Canadian Dollar (CAD)	1.8%	4.2%
Brazilian Real (BRL)	0.9%	0.9%
Thai Baht (THB)	0.8%	1.0%

^ The table shows the Fund's net exposures to the relevant currencies through its long securities positions, cash at bank, cash payables and receivables, currency forwards and long securities/index derivative positions, as a percentage of its portfolio market value.

Source: Platinum Investment Management Limited.

Outside of this, the price moves across the Fund tended to be more muted. Of the large positions, US auto lender **Ally Financial** and Indian truck manufacturer **Ashok Leyland** rose 10% and 8% over the quarter respectively after strong results, while DRAM semiconductor player **Micron Technology** (-4%) and Chinese heavy-duty truck engine maker **Weichai Power** (-10%) drifted lower on the aforementioned profit taking.

CHANGES TO THE PORTFOLIO

We have continued the pattern of rotating our holdings after strong price moves.

In this regard, we sold completely out of aerospace engine manufacturer **General Electric** and trimmed our holdings in US building products player **Louisiana-Pacific**, Italian bank **Intesa Sanpaolo** and miner **Glencore**.

We deployed these funds in a number of positions. In terms of companies with structural growth, we added to our position in Chinese e-commerce parcel giant **ZTO Express** and established new positions in financial derivatives exchange operator **Intercontinental Exchange** and European funds management distribution platform **Allfunds Group**. In terms of cyclicals, we increased our position in **Showa Denko**.

Showa Denko is a Japanese specialty materials and chemical company, with two main thrusts to the business:

1. Graphite electrodes are a consumable used in the production of steel using electric arc furnaces. Essentially, they conduct the electricity that is used to melt the scrap steel.
2. Speciality chemicals and gases are consumables used in the production of semiconductors, such as slurries to polish silicon wafers before production steps, or high purity gases used to dry etch transistor designs.

Fuelled by the growth in semiconductor demand, the semiconductor materials division has a solid growth outlook and operates in an attractive niche. They are a small part of the total cost of producing a chip but have a high cost of failure, and given the long qualification processes, once a semiconductor specifies a particular company's chemicals into their production, they are unlikely to be replaced.

The outlook for the graphite electrode business is intriguing, with the business potentially benefiting from the global push towards decarbonisation.

There are two main ways to make steel: either in a blast furnace or electric arc furnace (EAF). Virgin steel is produced in a blast furnace using coking coal, iron ore and limestone, whereas an EAF melts steel scrap via an electrical current. The energy consumption in the EAF process is considerably less, with a tonne of EAF-produced steel generating 67% less CO₂ vs. a blast furnace.²

Steel has not been an attractive place to be for the last decade. China, without a large base of scrap steel to tap into, built-out roughly one billion tonnes of blast furnace capacity in the early 2000s to produce the steel required for its rapid industrialisation. Post 2010, this huge steel build-out led to overcapacity, with Chinese steelmakers routinely exporting up to 100 million tonnes per year, suppressing global steel prices, and electric arc furnace utilisation in the process.

However, the situation is beginning to change. Firstly, after 20 years of rapid economic development, China now has a large enough pool of scrap steel (e.g. old cars, appliances) to feed considerably more EAF capacity. Secondly, the government is taking more action around its CO₂ emissions goals, with the practice of overproducing polluting and high CO₂-generative products for export increasingly being questioned.

We are starting to see a number of policy measures along these lines. Over the past nine months, the Chinese tax credit on steel exports was removed, blast furnace production curbs were implemented in Tangshan (a major steelmaking hub) and the ban on scrap steel imports was removed. These moves disincentivise exports, reduce blast furnace capacity and pave the way for China's steel capacity to shift more to EAFs.

With strong global steel demand, inventories of graphite electrodes have been run down to low levels and prices are now rising. The prospect of lower Chinese export tonnes, increasing EAF utilisation in the West, and in time, more EAF production in China, should have a large positive impact on the pricing of graphite electrodes, and in turn, we would expect on Showa Denko's profits.

² Source: Nucor.

OUTLOOK

Looking forward, on the positive side, the broad economic environment is highly favourable, there is considerable scope for further employment gains and thanks to the generosity of government stimulus payments, the household sector in countries like the US is in excellent shape.

The counter to this, we are at peak fiscal and monetary support and investor sentiment is very much up-to-date with a rosy view. Stock markets have appreciated materially and there are several areas of wild excess in plain view.³

In response to this, we have sold down stocks where the investment case had a large reliance on an economic recovery and increased our cash holding.

In thinking about the next areas of opportunity it's always worth identifying the defining investment focus of the time. In the mid-1990s, we had the enablement of the internet and mobile telephones, with huge wealth and activity created in internet services, networking equipment, servers and the mobile phone supply chain.

³ Examples include valuations placed on the US software-as-a-service (SaaS) space, along with speculation in crypto currencies, special-purpose acquisition companies (SPACs) and meme stocks such as AMC and GameStop.

Today, when thinking about the defining investment focus, it's about:

- **Decarbonisation or changing the electricity mix.** This captures electric vehicles (EVs), renewables and the fact that every major corporation has an Environmental, Social and (corporate) Governance (ESG) mandate, whether they like it or not (e.g. for Pepsi this means a greater demand for recycled or bioplastics).
- **Labour costs rising in traditional low-cost labour pools (e.g. China).** This will create demand for automation and re-shoring production.
- **New drug modalities and synthetic biology.**

Interestingly, the solutions to many of these issues will be industrial in nature and we are dedicating considerable time working through these areas.

Clay Smolinski

Co-Chief Investment Officer & Portfolio Manager
Platinum Asset Management

Macro Overview

by Andrew Clifford, Co-Chief Investment Officer, Platinum Investment Management Limited

Rising Inflation Signals the Need for Wariness in Highly Favoured Names

"The burden of today's spending measures by governments will either be funded by taxation (today or in the future) or through a loss of value in money or cash (i.e. inflation)."

March 2020 Macro Overview

"Assuming that limits do exist on this financial engineering, we need to understand at what point these limits will be reached and what will be the implications of exceeding them. These questions are not easily answered, but certainly, possibilities include a rise in goods and services inflation..."

June 2020 Macro Overview

Regular readers will know that since the outset of the COVID-19 pandemic, we have focused on the role of 'money printing' in funding government rescue packages and the potential for this to flow through to inflation in goods and services. Our concern has been that a surprising outcome in inflation would threaten the low interest rate environment, which has been a major factor underpinning the worldwide bull market in asset prices. The last six month-period has been interesting as we moved from there being no evidence of inflation, to nascent signs, and now some of the highest rates of inflation, at least in the major economies, that we have seen in decades.

Meanwhile, on other fronts, the relationship between the US (and the developed world) and China, on face value, continues to deteriorate. Attempts by governments around the world to rein in fast-growing monopolies in e-commerce and related areas continue. We are also seeing waves of COVID-19 variants continuing to spread across the globe. Yet, despite these developments, equity markets have broadly moved higher this year, with most markets at, or near, record highs. These share price moves mean valuations remain somewhere between stretched to speculative for much of the market. Admittedly, there has been some nervousness around bond yields, interest rates and inflation at various points along the way, however, by and large, markets have remained bullish. Of course, the positive news has been the very strong economic recovery in regions that are moving steadily toward a post-COVID era.

"While there is no evidence of a rise in inflation in goods and services in the major economies yet, it is easy to see an inflation scare unfolding as the year progresses."

December 2020 Macro Overview

"Daily readings of consumer prices already show inflation heading back to levels last seen in mid-2019."

March 2021 Macro Overview

Making predictions on economic variables is fraught with danger. However, the risk for markets with respect to inflation and the direction of interest rates is unlikely to be symmetric. If the inflationary spike turns out to be short-lived and interest rate rises remain a distant possibility, then the market can likely continue along the same path with valuations remaining elevated for the moment. However, the alternative scenario of persistent inflation that results in much earlier-than-expected interest rate increases by central banks is likely to result in dramatic falls in share prices, especially for the highly valued growth stocks. We would continue to argue, that in this environment, investors should remain cautiously positioned.

INFLATION – A TEMPORARY BLIP OR HERE TO STAY?

The US economy continues to power out of the COVID-induced recession. This is happening, even as unemployment benefits and other government transfer payments are progressively being wound back across the country. Employment growth, higher wages and a drawdown on the extraordinary level of savings stashed away last year are more than offsetting the cutbacks in government spending. In Europe, the economy is steadily making progress, even if at a slower pace than the US, and the Chinese economy is strong enough that the government is focused once again on slowing credit growth and reducing leverage across the economy. While growth rates will fall naturally as the year progresses and comparisons are no longer made against the trough of the recession, we do expect that, absent any other shock, global economic growth will remain robust as such momentum in the economy does not dissipate quickly.

This strong recovery, together with the fact that large service industries, such as travel, are still being impacted by COVID-related restrictions, has resulted in a surprising boom in demand for manufactured goods. This strong demand, together with supply chain disruptions in the early stages of the pandemic, has caused a wide range of commodities and manufactured goods, from copper to semiconductors and new homes, to be in short supply. This has resulted in rising prices for many goods and a spike in the consumer price index (CPI) to an annual rate of 5% in the US.¹

A most curious example of this phenomenon is evidenced in the US auto market, which is known for its endless supply of new vehicles. As new car sales reached the highest level recorded on a monthly basis since the global financial crisis (GFC) in April, production of new vehicles has simultaneously fallen to depressed levels as a result of component shortages (see Fig. 1). This has resulted in a 30% increase in the price of used cars and trucks over the past 12 months (see Fig. 2),² with stories that used cars are selling at levels well above the listed price for the same vehicle on the showroom floor!

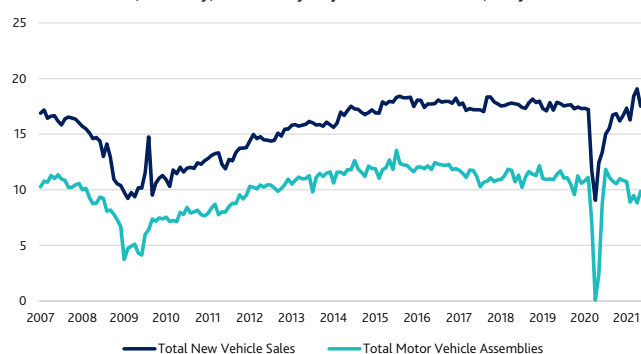
So, is this the beginning of a new era where inflation heads higher and remains persistent? The argument that this is a temporary phenomenon caused by unusual circumstances generally rests on two key propositions. The first is that the supply/demand imbalances we are experiencing will be temporary, even if they take a year or two to resolve, and prices will fall back to where they were. We strongly agree with this proposition. If the economy is good at one thing, it is resolving shortages in the supply of goods and services. The second part of the argument, is that, as government spending winds back, economies will slow dramatically. As we have pointed out, this isn't actually happening to date, and we don't expect it will. Still, that would only suggest that it may take a little longer for prices to fall away.

The debate on inflation is quickly moving to the cost of labour. Despite high unemployment rates in most economies, employers are universally reporting that it is hard to fill roles. This is true not only in the developed world, but also in China.

¹ Source: US Bureau of Labor Statistics.

² Source: Federal Reserve Bank of St. Louis.

Fig. 1: US New Vehicle Sales vs. Production
Millions of Units, Monthly, Seasonally Adjusted Annual Rate, May 2021



Source: Federal Reserve Bank of St. Louis.

There is strong anecdotal evidence that wages are rising and it is expected that various measures of employment costs will post high numbers as the year progresses. There were some expectations that the roll back of government benefits would help ease wage cost pressure as more people returned to the labour force, but it's not clear that this is happening. Time will tell.

However, the escalating cost of labour is not the concern that leads us to be wary about the re-emergence of inflation. Rather, it is the economic premise that if the rate of growth in money circulating in the economy is faster than the growth in the value of the economy's output (i.e. nominal GDP) it will necessarily be inflationary. It is an idea that has long been out of fashion and ignored because it wasn't apparently true.

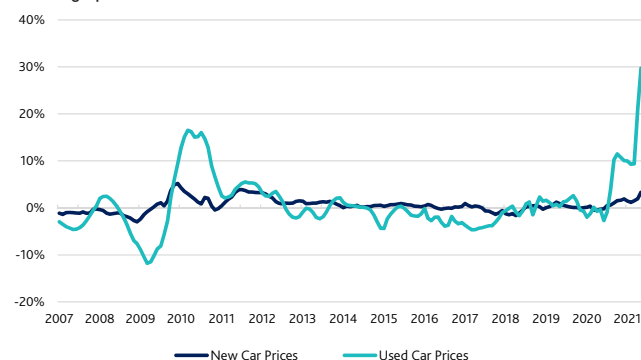
Money printing post the GFC didn't seem to create huge inflationary pressures, at least in the price of goods and services. This is partly because the excess growth in money supply (using aggregates such as M2 or M3) was quite timid. Additionally, inflation was only apparent in the price of assets such as property and shares – not goods and services. In the past 12 months in the US, the printing of money has been prodigious and there has been inflation not only in assets, with residential property prices up 15% over the year to June³ and the stock market up strongly, but now also in the CPI, with some of the highest numbers recorded in decades.

As fiscal spending initiatives roll off, the printing presses will slow. What is not known though is what happens to the so-called velocity of money (or more simply, how often money is spent in a given period). Where households had received government payments and simply left them in the bank, this money was passive and had no influence on the financial system. Economists would view this as driving down the velocity of money. As economies recover, if US households now elect to spend these savings over the next year or two, the velocity of money will start to recover and it remains possible that additional inflationary effects of the money printing last year could be experienced.

³ As measured by the S&P Case-Shiller National Home Price Index.

Source: FactSet Research Systems.

Fig. 2: US New Car vs. Used Car Prices
% change p.a.



Source: Federal Reserve Bank of St. Louis.

DOES IT REALLY MATTER THOUGH IF THE FED AND OTHER CENTRAL BANKS KEEP INTEREST RATES AT LOW LEVELS?

It is important to appreciate that the role of central bank statements is not to tell us what they think is the likely course of interest rates, but to tell us what “they want us to believe” will be the likely course of interest rates. This is not quite as Machiavellian as it sounds. Central banks have rates set low for a reason and they want consumers and businesses to act as if they will stay low for the foreseeable future. When the central banks see the need to change, they will let us know, but the idea that they have the predictive powers to know that this will be sometime in 2023 or 2024 is insane. I think a far better premise for investors is that central banks will increase rates if it becomes clear that inflation is likely to be persistent.

DOES IT REALLY MATTER IF INFLATION IS PERSISTENT? WHY SHOULD THE CENTRAL BANKS RESPOND AT ALL?

Ultimately, the issue with inflation is that it represents a transfer of wealth between different groups in society. This is clearly seen in the discussion around the question of house affordability for first-time buyers that has been taking place in many countries. With goods and services inflation, the impact is usually felt mostly by lower-income households who struggle to put food on the table as prices rise faster than wages. Ultimately, workers will respond and demand higher wages, sparking a wage-price spiral. For this reason, inflation historically has been a serious problem for governments.

Even if central banks don't respond initially to persistent inflation, it is ultimately a political issue. The experience of the 1970s and 1980s was that, the longer it took for governments to respond to rising inflation, the longer and more persistent the problem became.

WHAT DOES THIS ALL MEAN FOR MARKETS?

After the US Federal Reserve's (Fed) Open Market Committee meeting in mid-June, where the comments post the meeting were interpreted as bringing forward the first rate increase from 2024 to 2023, the stock market's reaction was curious. Investors returned to buying their favourite growth stocks and avoiding those more dependent on a good economic environment. This is an odd reaction, as a rate increase is literally years away (if we believe what the Fed tells us) and generally the economically sensitive stocks would be expected to perform well throughout the period of rising rates. This is quite possibly a reflex action by investors to return to perceived certainty (growth stocks and defensive businesses) at a time of uncertainty, rather than a statement that a possible rate increase in two years' time will immediately stifle the economic recovery. This period is also coincident with a rise in concerns around the spread of the COVID Delta variant.

HOW WILL THE CHINA/WEST RELATIONS PLAY INTO THE MARKET'S CONCERNS?

The Group of Seven (G7)⁴ meeting held in mid-June and celebrations of the centenary of the Chinese Communist Party in early July have brought the topic of China's relationship with the West to the front pages of the newspapers once again. As we have discussed previously, the interdependence of our economic systems is a significant limiting factor on actions that can be taken by either side. Certainly, statements from both sides in recent months appear to be more theatre for domestic politics than an intention of meaningful action. This is not to say there are not serious issues at stake here that need attention. When interviewed by the *Financial Times*, Armin Laschet, who is the current frontrunner to become Germany's next chancellor, was quoted as saying, “The question is — if we're talking about ‘restraining’ China, will that lead to a new conflict? Do we need a new adversary?” He also said “And there the European response was cautious, because, yes, China is a competitor and a systemic rival, it has a different model of society, but it's also a partner, particularly in things like fighting climate change.”⁵ This more nuanced approach to the issue of China relations is one that provides some small hope of resolving the current conflicts. In the meantime, the markets are treating the issue as a sideshow, which short of some dramatic developments, it probably is.

Finally, the issue of the anti-monopoly movement continues in the background. In China, action has been taken in regulating areas such as fintech and anti-competitive behaviours in e-commerce. The approach in the West is clearly more process driven and will most likely be a drawn-out affair. In the US, President Biden appointed Lina Kahn, a high-profile academic who has argued for a reframing of US competition laws, to chair the Federal Trade Commission (FTC). This is a pretty clear statement of intent. In the short term though, the FTC case against Facebook has been dismissed. We expect this movement to be a feature of the investment environment for the large e-commerce and payments businesses around the globe.

THE OUTLOOK FOR MARKETS?

In this overview, we have focused on a number of negative elements in the current investment environment. However, the one real positive is the strength of the global economy coming out of the 2020 recession. Generally, one would expect this to be a good time to own shares. Certainly, there are many companies that we hold across our portfolios that we expect will likely benefit from the recovery and still trade at reasonable valuations.

While there are reasons to be optimistic about stock market returns, there are obvious areas of concern, notably the risk of persistently high levels of inflation and the impact on interest rates. It is not a definitive prediction but a reason to remain wary, particularly for investors in the highly favoured growth stocks trading at extremely high valuations.

⁴ The G7 includes Canada, France, Germany, Italy, Japan, the United Kingdom and the United States.

⁵ Source: *Financial Times*, 21 June 2021.

MSCI REGIONAL INDEX NET RETURNS TO 30.6.2021 (USD)

REGION	QUARTER	1 YEAR
All Country World	7.4%	39.3%
Developed Markets	7.7%	39.0%
Emerging Markets	5.0%	40.9%
United States	8.8%	41.9%
Europe	7.6%	35.0%
Germany	4.7%	31.8%
France	9.1%	40.9%
United Kingdom	6.0%	31.3%
Italy	3.6%	36.6%
Spain	5.3%	30.7%
Russia	14.0%	38.6%
Japan	-0.3%	24.8%
Asia ex-Japan	3.6%	39.6%
China	2.3%	27.4%
Hong Kong	2.5%	28.9%
Korea	4.8%	66.2%
India	6.9%	56.4%
Australia	6.9%	39.6%
Brazil	22.9%	46.6%

Source: FactSet Research Systems.

Total returns over time period, with net official dividends in USD.

Historical performance is not a reliable indicator of future performance.

MSCI ALL COUNTRY WORLD SECTOR INDEX NET RETURNS TO 30.6.2021 (USD)

SECTOR	QUARTER	1 YEAR
Information Technology	10.5%	46.0%
Health Care	9.4%	23.5%
Energy	9.3%	39.1%
Real Estate	8.4%	27.0%
Communication Services	8.0%	42.0%
Financials	6.2%	48.9%
Materials	6.0%	49.0%
Consumer Discretionary	5.9%	46.3%
Consumer Staples	5.7%	20.7%
Industrials	4.7%	44.6%
Utilities	-0.4%	14.7%

Source: FactSet Research Systems.

Total returns over time period, with net official dividends in USD.

Historical performance is not a reliable indicator of future performance.

If you have any questions about your investment in the MLC-Platinum Global Fund, please contact the MasterKey Service Centre on

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