Platinum Japan Fund

James Halse
Portfolio Manager#

Performance

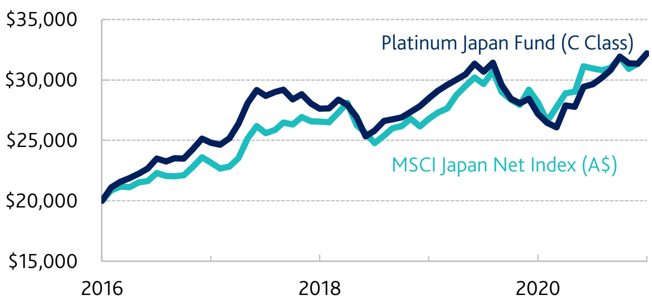
(compound p.a.[+], to 30 June 2021)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum Japan Fund*	1%	18%	5%	10%	14%
MSCI Japan Index^	1%	14%	7%	10%	3%

[+] Excludes quarterly performance.
* C Class – standard fee option. Inception date: 30 June 1998.
After fees and costs, before tax, and assuming reinvestment of distributions.
^ Index returns are those of the MSCI Japan Net Index in AUD.
Source: Platinum Investment Management Limited, FactSet Research Systems.
Historical performance is not a reliable indicator of future performance. See note 1, page 4. Numerical figures have been subject to rounding.

Value of $20,000 Invested Over Five Years

30 June 2016 to 30 June 2021



After fees and costs, before tax, and assuming reinvestment of distributions. Historical performance is not a reliable indicator of future performance. Source: Platinum Investment Management Limited, FactSet Research Systems. See notes 1 & 2, page 4.

The Fund (C Class) returned 0.8% over the quarter and 18.3% over the year.[1]

The Japanese equity market was broadly flat for the quarter in Australian dollar (AUD) terms, as the cyclical rally in the stocks of beneficiaries of stronger global growth and higher interest rates took a time-out, with the current elevated levels of consumer price inflation increasingly being viewed as transitory by market participants (please see our Macro Overview). Given the Fund's exposure to growth cyclicals and deep value plays, it was pleasing that the Fund delivered a similar return to the broader market.

From a Japan-specific standpoint, generally upbeat first-quarter earnings reports were offset by a reticence amongst company managements to raise profit forecasts due to the uncertainty generated by the pandemic. However, despite recurrent waves of infections and concomitant restrictions on movement, the latest Tankan business sentiment survey improved to the best level since mid-2018 for the country's large manufacturers.[2]

Toyota Motor (+13%) was the largest contributor to Fund performance during the quarter due to our large position size. Digital media company **CyberAgent** (+20%) continued its upward trend, as reported earnings and forward guidance beat expectations on a successful game release. **Astellas Pharma** (+14%) performed strongly following the release of an ambitious medium-term strategic plan that was well received by investors, supported by its cancer and anaemia drugs. **Eisai** (+47%) soared on approval of its Alzheimer's treatment by the US Food and Drug Association (FDA). Korean owner of the Bobcat brand of small excavators, **Doosan Bobcat** (+14%), rose on strong US construction-related demand.

Detractors from performance included: excavator manufacturer **Komatsu** (-19%) on fears of weaker demand

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

2 Source: FactSet Research Systems.

James Halse now manages the Platinum Japan Fund following the departure of Scott Gilchrist in April 2021. James joined Platinum in 2011 and has been managing the Platinum International Brands Fund since 2017 and also heads up the consumer sector team.

Disposition of Assets

REGION	30 JUN 2021	31 MAR 2021	30 JUN 2020
Japan	84%	90%	90%
South Korea	7%	8%	4%
Cash	9%	2%	6%
Shorts	-3%	0%	-30%

See note 3, page 4. Numerical figures have been subject to rounding.
Source: Platinum Investment Management Limited.

Net Sector Exposures

SECTOR	30 JUN 2021	31 MAR 2021	30 JUN 2020
Information Technology	24%	26%	8%
Industrials	21%	19%	6%
Consumer Discretionary	12%	19%	11%
Health Care	9%	13%	14%
Materials	8%	6%	3%
Communication Services	7%	8%	25%
Financials	3%	4%	1%
Consumer Staples	3%	1%	-3%
Real Estate	1%	0%	0%
Energy	0%	3%	0%
TOTAL NET EXPOSURE	88%	98%	64%

See note 4, page 4. Numerical figures have been subject to rounding.
Source: Platinum Investment Management Limited.

Top 10 Holdings

COMPANY	COUNTRY	INDUSTRY	WEIGHT
MinebeaMitsumi Co	Japan	Industrials	5.7%
Toyota Motor Corp	Japan	Cons Discretionary	5.1%
Lixil Group Corp	Japan	Industrials	3.5%
Itochu Corp	Japan	Industrials	2.5%
GMO Internet Inc	Japan	Info Technology	2.4%
Nintendo Co Ltd	Japan	Comm Services	2.4%
NEC Corp	Japan	Info Technology	2.4%
Astellas Pharma Inc	Japan	Health Care	2.3%
Toyo Seikan Group	Japan	Materials	2.3%
Kangwon Land Inc	South Korea	Cons Discretionary	2.3%

As at 30 June 2021. See note 5, page 4.
Source: Platinum Investment Management Limited

For further details of the Fund's invested positions, including country and industry breakdowns and currency exposures, updated monthly, please visit https://www.platinum.com.au/our-products/pjf.

and stronger Chinese competition; software distributor **Oracle Corporation Japan** (-13%) as earnings disappointed due to continued pandemic-driven weakness in its on-premise business; and IT services and network equipment firm **NEC Corp** (-12%) as weaker-than-expected near-term profit guidance disappointed the market. Other detractors included industrial tape and optronics manufacturer **Nitto Denko** (-11% to exit point) and trading company **Itochu** (-11%), as cyclical businesses generally pulled back from their highs.

Changes to the Portfolio

The first priority as a new portfolio manager is to acquaint oneself with the stocks held in the Fund and make an assessment with fresh eyes as to their attractiveness. As part of this process, we exited the Fund's large position in **Rakuten** over concerns around management's predilection for destroying capital in pursuit of its founder's empire building tendencies. The stock has been a COVID beneficiary due to its e-commerce exposure, so we were able to exit following strong recent performance. **Inpex Corp** was sold as we viewed its oil-linked exposure as less attractive following oil's strong rally. We also exited **Sony Corp** following a strong run of performance on the success of its gaming business. A number of other positions were exited or trimmed due to more attractive opportunities elsewhere.

Additions to the portfolio were primarily comprised of deep value and other opportunities where activist shareholder involvement provides a clear catalyst for improvement in governance and capital discipline. Stocks in this group included **Toyo Seikan**, **Hokuetsu**, **Fujitec**, **Hi-Lex Corp**, **Heiwa Real Estate** and **Katakura Industries**. We also added innovative property developer **Open House** based on its advantaged business model, growth outlook and attractive valuation. Brewer **Asahi Group** was the final major addition to the Fund as it looks likely to do well with its acquisition of Carlton United Breweries in Australia.

Commentary

Corporate governance was again the topic du jour, with revelations that Toshiba management colluded with government officials to pressure shareholders in relation to their votes at the 2020 Annual General Meeting (AGM). The revelations came in an independent report commissioned as a result of an Extraordinary General Meeting (EGM) in March called by activist shareholders. The report directly contradicted Toshiba's own internal investigation, which concluded there were no issues. CEO Kurumatani resigned not long after the EGM, amid criticism over a bid for the company from his previous employers, CVC Capital, and perhaps in anticipation of the report's conclusions. Recent pressure thus focused on Chairman Nagayama who despite joining Toshiba after the 2020 AGM, nevertheless fought against the establishment of an independent investigation. Proxy advisory firms ISS and Glass-Lewis recommended shareholders vote against Nagayama's reappointment at the 2021 AGM, and again demonstrated their influence at the EGM, with their advice to vote in favour of the shareholder proposals likely determinant of the outcome.

Activist shareholders have been involved with Toshiba, calling for change at a strategic and cultural level since 2017. Despite undertaking some restructuring, Toshiba has had an adversarial relationship with the activists. This stands in stark contrast to the approach taken by scandal-tainted Olympus, which welcomed Robert Hale, partner at shareholder ValueAct, on to the Board in 2019. The stock is up almost threefold since, as Olympus enacted changes including reforming its traditional seniority-based pay structure and selling its loss-making camera division. For reform-minded CEOs, activist shareholders can provide a compelling fulcrum on which to base a strategic rationale.

Emboldened shareholders are underpinned by former Prime Minister Abe's "third arrow" aimed at structural reforms in the management of Japanese companies. The Corporate Governance Code (applying to listed companies) and the related Stewardship Code (applicable to investment firms) are increasingly influential despite compliance being voluntary. The Toshiba scandal could be viewed as having the potential to throw a spanner in the works of this reform process, given the government's involvement. However, it seems more likely that Toshiba is a special case due to its size and the strategic importance of its nuclear business, and Toshiba shareholders appear to be winning the war in any case.

A further test of the appetite for reform may come with the latest scandal at Mitsubishi Electric. CEO Sugiyama resigned on 30 June after revealing that Mitsubishi had falsified inspection data in relation to air conditioning units and compressors used in brakes and doors for trains. The governance implications are particularly large as the conduct took place over 35 years and the revelation follows a similar issue at its rubber products subsidiary in 2018. This new malfeasance may open the door to calls for change from shareholders.

Meanwhile, shareholders continue to push companies for better behaviour, with an estimated 32 activist funds now operating in Japan,[3] and many other shareholders who would not traditionally be classed as activists now encouraged by the Stewardship Code to air their concerns with company managements. Upcoming additions to the Corporate Governance Code are supportive of further reform, including increasing the recommended proportion of independent directors to at least a third. Further reform of the Tokyo Stock Exchange's listing standards from 2022 may shock intransigent managements into action to avoid the loss of face associated with lack of inclusion in the "Prime" market.

Finally, the largest boon to those pushing for change at listed companies may be changes at the proxy advisory firms themselves. Glass-Lewis recently adopted a guideline, which states they will generally recommend voting against the chair of any company "…when the size of strategic shares held by the company exceeds 10% or more of the company's net assets."[4] The applicability of this in the Japanese environment is likely so wide as to be near-universal. Similarly, ISS will recommend voting against management of any company that allocates more than 20% of its net assets to cross-shareholdings.[5] The likely effect of these changes is to dramatically increase the probability of company managements losing shareholder votes, because of the reliance by many institutions on the proxy advisors to determine their voting behaviour. This should be a boon for Japanese stock prices, as companies are increasingly pushed to adopt more shareholder-friendly policies, enhance their capital allocation and improve returns on equity.

Outlook

With the manufacturing sector benefiting from robust global growth and demand for physical products amid pandemic-related restrictions in spending on services, such as travel and leisure, coupled with government fiscal largesse, we are optimistic about the outlook for our portfolio. Shortages of semiconductors should provide a tailwind to several holdings and recent strength in the US dollar will also assist exporters should it be maintained.

The key to the long-term outlook for the Japanese market, however, is the likely continued improvement in corporate governance, and thus capital allocation and shareholder returns. Around 31% of reasonably investable Japanese stocks trade below their net book value,[6] implying weak profitability and/or lazy balance sheets. This dynamic means improvements in returns on equity should not be difficult to achieve, and should provide a tailwind to the Japanese market over the medium-long term.

3 CLSA estimate.

4 Source: Glass Lewis 2020 Proxy Paper Guidelines, Japan

5 Source: https://www.issgovernance.com/iss-announces-2021-benchmark-policy-updates/

6 Stocks with a market cap greater than US$1 billion and daily average trading volume of greater than US$1 million. Source: FactSet Research Systems.

Notes

Unless otherwise specified, all references to "Platinum" in this report are references to Platinum Investment Management Limited (ABN 25 063 565 006, AFSL 221935).

Some numerical figures in this publication have been subject to rounding adjustments. References to individual stock or index performance are in local currency terms, unless otherwise specified.

1. Fund returns are calculated by Platinum using the net asset value unit price (i.e. excluding the buy/sell spread) of the stated unit class and represent the combined income and capital returns over the specified period. Fund returns are net of fees and costs, pre-tax, and assume the reinvestment of distributions. The MSCI index returns are in AUD, are inclusive of net official dividends, but do not reflect fees or expenses. [The gross MSCI index was used prior to 31/12/98]. MSCI index returns are sourced from FactSet Research Systems. Platinum does not invest by reference to the weightings of the specified MSCI index. As a result, the Fund's holdings may vary considerably to the make-up of the specified MSCI index. MSCI index returns are provided as a reference only. The investment returns shown are historical and no warranty is given for future performance. Historical performance is not a reliable indicator of future performance. Due to the volatility in the Fund's underlying assets and other risk factors associated with investing, investment returns can be negative, particularly in the short term.
2. The investment returns depicted in the graph are cumulative on A$20,000 invested in C Class (standard fee option) of the Fund over the specified period relative to the specified MSCI index in AUD.
3. The geographic disposition of assets (i.e. other than "cash" and "shorts") 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. With effect from 31 May 2020, country classifications for securities were updated to reflect Bloomberg's "country of risk" designations and the changes were backdated to prior periods. "Shorts" show the Fund's exposure to its short securities positions and short securities/index derivative positions, as a percentage of its portfolio market value. "Cash" in this table includes cash at bank, cash payables and receivables and cash exposures through derivative transactions.
4. The table shows the Fund's net exposures to the relevant sectors through its long and short securities positions and long and short 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".
5. 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.

Disclaimers

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