

# Platinum Japan Fund



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Portfolio Manager

## Performance

(compound p.a.<sup>+</sup>, to 30 September 2019)

|                               | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|-------------------------------|---------|-----|------|------|-----------------|
| Platinum Japan Fund*          | 5%      | 7%  | 11%  | 14%  | 14%             |
| MSCI Japan Index <sup>^</sup> | 7%      | 2%  | 11%  | 11%  | 3%              |

<sup>+</sup> Excludes quarterly performance.

\* C Class – standard fee option. Inception date: 30 June 1998.

After fees and costs, before tax, and assuming reinvestment of distributions.

<sup>^</sup> Index returns are those of the MSCI Japan Net Index in AUD.

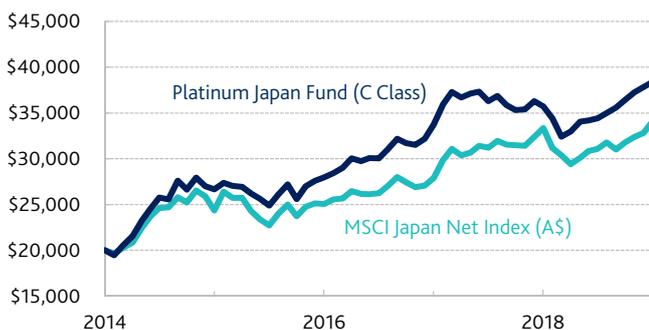
Source: Platinum Investment Management Limited, FactSet.

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 September 2014 to 30 September 2019



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.

See notes 1 & 2, page 4.

The Fund (C Class) returned 5.4% for the quarter and 7.4% for the year.

The Fund was conservatively positioned for most of the quarter, as it has been for the last 12 months, with an average 68% net invested position. Stocks that provided a positive contribution to performance during the quarter included **Oracle Corporation Japan** (+19% over the quarter in local currency terms), **ZOZO** (+22% to the date of exiting the position in late September), **Itochu** (+8%), **Lixil Group** (+12%) and **Toyota Motor Corp** (+8%). The short position in **Celltrion Inc** (-20%) also contributed to performance.

A stronger Japanese yen, especially relative to the Australian dollar, also contributed to the Fund's performance over the quarter and year, as did a weaker Australian dollar relative to the US dollar.

As discussed in last quarter's report, the market is projecting a deflationary environment and thus bidding up the prices for companies with predictable growth and dependable earnings. This is an awkward environment when valuation is such an important part of an investment process.

This current market environment is presenting many opportunities and the portfolio is gradually shifting to a mix of high-quality companies at multi-decade low valuations and reasonably priced growth companies. This shift accelerated during the quarter.

## Commentary

The global debate around deflation, interest rates, debt and sustainable economic growth rates continues to ebb and flow. Japan's corporations and consumers are very familiar with a deflationary environment. Highlighting how the Japanese economic outcome is spreading, Korea's consumer price index fell for the first time in its history. The twin effects of low-cost labour in the developing world and technology-driven disruption in the West are the key factors behind this broad deflationary impulse in any product or sector which faces competition. Many sectors, which previously seemed protected, are now seeing encroachment.

One of the major talking points during the quarter were the ructions in the overnight repurchase market, or repo market on Wall Street, where the median rate soared from its usual

## Disposition of Assets

| REGION | 30 SEP 2019 | 30 JUN 2019 | 30 SEP 2018 |
|--------|-------------|-------------|-------------|
| Japan  | 84%         | 84%         | 74%         |
| Korea  | 5%          | 5%          | 3%          |
| Cash   | 11%         | 11%         | 24%         |
| Shorts | -13%        | -26%        | -10%        |

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

## Net Sector Exposures <sup>^</sup>

| SECTOR                 | 30 SEP 2019 | 30 JUN 2019 | 30 SEP 2018 |
|------------------------|-------------|-------------|-------------|
| Consumer Discretionary | 19%         | 20%         | 12%         |
| Information Technology | 13%         | 12%         | 6%          |
| Industrials            | 12%         | 9%          | 12%         |
| Communication Services | 11%         | 19%         | 13%         |
| Materials              | 7%          | 7%          | 7%          |
| Health Care            | 6%          | 3%          | 5%          |
| Energy                 | 5%          | 3%          | 5%          |
| Financials             | 2%          | 3%          | 9%          |
| Real Estate            | 0%          | 0%          | 1%          |
| Consumer Staples       | -2%         | -2%         | -2%         |
| Other*                 | 0%          | -10%        | 0%          |
| TOTAL NET EXPOSURE     | 75%         | 63%         | 67%         |

<sup>^</sup> A major GICS reclassification was implemented during the December 2018 quarter. The changes affected the Information Technology, Communication Services (previously Telecommunication Services) and Consumer Discretionary sectors. Historical exposures have been updated for continuity.

\* Includes index shorts and other positions.

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

## Net Currency Exposures

| CURRENCY                | 30 SEP 2019 | 30 JUN 2019 | 30 SEP 2018 |
|-------------------------|-------------|-------------|-------------|
| Japanese yen (JPY)      | 102%        | 97%         | 94%         |
| US dollar (USD)         | 15%         | 15%         | 12%         |
| Korean won (KRW)        | 3%          | 3%          | 3%          |
| Australian dollar (AUD) | -20%        | -16%        | -10%        |

See note 5, page 4. Numerical figures have been subject to rounding.  
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>.

band of 2-2.25% to 5.25% in mid-September. The repo market is a key borrowing market in the US, used by banks and financial counterparties for short-term funding. The shortage of liquidity temporarily sent rates sharply higher, requiring the US Federal Reserve to step in and inject liquidity back into the system (by buying US bonds). This event and the subsequent discussion highlighted the lack of visibility in many markets, and the complexity of the highly leveraged global financial system.

This combination of deflation and system complexity gives rise to an important concept: most of our lived experiences are not a good frame of reference for the current environment. There are some episodes in the last few hundred years, which are perhaps analogous, but while history is an important guide, each episode or phase has its own unique characteristics. It's further complicated by the raw immediacy of living through the events, which brings a multitude of human biases into effect. In some past episodes, up to half of the value of the starting capital base was written down.

This year's annual report from **Itochu** highlights the uniqueness of Japan. The CEO wrote an extensive letter containing this sentence: "Each year, in the week after our General Meeting of Shareholders in June, I go to Otani Honbyo in Kyoto to visit the graves of Chubei Itoh I and II, where I make an annual management report."

He goes on to write, "...for example, every April we hold a Special Headquarters management Committee meeting, where we set the management plan for the fiscal year. Ten years ago, the documentation for this meeting ran to around 500 pages. We have gradually whittled this number down to just a fifth, or around 100 pages. We also shortened the meeting from three days to one. ....Nowadays, we start

## Top 10 Holdings

| COMPANY                 | COUNTRY | INDUSTRY           | WEIGHT |
|-------------------------|---------|--------------------|--------|
| Takeda Pharma           | Japan   | Health Care        | 5.0%   |
| Oracle Japan            | Japan   | Info Technology    | 4.5%   |
| Rakuten Inc             | Japan   | Cons Discretionary | 4.1%   |
| Itochu Corporation      | Japan   | Industrials        | 3.6%   |
| Japan Physical Gold ETF | Japan   | Materials          | 3.4%   |
| Nintendo Co             | Japan   | Comm Services      | 3.4%   |
| JXTG Holdings           | Japan   | Energy             | 3.2%   |
| Kyocera Corp            | Japan   | Info Technology    | 3.1%   |
| Canon Inc               | Japan   | Info Technology    | 3.0%   |
| Kangwon Land            | Korea   | Cons Discretionary | 2.9%   |

As at 30 September 2019. See note 6, page 4.

Source: Platinum Investment Management Limited.

acting right after the meeting ends. Instead of simply accepting the status quo, we continue to press forward".<sup>1</sup>

We have met with Itochu management regularly over the years and have developed a good understanding of the progression of their corporate behaviour over the last three decades, in particular the continual business and profitability transformation of the last decade under CEO Okafuji. The current market valuation of a P/E of 7x and dividend yield of 4% implies a return to their former sub-optimal behaviours.

**MinebeaMitsumi** has a 60% global market share for miniature ball bearings. Last year it produced almost 2.4 billion of these products.

In its latest annual report, MinebeaMitsumi's CEO Yoshihisa Kainuma states: "In the past ten years, we have built up a successful track record including 17 M&As both in Japan and overseas. Implementation of these M&As contributed to an increase of approximately 500.0 billion yen in consolidated net sales. We recorded approximately 15.0 billion yen in goodwill, but with the recording of negative goodwill on certain M&As, net goodwill was just 0.3 billion yen".<sup>2</sup>

If you don't own parts of some of the best businesses in the world, which just happen to be valued at multi-decade low valuations in the cheapest developed market in the world, then what do you own?

## Outlook

It's a common belief amongst the dominant news and economic media outlets that Japan's future is dull. This mode of thinking permeates the words, speech and subtext of Western culture and infects the rest. The majority of these accepted mantras are easily proven false. The core of the misrepresentation lies in the short time period used to frame the discussion and the adoption of an easily available template. With North American markets at historically high valuations after a multi-decade bull market it's hard to conceive their return to prior periods of neglect seen last century, even though the conditions and catalysts are already in place. Behavioural finance, valuations, history and contrarian thinking all suggest that investing in Japan should produce strong investment returns over most future timeframes.

The Fund commenced investing in Japan in the market trough of June 1998. Over the subsequent two decades, the Fund has returned 14.3% compound p.a. for a cumulative return of

1,621% (as at 30 September 2019). Over the same time period, the broad Japanese market returned 3.2% compound p.a. for a cumulative return of 93.6%. The Topix Index in June 1998 was roughly 1200, not far below today's level of 1600.

Since its inception, the Fund has experienced three multi-year episodes of significant returns. The first two episodes were followed by an extended fallow period. The last seven years have not been fallow with a compound return of 20.8% p.a., or a cumulative return of 274.9%.

As illustrated by the above quotes from the CEOs of Itochu and MinebeaMitsumi, Japan abounds in cheap investment opportunities combined with management that charts their own path, often far from global norms. A recent presentation highlighted the dramatic rise in shareholder activism and private equity agitation against Japanese companies. This is against a backdrop of continuing improvement in corporate governance, domestic pressure for improved financial performance and the need for higher dividends in an environment of low interest rates. Future returns are unlikely to be what your personal investment experience would lead you to expect, and are unlikely to be the same as those found in other regions, perhaps even diametrically opposed.

In contrast to the clear opportunity, sentiment towards the Japanese stock market is weak. Foreigners have been selling Japanese equities consistently for the last few years. Locals have been building their cash positions and they now hold many trillions of yen in bank deposits earning zero interest. They will presumably soon be confronted with negative rates as seen in other regions.

After an extended period of global uncertainty, it appears as though one of the underlying concerns has been partially addressed through the provision of bountiful short-term US dollar liquidity to global markets. The destination of liquidity is never certain. Many underlying issues remain to be addressed, but perhaps the rise of Modern Monetary Theory's veiled confirmation of the government's monopoly on the issue of money and thus their implicit ability to set the price level across the economy is a broad pacifier. Increasingly, global central banks are acting as liquidity providers of the first resort.

The ever-changing fads, whims and fashions of human behaviour are a constant, which is particularly evident and powerful in Japan. When combined with the current unsettled economic environment, these ebbs and flows of investor psychology present a broad range of investment opportunities at prices that are both rare and attractive. This is most certainly the case today, even after a long stretch of good performance by the Fund.

<sup>1</sup> Source: [https://www.itochu.co.jp/en/ir/doc/annual\\_report/index.html](https://www.itochu.co.jp/en/ir/doc/annual_report/index.html)

<sup>2</sup> Source: [https://www.minebeamitsumi.com/english/corp/environment/integrated\\_report/](https://www.minebeamitsumi.com/english/corp/environment/integrated_report/)

## Notes

1. Fund returns are calculated using the net asset value (NAV) unit price (which does not include the buy/sell spread) of the stated unit class of the Fund and represent the combined income and capital returns of the stated unit class over the specified period. Fund returns are net of fees and costs, are pre-tax, and assume the reinvestment of distributions. Returns for P Class are net of any accrued investment performance fee.  
The MSCI Index returns are in Australian Dollars and are inclusive of net official dividends, but do not reflect fees or expenses. For the purpose of calculating the "since inception" returns of the MSCI Index, the inception date of C Class of the Fund is used. Where applicable, the gross MSCI Index was used prior to 31 December 1998 as the net MSCI Index did not exist then. Fund returns are provided by Platinum Investment Management Limited; MSCI index returns are sourced from FactSet.  
Platinum does not invest by reference to the weightings of the Index. A Fund's underlying assets are chosen through Platinum's bottom-up investment process and, as a result, the Fund's holdings may vary considerably to the make-up of the Index that is used as its reference benchmark. Index returns are provided as a reference only.  
The investment returns shown are historical and no warranty can be 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.  
The stated portfolio values of C Class and P Class of the Platinum International Fund (PIF) do not include funds invested in PIF by the Platinum International Fund (Quoted Managed Hedge Fund), a feeder fund that invests primarily in PIF. The stated portfolio values of C Class and P Class of the Platinum Asia Fund (PAF) do not include funds invested in PAF by the Platinum Asia Fund (Quoted Managed Hedge Fund), a feeder fund that invests primarily in PAF.
2. The investment returns depicted in this graph are cumulative on A\$20,000 invested in C Class (standard fee option) of the specified Fund over the specified period relative to the specified net MSCI Index in Australian Dollars.
3. The geographic disposition of assets (i.e. the positions listed other than "cash" and "shorts") represents, as a percentage of the Fund's net asset value, the Fund's exposures to the relevant countries/regions through direct securities holdings and long derivatives of stocks and indices.
4. The table shows, as a percentage of the Fund's net asset value, the Fund's exposures to the relevant sectors through direct securities holdings as well as both long and short derivatives of stocks and indices. In the case of the Platinum Unhedged Fund, the Fund does not undertake any short-selling. Its net exposures are therefore the same as its long exposures.
5. The table shows the effective net currency exposures of the Fund's portfolio as a percentage of the Fund's net asset value, taking into account the Fund's currency exposures through securities holdings, cash, forwards, and derivatives. The table may not exhaustively list all of the Fund's currency exposures and may omit some minor exposures.

6. The table shows the Fund's top 10 long equity positions as a percentage of the Fund's net asset value, taking into account direct securities holdings and long stock derivatives. The designation "China" in the "Country" column means that the company's business is predominantly based in mainland China, regardless of whether the company's securities are listed on exchanges within mainland China or on exchanges outside of mainland China.

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