Platinum®
ASSET MANAGEMENT

# Quarterly Report

## 30 June 2014

Platinum International Fund
Platinum Unhedged Fund
Platinum Asia Fund
Platinum European Fund
Platinum Japan Fund
Platinum International Brands Fund
Platinum International Health Care Fund
Platinum International Technology Fund

The Platinum Trust quarterly report is available on our website, *www.platinum.com.au*, from approximately the 15th of the month following quarter end

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# Performance Returns to 30 June 2014

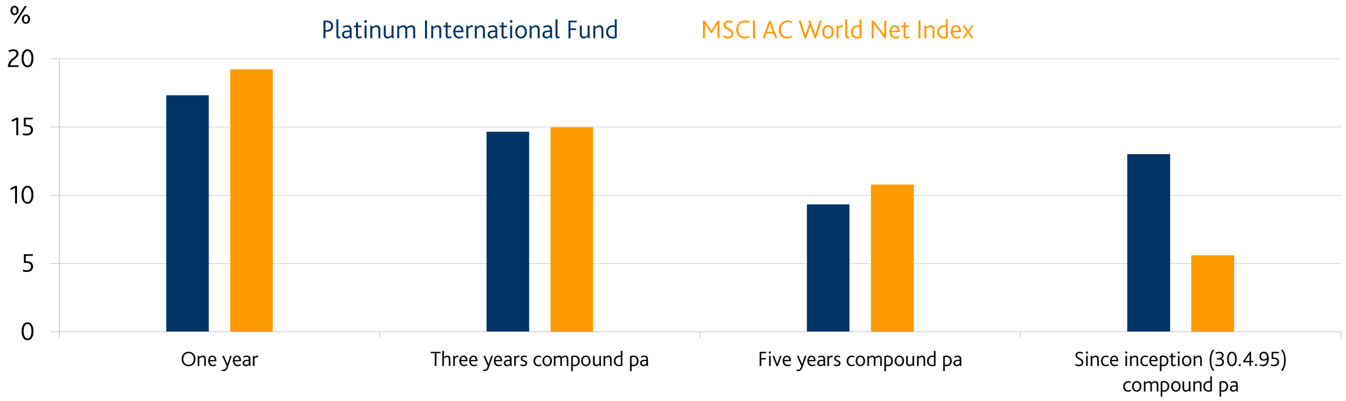
| FUND | PORTFOLIO VALUE (POST 30 JUNE CASH DISTRIBUTION) | QUARTER | 1 YEAR | 2 YEARS *COMPOUND PA* | 3 YEARS *COMPOUND PA* | 5 YEARS *COMPOUND PA* | SINCE INCEPTION *COMPOUND PA* |
|---|---|---|---|---|---|---|---|
| International Fund | $9523.5m | 2.2% | 17.3% | 26.9% | 14.7% | 9.3% | 13.0% |
| MSCI AC* World Net Index | | 3.1% | 19.2% | 24.8% | 15.0% | 10.8% | 5.6% |
| Unhedged Fund | $291.6m | 3.1% | 22.2% | 28.7% | 16.0% | 13.1% | 11.2% |
| MSCI AC World Net Index | | 3.1% | 19.2% | 24.8% | 15.0% | 10.8% | 4.8% |
| Asia Fund | $4425.9m | 6.2% | 17.4% | 22.9% | 12.2% | 8.7% | 16.0% |
| MSCI AC Asia ex Japan Net Index | | 5.3% | 12.9% | 17.3% | 7.6% | 7.6% | 9.8% |
| European Fund | $288.0m | 0.5% | 18.5% | 24.8% | 14.9% | 16.0% | 12.1% |
| MSCI AC Europe Net Index | | 1.6% | 24.4% | 28.3% | 12.6% | 9.4% | 2.0% |
| Japan Fund | $425.5m | 5.0% | 14.5% | 35.8% | 20.9% | 10.4% | 14.3% |
| MSCI Japan Net Index | | 4.7% | 6.5% | 20.8% | 12.2% | 4.0% | 0.5% |
| International Brands Fund | $1229.1m | -0.4% | 11.1% | 21.6% | 11.9% | 15.5% | 13.0% |
| MSCI AC World Net Index | | 3.1% | 19.2% | 24.8% | 15.0% | 10.8% | 0.3% |
| International Health Care Fund | $102.7m | 0.7% | 20.0% | 27.2% | 19.2% | 16.5% | 7.7% |
| MSCI AC Wld Health Care Net Index | | 2.9% | 24.6% | 32.9% | 24.7% | 15.5% | 7.1% |
| International Technology Fund | $59.9m | 1.7% | 21.7% | 24.1% | 14.8% | 9.2% | 8.7% |
| MSCI AC World IT Net Index | | 4.3% | 27.1% | 24.8% | 19.7% | 13.0% | -4.9% |

*Morgan Stanley Capital International All Country

Source: Platinum and MSCI. Refer to Note 1, page 40.

**Platinum International Fund Versus MSCI AC World Net Index**

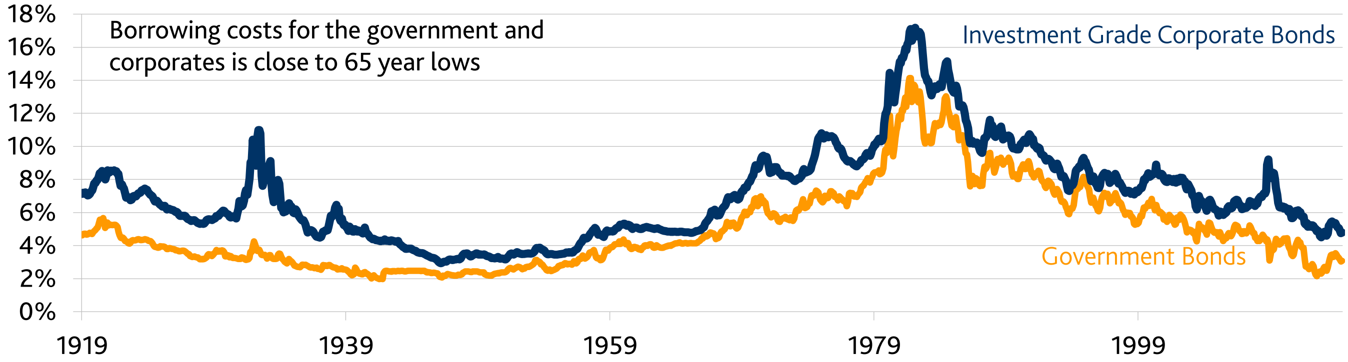
*To 30 June 2014*




Source: Platinum and MSCI. Refer to Note 1, page 40.

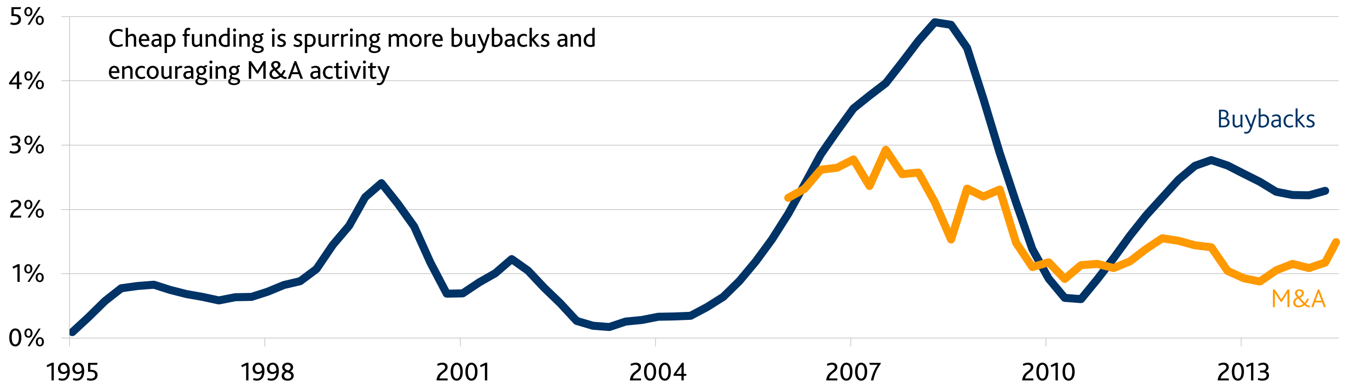
# Market Panorama

### US Bond Yields



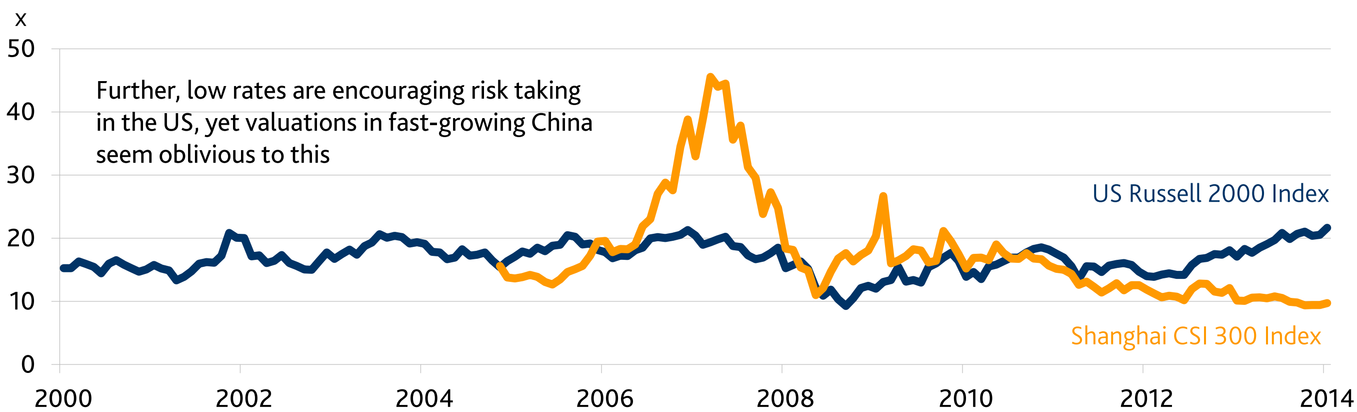

Source: Ned Davis Research

### US Corporates - Buybacks and Merger & Acquisitions (% of market cap)




Source: Ned Davis Research

### Trailing Price/Earnings Ratio (ex loss makers)




Source: Ned Davis Research

# Platinum International Fund

**Kerr Neilson** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| North America | 27% | 26% |
| Europe | 24% | 26% |
| Asia | 23% | 21% |
| Japan | 14% | 15% |
| Russia | 3% | 1% |
| Australia | 1% | 1% |
| South America | 1% | 1% |
| Cash | 7% | 9% |
| Shorts | 12% | 13% |

Source: Platinum. Refer to Note 3, page 40.

## Performance

**(compound pa, to 30 June 2014)**

| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Int'l Fund | 2% | 17% | 15% | 9% | 13% |
| MSCI AC World Index | 3% | 19% | 15% | 11% | 6% |

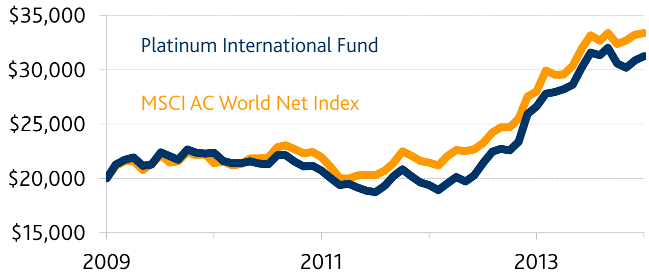
Source: Platinum and MSCI. Refer to Note 1, page 40.

Markets edged progressively higher over the last quarter. It was not without dissent as the highly rated Internet, big data and biotechs got hammered, falling typically by 30% as the market reassessed their virtues. Preference moved to their 'old economy' tech forebears like Intel, Microsoft, Oracle and Qualcomm which in some cases are rated below the average of the US market. More attention was paid to cyclical stocks.

The scare about the emerging markets and the adverse effect of rising US rates dissipated. Flows turned positive by quarter's end. These fears are well-founded in the case of Russia, Brazil, Turkey and South Africa as they have squandered the resource bonanza by shunning economic reforms. Their soft political underbelly was further exposed by the evident machinations in the border region of the Ukraine, the pre-World Cup demonstrations in Brazil and sinister revelations regarding the political elite.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

Concerns also arose in China as some wealth management products became unstuck, bonded holdings of commodities were found to be missing and residential property prices crumbled. By quarter's end all was forgiven following reassurance by the leadership and prospects of continuing reform. The jubilation that surrounded the emphatic win by the Bharatiya Janata Party (BJP) led by Narendra Modi set the Indian market on fire.

The MSCI World Index in Australian dollars finished the quarter 3.1% higher and up 19.2% for the last 12 months. Noting the improving tendency of the more cyclical sectors, the Fund achieved 17.3% for the year.

## Changes to the Portfolio

Growing excitement about opportunities in some metal, noted last quarter, and financials in China, caused us to exit or cut some very successful and long-held companies like **Amadeus IT Holding, Roche Holding AG, Bank of America, Yonyou Software, Toyota Motor, Hoya, Rohm Semiconductor and SBI Holdings.** We also cut the holding in **Jacobs Engineering** even though the US investment cycle is still young because of disappointment with its recent acquisitions. Using the proceeds, we added to a beaten-up competitor, **KBR**. Funds were removed from Intesa Sanpaolo after it had doubled in less than a year.

The thrust of our buying was in Asian financials, metals and minerals and the new Internet opportunities. Around 2.5% was employed in nickel plays like **Sumitomo Metal Mining** and **Norilsk Nickel**, and a derivative concept thereof in stainless steel, **Outokumpu**. We added further to our oil play, **Canadian Oil Sands**.

It is the antiquated regulation of interest rates that sits at the heart of the surge in so-called wealth management products in China. This in turn is distorting the fluid flow of capital and this is subject to review for change. As interest rates are allowed to function freely (to ration and allocate capital) so the benefits will accrue to those who **control large pools of savings**, namely, the insurance industry and prospectively, the banks. We, however, favour the life insurers as they have been the most penalised by these restrictions through their large holdings of cash and bonds and will potentially gain the most from their liberalisation.

Following the problems of the industry around 2005, the insurance regulator in China has set very conservative guidelines as to the deployment of insurance investment pools. Both China Life Insurance and China Pacific Insurance are the most conservative of the domestic providers.

**MSCI World Index Regional Performance (AUD)**

| REGION | QUARTER | 1 YEAR |
|---|---|---|
| India | 11% | 24% |
| Hong Kong | 6% | 14% |
| **Asia ex Japan** | **5%** | **13%** |
| **Japan** | **5%** | **7%** |
| **Emerging Markets** | **5%** | **11%** |
| Korea | 4% | 21% |
| United Kingdom | 4% | 23% |
| China | 4% | 12% |
| **United States** | **3%** | **20%** |
| **Developed Markets** | **3%** | **20%** |
| **Europe** | **2%** | **24%** |
| Australia | 1% | 17% |
| France | 0% | 24% |
| Germany | 0% | 25% |

Source: MSCI

**MSCI World Index Sector Performance (AUD)**

| SECTOR | QUARTER | 1 YEAR |
|---|---|---|
| Energy | 10% | 24% |
| Utilities | 5% | 19% |
| Information Technology | 4% | 27% |
| Consumer Staples | 3% | 11% |
| Health Care | 3% | 25% |
| Materials | 3% | 19% |
| Telecommunication Services | 2% | 15% |
| Consumer Discretionary | 2% | 17% |
| Industrials | 1% | 21% |
| Financials | 1% | 15% |

Source: MSCI

**China Life Insurance** is the largest life insurer in China with 177 million policyholders, 650,000 agents and a market share of about 30%. It has been slow to fully industrialise its sales force, and like its peers, went through a period of selling low-margin savings products (as the wealth management products introduced more competition in its traditional domain) and fretted about market share.

This emphasis is now changing as it realises the benefit of streamlining its sales force and focusing on the long-term profitability of its ever-growing book of business. By comparison with the performance of its peers in countries like India, the Chinese insurers have undersold life insurance with premiums running at only 33% of GDP versus 58% in India. We therefore believe that maintaining the historic premium growth rate of 15% pa is quite achievable in the foreseeable future. In addition, the spreads on their book should gradually creep upwards as interest rates are allowed to reflect real market conditions and developments such as a market in provincial bonds takes root. They should also benefit from the share component of their investment pools, which represent some 8% of the total, as the Chinese domestic equity market recovers. The Shanghai Index has more than halved while the economy has doubled in size and now trades on under 9 times earnings. Overall, the odds favour this company to give us a return of 20% pa for several years!

**China Pacific Insurance** which is controlled by the Shanghai Government is arguably more advanced in this transformation process. Having faced difficulties in 2005, it benefitted from an injection of capital and know-how from the Carlyle Group and other foreign insurance participants. It is well-capitalised and from what we can learn is successfully adopting the highly structured agent-based sales approach mastered by foreign experts like AIA. We are buying these businesses at a discount to comparable companies in other jurisdictions even though they are likely to grow faster. (Ping An Insurance is generally regarded as the most competent indigenous insurer but it owns a bank and also has much greater exposure to higher risk loans making it more susceptible to the unwinding of the property market in China.)

Weakness in Russia allowed us to add to our position in the Russian-based search provider, **Yandex**. This company dominates the local market with nearly 70% market share and has augmented its offering with ancillary services. As more sophisticated 4G phones fall in price, Yandex should benefit. It is not without risks on account of Google's stranglehold on the android operating system and products like Chrome. However, the company is likely to continue to grow strongly and at 25 times earnings, is good value. We also added to **Tencent Holdings, Youku Tudou** and **Baidu** having cutback **Zillow** and **QIWI** after very strong moves.

We also initiated a position in **LinkedIn**. For the investment case, please read Clay's rendition in the Platinum Unhedged Fund Quarterly Report.

### Shorting

The shorts continue to see-saw, only giving the benefit of evening out some of the short-term volatility of the portfolio. There was little change in our positions at 12%.

### Currency

We continue to hold little Australian dollar and Japanese yen, favouring the US dollar and the underlying European and Asian exposures. We did, however, hedge out 4% of the underlying exposure to the Chinese renminbi in the belief that a slightly weaker currency would assist the economic transition that has now begun.

## Commentary

We have been perplexed by the persistent caution expressed by investors and financial advisors during the road show we held over the last few weeks in Australia's major cities. Going back over our quarterlies we can trace a clear message of opportunity and it was only in March that we started to express concern about US valuations, particularly of those in the Russell 2000 Index.

We still hold the view that the global economy is gradually healing, that inflation risks are low in most countries; hence there is no need for Central Banks to tighten monetary policy quite yet. To the extent that the US economy is experiencing a sturdier recovery, it together with Britain, will be among the forerunners to experience higher rates but the European Central Bank (ECB) and the Bank of Japan (BOJ) are far from this point. This was underscored with the last ECB policy statement in early June when it announced a cut in rates and introduced penalties on the deposits of commercial banks held with itself (so-called negative interest rates). It is also now offering commercial banks special subsidised lines of credit provided these loans are directed to fostering economic growth. At the same time, the BOJ has been injecting funds directly into the equity market through purchases of Exchange Traded Funds (ETFs), in addition to swallowing every Japanese Government Bond in sight.

**Inflationary fears are indeed occurring, though in financial assets.** The early adopters of Quantitative Easing (QE) have seen strong equity markets and significant lifts in residential property prices while a basket of daily purchases has typically been rising by 1.5 to 2% pa. There may be some tightening of the labour markets as unemployment diminishes but thus far, pricing power has been remarkably subdued. This leads one to possible concerns about the **unintended consequences** of QE.

The most intriguing distortion is the low cost at which 'non-investment' quality US corporations can now raise money versus their investment grade peers. Having peaked at 12% during the GFC, these low rated corporations are now able to raise 4-5 year bonds at 3.5% pa versus the 2% being paid by higher quality companies. This is the **lowest rate and spread** for at least the last 25 years and in fact **well-below the average rate paid by the US government for 10 year bonds of 5.0% over the last 100 years**![1] (There is no need to remind readers of the tax gathering capacity of governments.) As one might expect there has been a surge in issuance (a fivefold rise) compared to levels at the turn of this century, currently running at an annual rate of $237 billion and accounting for more than half of all US corporate issuance.

This cheap funding in turn is **facilitating an increase of merger and acquisitions and share buybacks**. The latter is running at around 2.3% of the capitalisation of the US stock market, which is currently US$17 trillion, while merger and acquisition (M&A) activity is withdrawing a further 2%. M&A is still relatively subdued but likely to accelerate strongly on the back of growing confidence, cheap money and the normal pattern of rising interest rates. Historically share swaps accounted for around 35% of these M&A deals but cheap money has tilted the equation to favour debt funding. We can therefore expect relatively tight share supply as we await the traditional lift in IPOs. The combination of high levels of profitability across the major economies and low borrowing costs has resulted **in interest cover being at least twice the levels of the 1990s**. Overall net debt levels, expressed as a percentage of book value, are well-down compared to the last 25 years at around 50% for the US, Europe and Japan, and under 40% for the rest of Asia.

Our conclusion is that there is **no immediate concern about funding risks** in markets and if anything, one should prepare for an acceleration of corporate activity and a late surge in low quality bond issuance as interest rates begin to move upwards. There will need to be a marked lift in capital expenditure and/or a drop in profits to change what has essentially been a **deleveraging of balance sheets** across Asia and North America, while Western Europe has seen leverage undulating between 55% and 65%.

Combine reasonable balance sheets and a trend of increasing profits, a shrinking quantity of shares outstanding, for now at least, and one can be reasonably optimistic about markets. **It is critical though that with valuations at the upper band of historic limits, earnings must meet current expectations.** There are enough uncertainties on both the geopolitical and economic front to argue that cheap money is creating a Panglossian world. Rates are likely to gradually change direction and growth in Europe is still fragile but we can also identify exciting **reform-driven change in the world's two most populous economies**, China and India.

Last quarter we wrote about the likely victory by Modi in the Indian national elections and it has been even more emphatic than we could have hoped. We look on eagerly to see the priority that is given to reforms. Should the headlines shrilly relate negative news about the weak monsoon rains or the loss of momentum from Delhi, we at Platinum will likely hold fast to our conviction that India can resume its growth trend of close to 8% pa. **The nation has unambiguously embraced the hope for economic reforms and a development bias over the former diet of handouts and subsidies.** While India may not have the leverage that the Chinese exploited to gain technology and foreign participation in its economy, the very institutions that precluded this will be, in all likelihood, brought to bear in transforming this market economy back to its high growth trajectory.

[1] It is conspicuous that the average modified duration of US corporate debt has risen from the 25 year average of 4.5 years to over 5.5 years since 2010, while the duration of high yield borrowers has shrunk to around 4 years.

We have addressed some of the **perils within the Chinese economy** in these quarterlies over the last few years. The fall of property prices and the abrupt arrest of residential building starts is no surprise but with the easing of lending restrictions, we believe it will be a painful period for parts of the economy rather than cause a complete loss of economic growth. There are many areas that can augment the reduction of building activity, not least the need for **State-owned Enterprise (SOE)** reforms, greater investment in the protection of the environment, as well as greater assistance in healthcare, education and other services.

The importance of the SOEs has shrunk considerably with the enactment of three earlier bouts of reforms[2]. Having accounted for over 60% of the urban workforce in 1990, they now employ less than 20%. However, SOE wages are typically 60% higher than those of the private sector at RMB52,000 pa and in addition there are other perks and very-evident opportunities for self-enrichment. While their profitability is inferior to that of private firms, it varies according to the openness of the industry. The general belief is that less protection and more accountability will lead to a more equitable society and a much improved allocation of capital and other resources. Resistance to surrendering entrenched privilege is **one of the motivations behind the intensification to the anti-corruption drive** by the ruling *junta*. This serves to both mollify the general public as well as to bring extreme pressure on the upper echelons of the SOEs to change.

## Outlook

We remain optimistic and are shifting the weight of the portfolio to the East.

Growth in the Western hemisphere is gaining impetus and higher share prices can co-exist with higher rates on account of dissipating economic risks. For now, inflation and credit markets risks appear subdued.

The engagement of reform in the world's two most populous nations underpins our belief in the durability of global growth. That there will be setbacks is likely but in the case of China, the domestic stock market has been in a severe downward trend for over six years and valuations are almost half of those in the Western hemisphere for an economy that is growing twice as fast! Other markets in Asia are equally interesting and we are finding companies we want to own.

[2] There are some 147,000 non-financial SOEs in China employing about 70 million urban workers. They have assets of about US$15 trillion and these generate profits of about US$400 billion. There number incorporates a plethora of small provincial as well as prefecture and county enterprises. Apart from stripping away protection and privilege, the reforms aim to introduce more rational industry structures (consolidation), to make way for more private sector participation and to change to partial or full private ownership through stock market listings. Already some of the leading SOEs are experimenting with stock options for the staff. Of the 2500 companies listed on the 'A' share market, 980 are SOEs.

# Platinum Unhedged Fund

**Clay Smolinski** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| North America | 28% | 28% |
| Japan | 22% | 23% |
| Europe | 20% | 18% |
| Asia | 18% | 19% |
| Australia | 3% | 2% |
| South America | 1% | 2% |
| Africa | 1% | 1% |
| Russia | 2% | 1% |
| Cash | 5% | 6% |

Source: Platinum. Refer to Note 3, page 40.

## Performance and Changes to the Portfolio

**(compound pa, to 30 June 2014)**

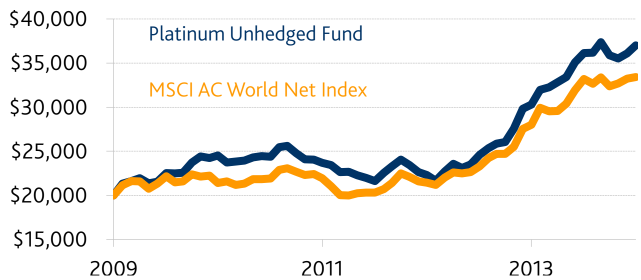
| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Unhedged Fund | 3% | 22% | 16% | 13% | 11% |
| MSCI AC World Index | 3% | 19% | 15% | 11% | 5% |

Source: Platinum and MSCI. Refer to Note 1, page 40.

The standout performers over the quarter were the Fund's Indian holdings, as the market rejoiced in the majority victory of the Bharatiya Janata Party (BJP) and its pro-business leader Narendra Modi. Our Indian stocks are concentrated in property and infrastructure, a sector that had gotten extremely cheap as projects went into gridlock post several corruption scandals. The likes of Housing Development & Infrastructure (+81%) and Jaiprakash Associates (+46%) have rallied in the hope that activity will restart again under the new government.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

## Commentary

The recent sell-off in the global Internet names gave us an opportunity to take a closer look at some of the truly unique business models in the sector. Facebook is a good example. There are few consumer companies who control a product that is used by 1.2 billion people on a weekly basis.

In the space we are particularly interested in the companies that have built a global user base, have a defensible business model and are just getting started monetising their service. When you have this combination, a high starting valuation doesn't necessarily preclude them from being interesting investments. A company that meets these criteria is **LinkedIn**.

Readers who have changed jobs over the last five years will likely be familiar with LinkedIn. The LinkedIn profile has become the default on-line CV and the site is a good place to both search for a job and attract the attention of employers. From its roots in recruitment, the site is evolving towards becoming a platform to showcase your professional brand and a place to curate, consume and share professional content – an acceptable social platform to be logged on during work hours!

A key asset of the company is the ***quality*** of data it has on its users. Via filling out your profile you will typically provide your real name, current title, work history and educational background. This is extremely valuable information in determining aspects like your salary, age, and professional interests. Importantly, unlike a brand I may have 'liked' on Facebook a year ago, these are data points that are likely to hold their ***relevancy over time.*** Combined with our attractive user demographic (usually the wealthier slice of the population), you can see why this database is attractive to advertisers and companies alike.

The quality of the database is evident when you consider where LinkedIn is making its revenue today. Unlike the other social networks, LinkedIn is not purely an advertising driven model. In fact 75% of revenue comes from database software products sold to corporates. The value of a global database of professional identities is obvious to those looking to hire or those involved in sales trying to find the right contacts to speak to.

A historical weakness of LinkedIn has been user engagement. Indeed early adopters will likely remember the site being fairly bare - after filling out your profile you might answer the odd connection request, check out who's been viewing your profile and not much more. Like many Internet companies the management is working hard to make a visit to LinkedIn part of a user's daily routine.

Users can now follow their favourite news sources (i.e. ***The Economist***), or track what their favourite business luminaries are saying via the LinkedIn Influencers program. A further extension has been the decision to give individual users the ability to write their own blog posts, which will appear on their profile. In a similar vein to twitter, users who are posting articles can be 'followed' allowing you to keep track of what interesting folks are writing without needing to formally connect. These features combine to allow one to design an interesting daily news feed and give one another reason to sign in.

The company has now achieved global scale. LinkedIn has over 300 million accounts in total and new users are joining at a rate of 8 million per month. Similar to Facebook, LinkedIn has tended to displace local competitors over time and it is now clearly the dominant professional network globally, holding leadership positions in every major market outside of Germany and China.

LinkedIn currently has a market cap of $20 billion, and the Fund did some good buying at the crescendo of the recent sell-off to build a starting position. However, with the company expecting to earn $2.2 billion in revenue this year, it is important for it to continue to improve engagement to fully monetise its three revenue streams.

There are a few factors supporting future revenue growth. Firstly, two of their major product categories, the database software subscription targeting sales reps and the 'sponsored update' advertising product, are still in their infancy in terms of roll out. Secondly, as the customer base is global, the end markets are huge. Finally, LinkedIn has what we would describe as a contributory or 'user generated' database business. These businesses, where companies effectively collect data from users for free and resell it, tend to be highly profitable once revenue scales.

## Outlook

The Western stock markets have re-rated, with valuations in Europe at their long-term average and the US a touch higher. However, these valuations need to be viewed through the prism of very low interest rates. European investors with the choice of earning 1% on a 12 month term deposit or buying a stock on a 7% earning yield (which is paying a 3% dividend) are increasingly choosing the stock!

As Kerr mentions in his International Fund quarterly report, given the progress of reforms and the cheap valuations on offer, the Fund is currently devoting time assessing a number of ideas in China.

Clay Smolinski was appointed portfolio manager of the Platinum Unhedged Fund during the quarter. Clay has worked at Platinum for eight years and is the manager of the Platinum European Fund.

# Platinum Asia Fund

**Andrew Clifford** Portfolio Manager

**Joseph Lai** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| China (Listed Ex PRC) | 24% | 24% |
| China (Listed PRC) | 6% | 6% |
| Hong Kong | 2% | 1% |
| Taiwan | 1% | 2% |
| **Greater China Total** | **33%** | **33%** |
| India | 20% | 18% |
| Korea | 15% | 16% |
| Thailand | 9% | 9% |
| Phillipines | 6% | 6% |
| Malaysia | 4% | 5% |
| Singapore | 4% | 4% |
| Vietnam | 2% | 2% |
| Indonesia | 2% | 1% |
| Cash | 5% | 6% |
| Shorts | 0% | 0% |

Source: Platinum. Refer to Note 3, page 40.

## Performance

**(compound pa, to 30 June 2014)**

| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Asia Fund | 6% | 17% | 12% | 9% | 16% |
| MSCI AC Asia Jp Index | 5% | 13% | 8% | 8% | 10% |

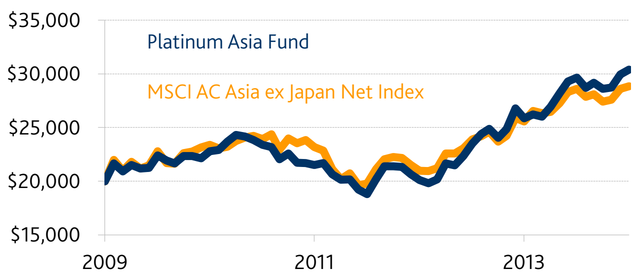
Source: Platinum and MSCI. Refer to Note 1, page 40.

Over the quarter, the Indian market was the outstanding performer (up 13%) although the Chinese markets were weak. Both the Chinese A-share market (flat) and H-share market (up 2%) were weak performers as the Chinese property market weakened under tight mortgage policies. The Thai market was up 7%, as a series of backed-up infrastructure projects were greenlighted. Elsewhere, the Asian markets were little changed.

The Fund's performance at 6.2% was ahead of the market. In local currency terms, Asian markets returned 5.8% for the quarter.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

The Fund's Indian holdings contributed the most to the rise in performance. Unitech (properties) was up 120%, IRB Infrastructure (toll roads) up 100%, Housing Development (properties) up 56% and Sobha Developers (properties) up 38%. The Fund's holding of SK Hynix (semiconductors), jumped 75%, as the industry enjoyed better pricing and greater capital discipline. Not surprisingly, the biggest drag on performance were the Chinese investments.

## Changes to the Portfolio

The Fund remains fully invested at 95%. We started buying Weichai Power, China's dominant heavy duty truck engine manufacturer. With a 30% market share, it is well-placed to exploit the expanding forklift and logistics services sectors which are showing strong growth. At 7 times price earnings, the shares more than discount mid-cycle pricing power.

China Pacific Insurance, based in Shanghai, was also introduced. It is the third biggest life insurer in a country whose burgeoning middle class is underserved by life insurance products. The appetite for protection is increasing with rising wealth. With its 300,000 strong agency force, China Pacific is primed to capture the emerging demand. Valuation merely reflects its existing book of business and with virtually nothing assumed for the immense opportunity ahead, it's a most attractive proposition!

A position in Daum Communications was also started following the transformational merger between Daum and KakaoTalk in Korea. Post transaction, Daum's strong on-line advertising properties can leverage KakaoTalk's dominant instant messenger user base, cementing its position in the vibrant Korean mobile Internet space.

## Commentary

Since commencing economic liberalisation some 30 years ago, the Chinese economy has undergone an incredible transformation beyond the imagination of even the most optimistic pundits. Movement of cheap labour to urban centres and private sector entrepreneurship turned China into the factory of the world. Metropolises sprang up across the country driven by rapid urbanisation and income growth. Urbanisation rose to 50% of the population and the gap widened further between urban and rural incomes.

Gross domestic product grew at an average of 10% over the last 30 years. Exporting US$2.2 trillion of goods, China accounts for 12% of the world's total export market. At the same time, property market sales volume has grown at a breakneck pace of 18% pa for the last 15 years! The associated steel and cement capacities also climbed relentlessly in response to this insatiable demand.

Recent data coming out of China has been lacklustre. Much of the concern centres around China's shadow banking system which grew in excess of 30% in the last five years post the global financial crisis. Trust Products, worth around US$2 trillion was one of the major components and the recipient of disbursements were property developers and local government (related) entities. Given the boom in credit creation, the credit quality was likely suboptimal. More borrowers will default but we believe the eventuality of a debilitating systemic crisis is highly unlikely.

One has to bear in mind that the Chinese shadow banking system is implicitly or explicitly backed by the Central Government. Its balance sheet is robust with total government debt-to-GDP ratio sitting at a reasonable 50%. The country is still growing at a decent pace, lessening the debt burden over time. Further, most debt is denominated in the Renminbi, money printing is a potential policy lever.

What is important is to halt the continual accumulation of low quality lending. From this perspective, the banking regulator has strengthened the risk management process for financial institutions and encouraged the development of the more transparent corporate bond market.

The latest sign of weakness emanates from the property market. Lending controls have reduced buyer appetite. The volume of property transactions year-to-date is down 9% from a year ago. Prices in many cities are edging down, with the smaller second and third tier cities reporting more significant declines than the bustling cities of Beijing, Shanghai and Guangzhou. Instead of rushing in to buy properties, many prospective buyers are now waiting.

Despite mild easing of monetary conditions, a devaluation of the Chinese currency and incremental relaxation of the restrictive property purchase rules, property investment will become less fashionable, particularly with a large stock of near complete residential blocks.

We have often commented on the unsustainable nature of China's investment-led growth and the structural economic slowdown that can be expected out of China as the country shifts away from this growth model. We, however, urge readers to avoid premature judgement. This is now a vast, complex economy with many choices lying open to policy makers.

China is taking various steps to encourage the ***market*** to participate more in resource allocation, reducing the influence of State-owned Enterprises (SOEs) while favouring private enterprise. As the economy changes from export and investment, to consumption, the energetic market-oriented operators, responsible for the bulk of jobs created, are taking full advantage.

Importantly, at the same time, tightness in the labour market and rising productivity have pushed wages higher. Financing for consumer goods, a fuel to consumption, is merely a fraction of that of developed economies!

The locals are seeing their wages rising, job opportunities are abundant and consumer credit (car loans predominantly) are growing in significance. These newly minted aspirational consumers like to travel the world, connect to the Internet, and buy the latest brands. It is not a surprise that Chinese car sales are growing nicely at a 15% clip! (see the Platinum International Brands Fund quarterly report).

"*Reading ten thousand books is not as useful as travelling ten thousand miles*" is a renowned Chinese proverb. With increasing wealth, China has well and truly picked up the travel bug. Last year, 98 million outbound trips and 3.2 billion domestic trips were made by Chinese nationals. Modern lodging facilities, ranging from the budget to the luxurious, are springing up across the country to satisfy the voracious demand. Our Chinese hotel (China Lodging) and on-line travel websites (Ctrip and Qunar) are seeing an amazing upsurge in bookings.

The rise of China's Internet population is staggering especially considering as recently as 15 years ago, most did not even have access to fixed line telephony. Today close to half of the population, more than 500 million, have access to the Internet and this is growing even faster now thanks to the mobile Internet!

Shopping over the Internet (e-commerce), which offers superior price and range is leaving the under-developed off-line retail and logistic sector in its dust. E-commerce sales value in China is around US$295 billion a year, growing at a 40% rate, equivalent to 7.9% of total retail sales. This figure is low compared with the more mature markets (South Korea at 16% and still growing), suggesting vast potential in China. Our exposure to the key Internet properties (search, social networks and on-line video) will undoubtedly benefit.

E-commerce in China is competitive and many e-commerce players in China are building their own logistic platforms to be best-in-class in delivery. JD.com, the 'Amazon' of China, has more than 86 warehousing centres across the country, close to 1620 distribution stations and more than 214 pickup stops in 495 cities. Its competitor, Alibaba Group, is teaming up with the major express delivery companies and aims to build a super logistics network over the next 8-10 years that will eventually ensure delivery within 24 hours across the country, supporting trillions of US dollar on-line sales a year.

Logistics is important, not only in the on-line world. Consumer goods need to be transported across this vast country. The Chinese logistics sector is backward and inefficient. Logistic related costs in China represents 18% of GDP compared to below 10% for more developed peers! It is little surprise that this industry is catching up fast.

The modern logistics industry is opening up the country for consumer goods and along with it palletised transport. Over the last six years, pallet usage, still at its infancy, has grown a remarkable sixfold. Forklift sales have also taken off over the same period. Weichai Power, with its dominant truck engine business and owner of 25% of Linde (forklift), is exposed favourably to this trend.

## Outlook

China is undergoing a major transformation where significant progress is already being made. We are now entering the fourth chapter of SOE reform. Resistance is being met with a clamp-down on featherbedding and graft. Audit teams swarm over recalcitrant organisations and name-and-shame is the order of the day. The objective is to move these organisations further along the capitalist path of management independence and greater public share ownership. At the same time, over-reaching tentacles will be severed to give much more space to private entrepreneurs to offer services in hitherto restricted 'zones'. The unleashing of this energy should be not be under-estimated.

Elsewhere, the general election result has given the Indian Government an extremely strong mandate for change. We can expect to see much-needed investment in basic infrastructure and policy reforms, unleashing vast productivity improvement and economic development.

We continue to find interesting opportunities with robust growth potential and will deploy capital towards these stocks as opportunities present themselves.

# Platinum European Fund

**Clay Smolinski** Portfolio Manager

**Nik Dvornak** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| Germany | 23% | 24% |
| UK | 21% | 23% |
| France | 8% | 8% |
| Italy | 6% | 7% |
| Russia | 5% | 4% |
| US * | 4% | 1% |
| Spain | 3% | 3% |
| Austria | 3% | 3% |
| Switzerland | 2% | 2% |
| Sweden | 1% | 1% |
| Netherlands | 1% | 1% |
| Turkey | 1% | 1% |
| Belgium | 1% | 1% |
| Cash | 21% | 21% |
| Shorts | 2% | 2% |

*Stocks listed in the US but predominent business is conducted in Europe

Source: Platinum. Refer to Note 3, page 40.

## Performance and Changes to the Portfolio

**(compound pa, to 30 June 2014)**

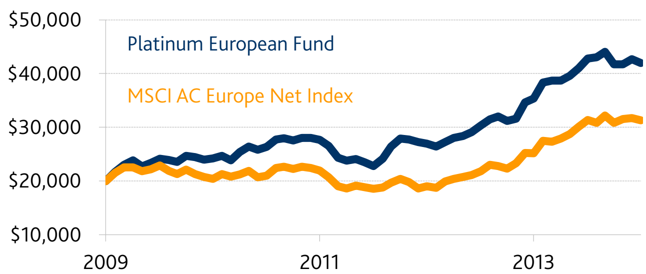
| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum European Fund | 1% | 19% | 15% | 16% | 12% |
| MSCI AC Europe Index | 2% | 24% | 13% | 9% | 2% |

Source: Platinum and MSCI. Refer to Note 1, page 40.

The Western European markets moved modestly higher over the quarter. The standout was Spain +8%, followed by Germany +4%, while the French, UK and Italian markets all rose less than 2%. The Russian market bounced 14% as the standoff between Russia, Ukraine and Europe did not continue to escalate.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

In terms of position changes, we added to our holding of Russian search engine leader, **Yandex**. We took advantage of the sharp sell-off triggered by President Putin's comments around greater state control of the Internet (which would incidentally cause greater harm to its main competitor Google). Elsewhere we participated by the IPO of **Markit**, with Nik outlining the rationale in the commentary below.

For the quarter, the Platinum European Fund returned 0.5% versus 1.6% for the MSCI Europe Index.

## Commentary

Bank regulation doesn't excite most people. Subjects like capital adequacy, liquidity coverage ratios and counterparty valuation adjustments are dry, even downright boring. Most in the investment community share these sentiments, which is precisely what attracts us to the subject.

Regulatory constraints on banks have been progressively loosened since the 1970s. This was partly a response to political pressure fuelled by bank lobbying and partly driven by a genuine belief in the free market doctrine, which held that market discipline could moderate banks' irrational tendencies. Whatever the reason, the trend was undeniably one of deregulation. This came to an abrupt halt following the 2008 financial crisis. Political winds changed as former political allies rushed to disassociate themselves from the banks. Regulators, once brought to heel, were now unleashed and have been reapplying the shackles with zeal.

Banks are reeling under the waves of new rules, sanctions, scrutiny and some truly eye-popping fines. Their position is a treacherous one. In their eagerness to appease the public, lawmakers rushed through legislation without much thought given to implementation. Regulators are scrambling to interpret the new rules and figure out how to implement them. Ultimately, this is an evolutionary process that necessitates 'learning by doing' which makes life hard for banks who find the goal posts keep shifting. Yet they get little sympathy, with compliance failures likely to attract severe punishment from regulators and capital markets alike. For once, it is not just shareholders who suffer, with senior management necks on the block too; CEOs included.

Predictably, investors see regulation in a negative light; regulation makes banking safer but less profitable. That's bad for business, right? Well, for banks, perhaps. But it should be great for business, if your business is helping banks navigate this treacherous environment. Nothing loosens a bank's purse strings quite like a risk that could get the CEO fired.

Hunting for beneficiaries of tighter regulation has yielded a mere handful of candidates, typically US-based. Europe proved fallow ground until the recent IPO of UK-based **Markit** in which we participated.

Markit is just over a decade old, founded by derivatives traders from Toronto Dominion (TD) Bank. They recognised the difficulty TD's risk managers had valuing the positions of its traders. Often risk professionals were forced to rely on the very traders they were overseeing for essential information – basically the traders were auditing themselves! This group left TD to provide i**ndependent, third-party valuations** to risk managers across Wall Street.

The core product here is a **contributory database**. Banks submit information to Markit which combines it, cleans it and then sells it back to those same banks, as well as asset managers, hedge funds and regulators the world over. A business that gets something for free only to sell it back to its providers, and many others, is an appealing investment proposition.

Originally, the business addressed a small niche within the securities market. To create a truly valuable company, they needed to expand to cover as many financial instruments and markets as possible. To this end, the founders sold 70% of the company to their largest client banks. This not only gave them the money needed to build out their business but also ensured the participation of those banks. That participation was critical in the early days because more contributors mean more accurate and reliable data which, in turn, attracted new users and contributors.

With ever greater oversight high on the agenda, bank boards, risk managers and regulators are finding Markit's data indispensable. It is **emerging as the de facto standard** for valuing a broad range of financial instruments. This not only underwrites the strong demand for this product but creates a powerful lock on customers. If the regulator and every other bank use this data, no risk manager is going to go out on a limb and start using something else. Today this business generates half a billion dollars of revenue per year and growing, albeit modestly. Not bad for a company just entering its second decade.

Yet management haven't been idle. Being a trusted provider to, and majority-owned by the banks puts Markit in a unique position to identify new problems that they can help solve. In 2007, they established a **second leg** to their business: an electronic **platform that processes so-called 'over-the-counter' derivatives transactions** which account for the bulk of derivatives trades. Today, this segment brings in a further quarter of a billion dollars per year, serving those same bank customers, helping them reduce operational risk and stay on the right side of regulators.

The third and **final leg** to this company is a 'solutions' business, the most interesting facet of which is a database Markit is building to **help banks comply with onerous 'Know Your Customer' rules**. This issue is especially pressing because US prosecutors are now applying a much tougher standard than the rest of the world. As *The Economist* recently put it, it's no longer enough to merely know your own clients. You're now expected to know your clients' clients! The cost of doing so is hefty. The ten largest banks, between them, spend over a billion dollars a year on this effort. Yet failure is more costly still, with French bank BNP reportedly facing a staggering $10 billion fine.

There is **undeniable commercial logic** to having a third-party build and maintain this sort of database, with banks paying to access this data, **rather than each building its own**. Banks are desperately looking for someone to fill that role and Markit is endeavouring to assume it. Should it emerge as the provider of choice, the rewards will be significant. The 'solutions' business already brings in a quarter of a billion in annual revenue and grows 20% pa. This new venture could underwrite that sort of growth for years to come.

IPOs are typically not our cup of tea. They usually constitute sales by well-informed insiders looking to get out. This one was different because the sellers were the banks, probably motivated by regulatory concerns around conflicts of interest. <u>The founders and senior management chose not to sell their shares</u>. They will stay and grow this business with the bulk of their capital invested alongside shareholders.

At 18.5 times earnings, this company is not a steal although it is cheaper than similar businesses which trade at P/E multiples well over 20 times. The lower multiple reflects **investor concern** over a regulatory **push to have derivatives trades centrally cleared**, which will hurt Markit's business to a degree. This concerns us too, especially since we aren't exactly buying this company on the cheap. Yet the time frame and extent to which this happens will give this entrepreneurial management team plenty of time to nurture its new ventures to fruition and use its unique relationship with banks to discover new avenues for growth. With the theme of re-regulation in full swing there is unlikely to be any shortage of such opportunities. Rather the shortage is of listed companies that are well-positioned to capitalise on these opportunities and management teams that can develop them.

## Outlook

We are relatively sanguine about the outlook for Europe.

While the market is trading at roughly fair value, asset prices will continue to be supported by very low interest rates and the European Central Bank gradually increasing its efforts to stimulate the economy. This can be seen in the recent ramp up in merger and acquisition activity in Europe as corporates, aided by very cheap money, increasingly realise it is cheaper to buy rather than build.

We will continue to use our cash balance to take advantage of any periodic set-backs in stock prices.

Nik Dvornak has joined Clay Smolinski as co-manager of the Platinum European Fund. Nik has covered financials over the past seven years at Platinum.

# Platinum Japan Fund

**Jacob Mitchell** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| Japan | 90% | 88% |
| Korea | 7% | 7% |
| Cash | 3% | 5% |
| Shorts | 5% | 5% |

The Fund also has a 12% short position in Japanese Government Bonds.

Source: Platinum. Refer to Note 3, page 40.

## Portfolio Position

Changes in the quarterly long portfolio composition:

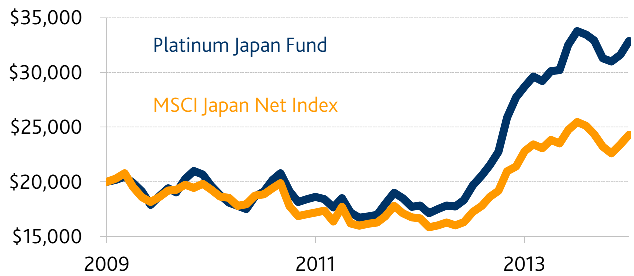
### Sector Breakdown

| SECTOR | JUN 2014 | MAR 2014 |
|---|---|---|
| DOMESTIC | 50% | 52% |
| Consumer and Retail | 13% | 14% |
| Financials | 12% | 12% |
| Healthcare | 9% | 10% |
| Services | 7% | 7% |
| Telco and Utilities | 6% | 6% |
| Property and Construction | 3% | 3% |
| EXPORT | 47% | 43% |
| Tech/Capital Equipment | 19% | 22% |
| Durables | 17% | 15% |
| Commodities | 11% | 6% |
| Gross Long | 97% | 95% |

Source: Platinum

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

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

Whilst we build the portfolio one idea at a time, some themes that are represented prominently within the Fund include:

- Emergent industrials with leading global positions.
- Corporate revitalisation, industry reorganisation and potential merger and acquisition targets.
- Potential policy change beneficiaries (e.g. industry deregulation, labour market reform, tax reform, new business incubation incentives).
- Internet 2.0 and service sector growth opportunities.
- Emergent energy management opportunities (smart cities/grids/buildings).
- Cheap real asset exposures that domestic investors are likely to seek as inflation hedges.

## Performance

**(compound pa, to 30 June 2014)**

| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Japan Fund | 5% | 14% | 21% | 10% | 14% |
| MSCI AC Japan Index | 5% | 7% | 12% | 4% | 0% |

Source: Platinum and MSCI. Refer to Note 1, page 40.

The Japanese market remains range-bound, significantly underperforming global markets over both the short and longer-term with the heady outperformance of late 2012, early 2013 fading. Early in the quarter the impact of the consumption tax weighed on investor sentiment. However, as evidence that end-demand was normalising, the market, especially the domestic exposed consumption sectors (retail, financials and property) rebounded. We find it interesting that locals turned into buyers throughout the weakness, evidence of growing belief in the recovery. Anecdotally, the market is rewarding companies that are showing greater respect for capital allocation; this is more of a factor for outperformance than growth per se.

Key performance contributors included our more recent purchases (Sumitomo Metal Mining and Inpex; severely beaten down cyclicals with fortunes changing for the better; detailed below), large holdings such as Nippon Telegraph and Telephone (update below), Panasonic and Rohm, and mid-sized exporters such as TopCon and Glory. The major detractor from performance was DeNA. Having reviewed the original thesis that the company would ultimately navigate the transition from feature to smartphone gaming, we see no reason to alter course even though near-term earnings have disappointed.

Shorts and currency positions had negligible impact on performance.

## Changes to the Portfolio

We sold out of Ryohin Keikaku as the valuation started to price in some relatively enthusiastic expectations of overseas growth. The company's Muji-Rushi (literally "no-brand") retail format offers a unique minimalist design ethos across a broad range of high quality household furniture, apparel and food items at reasonable prices (think kikki.K/IKEA with a Japanese flavour). Over the past three years, the stock price has close to tripled as the company delivered on promises to ramp up its international store rollout and reinvigorate the product offering. However, we see growth pangs emerging as the development of its internal supply chain lags the Asian store expansion. Whilst the longer term story remains a good one, the valuation no longer affords a real margin of safety.

Last quarter we alluded to opportunities of a more cyclical nature that were moving onto our radar; of the three stocks we acquired, we'll detail Inpex and Sumitomo Metal Mining, leaving Nippon Electric Glass for another day.

Our investment in **Inpex** is based on a scenario analysis around the development of the massive $34 billion Ichthys 8.4 mt LNG/condensate project (Browse Basin, Timor Sea, located approximately 820 km west of Darwin). Single project risk is high with Ichthys representing 60% of likely future production value and by any estimate this is an audacious project. Further, the inability of seasoned campaigners such as Shell, Chevron etc to deliver a North West Shelf project on time and on budget has led most to conclude that Inpex will suffer a similar fate. However, even under a scenario of a +45% capital spending over-run (i.e. the Gorgon experience) and a three year delay, we still have a margin of safety afforded by the valuation. Further, we think this scenario is avoidable given the combination of high fixed-price construction contract cover, a falling Australian dollar and easing contractor rates.

Even though the project is now 50% complete and currently on budget with first gas expected in late 2016, given the propensity for most cost issues to arise in the final stages, a discussion around valuation is best framed by way of scenario analysis. Our entry price and a 15% cost over-run equates to a March 2019 P/E of around 5 times and cash-flow yield of 26%. Whilst a cost and time overrun at Ichthys would seem inevitable, what could really hurt this investment, is the failure of a major component/system which impacts the critical path to production. Accordingly, though the current price provides a large margin of error, the only way to account for this tail-risk is to maintain a commensurate position size. Furthermore, we wouldn't want to promote the attractiveness of Inpex in isolation given the general neglect around oil stocks globally, combined with what appears to be a generally tight oil market given the likelihood of ongoing Middle Eastern production disruptions.

The second cyclical **Sumitomo Metal Mining** is based on our bullish outlook for nickel. The origins of this idea are to be found in a piece of Indonesian legislation dating back to 2009 when the government passed a law to ban all exports of unrefined nickel ore by early 2014. Its goal was to encourage investment in the local smelting/refining industry (unrefined ore sells for $20-$100/tonne versus refined nickel at a current price of around $19,000/tonne). The interesting aspect of this was that many industry participants assumed the law would never be enacted and the Chinese proceeded to create some 7mt of stainless steel capacity fed by Indonesian nickel ore exports. However, as testament to Indonesia's growing reform and good governance credentials, the export ban is holding (and there's a net financial benefit to Indonesia if this continues). China represents 50% of 40mt of global stainless production and the Indonesian export ban has left a third of this Chinese capacity short nickel without a medium-term replacement. That's clearly bullish for the nickel price and the primary reason behind the recent rise in the metal.

Sumitomo Metal Mining offers exposure to 56,000 tonnes of refined nickel production and we estimate a 25% move in the nickel price would result in a 50% rise in after-tax profits. The company has used its processing technology where it is acknowledged as one of two global leaders in HPAL (High Pressure Acid Leach for processing low grade laterite ores) to negotiate decent equity positions in nickel producers such as Nickel Asia (Philippines) and Vale Inco (Indonesia). The company has a good long-term record. Importantly, it has not overpaid for assets during the commodities boom, instead growing via organic mine development and opportunistic acquisitions.

Overriding concerns about the sustainability of Chinese investment and related commodity issues allowed us to acquire a holding at less than book. We acknowledge that the investment intensity of Chinese growth must fall and with Chinese construction directly accounting for some 10% of nickel use, demand will likely disappoint. However, the market is not paying sufficient heed to the emerging Indonesian supply-side shock with the high likelihood of a long-term structural shortage supporting a much higher clearing price for nickel.

## Commentary and Outlook

As we have stated in the past, the reforms most likely to succeed in Japan are those of a Trojan Horse nature. We see this in government and institutional support of the new Return on Equity (RoE), growth and governance based JPX-Nikkei 400 Index, with corporates now using the shame of omission as grounds for better capital management. For example, serial capital hoarder and machine tool maker Amada's decision to target a 100% pay out of profits via dividends and buybacks to lift RoE, was specifically made so as to qualify for index inclusion. At one level it's a little sad that common sense behaviour requires an institutional imperative, though we are not complaining.

The other Trojan Horse can be found in the clear political support lent to GPIF's ($1.3 trillion government pension manager) reform process. Behind the guise of some erudite academic thought pieces, a very simple consensus has coalesced. That is, with the Bank of Japan (BOJ) now committed to a hard inflation target, it makes logical sense for the national pension fund to cut exposure to nominal assets such as bonds. Whilst details are still hazy (not surprising given the market sensitive nature of such a large asset allocation decision), GPIF's current 60% allocation to domestic bonds is likely to fall to around 40% in preference for domestic equities and foreign assets. The government clearly believes domestic asset price wealth effects, and the likely Yen weakness that should result from GPIF's offshore portfolio shift, are important to achieving its reflationary goals.

Whilst we see these top-down changes as important, what is more encouraging is renewal at the corporate level e.g. Panasonic, Asahi Group, Takeda, Hitachi, Mitsubishi Heavy, and Nippon Telegraph and Telephone (NTT). In the case of NTT, whilst the market is celebrating the now obvious commitment to earnings targets and capital efficiency (with 100% of free cash flow now channelled into dividends and buybacks), the surprising news for us was the company's plan to move its fibre (broadband/fixed line) business to a wholesale structure. Pricing details will be announced next quarter. It is impressive that NTT is proposing to effectively self-regulate by cutting interconnect and converting this to a wholesale deal for resellers before the regulator forces some other deal on them. Simplistically this allows NTT to focus on cutting infrastructure headcount/costs and leaves others to fight it out at the retail level, discourages KDDI from becoming too aggressive in its own fibre rollout and realistically shuts the door on any other competition. So assuming NTT gets the wholesale pricing right, it will have DoCoMo, Softbank, electronic retailers etc all selling the service to the 24 million households that are yet to take it. On pricing, a balancing act is required; cut it enough to get resellers interested but not so far that these resellers can eat into our existing 18 million sub core. NTT can bundle cable TV and other services to keep the core loyal. From an NTT perspective, any move that accelerates take-up of the fibre network and brings forward the date that the copper network is shut down, is good news.

In summary, NTT is just one example of the sensible and somewhat overdue reforms that are taking place across a range of Japanese companies. These reforms ultimately underpin our generally optimistic view of the portfolio.

# Platinum International Brands Fund

**Simon Trevett** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| Europe | 30% | 34% |
| Asia and Other | 26% | 26% |
| North America | 9% | 10% |
| Latin America | 7% | 7% |
| Japan | 5% | 5% |
| Russia | 3% | 3% |
| Africa | 2% | 2% |
| Cash | 18% | 13% |
| Shorts | 6% | 6% |

Source: Platinum. Refer to Note 3, page 40.

## Performance and Changes to the Portfolio

**(compound pa, to 30 June 2014)**

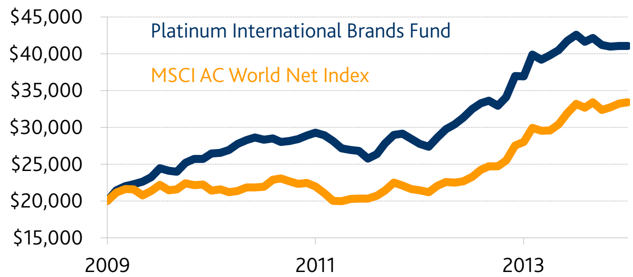
| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Int'l Brands Fund | 0% | 11% | 12% | 15% | 13% |
| MSCI AC World Index | 3% | 19% | 15% | 11% | 0% |

Source: Platinum and MSCI. Refer to Note 1, page 40.

The Fund's short positions and a relatively higher exposure to emerging markets were the key detractors from the quarter's performance. India's Nifty Index, one of the world's best-performing markets, has risen 13% over the period on optimism surrounding the change in government. Although there is much that can be done by this new government, with good cause for long-term enthusiasm, the Fund has taken a more cautious view and maintained the short position. In Germany, the cost of maintaining the short position was not recovered by the performance of the underlying holdings.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

There were mixed outcomes in the quarter across the stocks; the UK stocks tending to detract from performance as interest rates start to rise, while patches of positive performance showed through in some of the weaker emerging markets. On a distinctly more positive note, the more recent additions to the Fund in the jewellery sector such as Tiffany and Gemfields, both showed signs of early and encouraging performance. The Fund has confidence that this theme will endure for a number of years and has continued to add to these holdings as well as to the leading Chinese jeweller, Chow Tai Fook. Likewise, previous reports have noted the Fund's interest in tourism and those investments have also shown good short-term performance.

## Commentary

The financial market's commentary on the state of the Chinese consumer and their willingness to lift consumption has not been encouraging over the past year, especially in the more indulgent and luxury categories. Clearly much of this has been linked to the anti-corruption purge and restrictions on largesse being pursued by the central administration. The more positive commentary from some of the Fund's investments might therefore initially appear at odds or contradictory to the somewhat negative perceptions of the economy.

Chow Tai Fook reported revenue and profit growth of over 30% for the past year with an even higher growth in mainland China. We certainly wouldn't expect that to continue unabated, although it does serve to illustrate the potential in a market that's currently considered suppressed or subdued and certainly out-of-favour with the investment community.

Chow Tai Fook continues to add to their store base of more than 2000 outlets at the rate of about 10% a year and we would expect an increase above that in the overall revenue of the company. Perhaps more encouraging is the growth in gem-set jewellery, at potentially much higher margins and in particular the development of diamond jewellery. It was therefore encouraging to see Chow Tai Fook acquire the US diamond jeweller " Heart of Fire" and hence the opportunity to more quickly develop their focus on higher value diamond products, especially the premium bridal collections. Our discussions with various diamond miners across the world have been encouraging and confirm that the Chinese consumer clearly has the potential to overwhelm a limited supply in the years to come.

Readers may chose to dismiss the Chow Tai Fook commentary as perhaps an isolated example and not particularly representative of the underlying dynamics of the Chinese consumer economy. It may not be intuitive given the overall economic commentary, however, the Fund is finding a number of opportunities and examples of healthy growth at prices that seem to reflect the investment community's apparent disinterest.

The Fund has continued with its investment in BMW and also in their Chinese JV partner Brilliance. This may not have seemed such a wise choice with reports that wealthier consumers are suffering from greater government scrutiny, weaker property markets, credit restrictions and new car licence restrictions in the major cities. Nonetheless, the Chinese car market has continued to grow in excess of 10% pa, faster than the economy and within that, the luxury car makers have significantly outperformed the domestic producers.

Might this be explained by the ability of the luxury German producers to utilise their balance sheet? In an environment where credit has been increasingly difficult to obtain, they have extended credit to their dealer network to stock the showrooms and incentivised the sales staff to offer credit to prospective customers. The local producers and dealer networks are less able to do this without the benefit of strong (offshore) balance sheets, having mostly relied upon the Chinese banks and financial system.

A young employed male consumer might be faced with some interesting choices. Is he to save for longer to contend with the daunting prices of apartments or instead consider the purchase of a vehicle in his attempts to distinguish himself as he contends with the difficulties of being outnumbered in the pursuit of a partner?

If he were to look at one of the local brands then most likely he would be required to fund the entire purchase price in cash. Alternatively, his cash could be used for a deposit on a BMW with credit obtained at zero interest. BMW dealers are reporting between 50 and 70% of sales made on credit, and a year-to-date increase in sales of over 25%. Perhaps it's not so difficult to imagine that despite the headlines there is still a growing and vibrant consumer economy with enormous opportunity. We trust our exemplar young man also retained sufficient funds for a diamond ring!

As regular readers would know, there's always been an inherent reluctance on our part to add commentary to the major press topics of the day. So to pose a question such as "Who is the greatest footballer of all time?" might appear out of place. We are grateful to Mr John Clemmow of Barclays for posing just that question and found his commentary to be not only timely but also especially relevant to the current positioning of the Fund. With his permission we would highlight a couple of key points.

The answer it seems depends on your age! As does your answer to many similar questions about your 'favourites'; movies, authors, film stars. Many would likely agree that their preference in music is quite different from that of their parents and hopefully their teenagers! In psychology terms, Mr Clemmow explains there's something called "reminiscence bump" and it's the reason your favourites are often from your youth. It's when your mind is at its most efficient and the creation of memories the strongest. The magic number appears to be 17! That's the age when the strongest impressions were made on you. If you were born between 1966 and 1975 the researchers found that Maradona was favoured, whereas Pele was the favourite for those born between 1946 and 1955.

Is this really just about reliving impressionable teenage memories? The world's population of adolescents and youth is at an all time high! The advertising and consumer goods industry understand very well the future benefits to be reaped from building those strong associations and identification with particular products and brands. Building the trust, perceptions and memories, adapting to and reinforcing each generation's identity is the underpinning of the successful companies. It's applicable not just to those brands associated with aspirational 'success' but also the everyday local brands that a generation grows up with; it is the equivalent Vegemite and Coke of the current youthful generation across the globe that we seek as investments for the future. It is also the reason, along with price, that the Fund has a significant interest in the youthful emerging and developing economies.

## Outlook

The Fund has continued to add to positions in emerging markets as volatility and falling share prices provide longer term opportunity. On a shorter term basis there are encouraging signs of interest in some markets and investments that have more recently subdued the Fund's performance.

As noted in the commentary, the Fund's Chinese consumer-related investments have started to perform well. There's good reason to be encouraged about the changes underway in India, the Fund's Russian and Brazilian holdings are recovering, while Europe, with some of the Fund's larger investments, continues to repair and rebuild their economies.

# Platinum International Health Care Fund

**Bianca Ogden** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| Europe | 46% | 45% |
| North America | 25% | 23% |
| Japan | 6% | 6% |
| South America | 1% | 1% |
| Australia | 1% | 1% |
| Cash | 21% | 24% |
| Shorts | 0% | 2% |

Source: Platinum. Refer to Note 3, page 40.

## Performance and Changes to the Portfolio

**(compound pa, to 30 June 2014)**

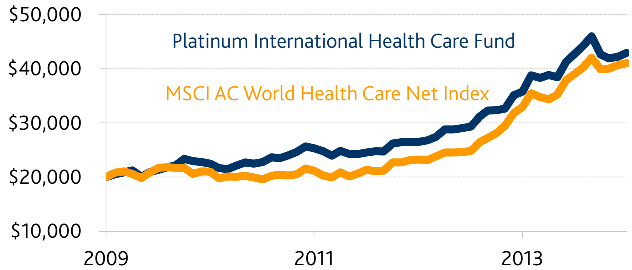
| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Int'l HC Fund | 1% | 20% | 19% | 16% | 8% |
| MSCI AC World HC Index | 3% | 25% | 25% | 15% | 7% |

Source: Platinum and MSCI. Refer to Note 1, page 40.

Corporate activity in healthcare continues unabated. Novartis sold its vaccine business and set-up a consumer joint venture with GSK, before offloading its animal business to Eli Lilly. This deal also allowed Novartis to add GSK's oncology products to its own portfolio. Novartis can now focus on its strengths, namely drug development, eye disease and biosimilars.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

During the quarter, Pfizer was unsuccessful in acquiring AstraZeneca (up 12% for the quarter), while AbbVie failed to convince Shire (up 55% for the quarter) to enter its fold. Europe is truly back in focus and we believe these companies are correct in defending their independence, particularly as they have worked so hard to get their business fundamentals right.

Our other European holdings also had positive news; Actelion (up 34% during the quarter) reported good mortality results for Selexipag, an oral prostacyclin receptor agonist tested for the treatment of pulmonary arterial hypertension (PAH). Actelion, a company that was heavily criticised for its research and development (R&D) spend not long ago, is now thriving. Recent data on Selexipag confirms Actelion will be able to defend its lead position in PAH.

Rare disease company, Swedish Orphan Biovitrum (up 25% during the quarter), received approval for its longer-acting haemophilia A drug and together with Biogen Idec, is now ready to shake-up the haemophilia market.

During the quarter we added to our rare disease holdings as well as to other biotech holdings. At the same time, we closed our biotech index short that finally made us some money.

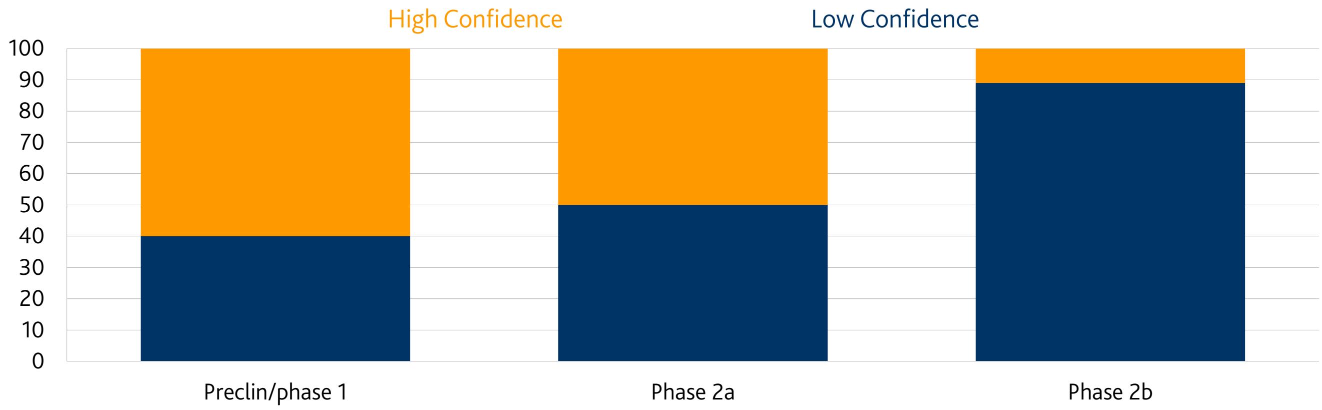
## Commentary

**AstraZeneca**

The journey of AstraZeneca is interesting. For several years it has had the worst of times; continuous pipeline failure, restructure after restructure, looming patent expirations and a leadership team that was too marketing orientated and reverted to short-term financial fixes. The inevitable happened; a new Chairman was recruited and the entire senior management team replaced. The new team was able to turn the company around and steer it on a more effective course; building up a solid drug research portfolio and boosting innovation. AstraZeneca indeed had some good building blocks: Medimmune (the biologics division of the company), diabetes (AstraZeneca now has full control over its diabetes franchise), a good Japanese business, solid respiratory franchise and solid cash (once it stopped its buybacks). However, it also had a big worry; a research and development engine that had a spectacular failure rate. The engine was defunct and its scientific curiosity almost extinguished. A detailed analysis of their failures revealed some remarkable insights and confirmed what we thought went wrong.

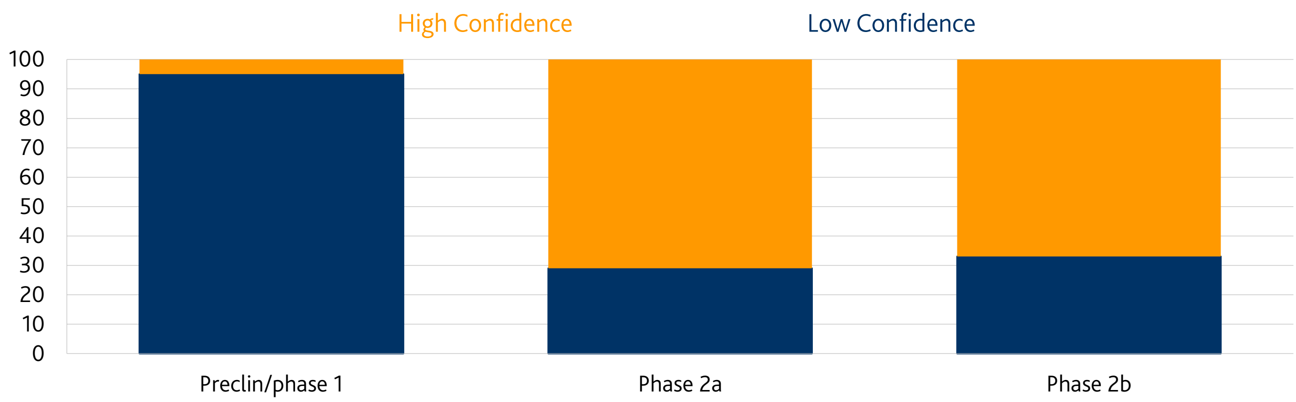
The never-ending string of pipeline failures stifled decision-making, fostering a culture of minimal risk taking. Projects either got stuck or were moved ahead for the wrong reasons. Focus was on 'volume' i.e. moving projects through to the next stage of development. This distorted decision-making process hampered the pursuit of the best therapeutic approach to diseases. As an example, at one stage about half of AstraZeneca's portfolio was made up of backups, some not

**Right Target in Right Patient (%, 2005-2010)**




Source: Nature Reviews Drug Discovery Volume 13, pages 419-431 (2014)

**Perceived Commercial Value (%, 2005-2010)**




Source: Nature Reviews Drug Discovery Volume 13, pages 419-431 (2014)

even structurally diverse enough to actually mitigate development risk. All that mattered (which provided management comfort) was that the drugs progressed through the development cycle and consequently fulfilled the volume-based goals.

Quality did not rate high on their agenda and at times pre-clinical safety signals were ignored. This carelessness would later cause the failure of projects in mid-stage clinical development. Commercial attractiveness was often used as justification for moving ahead, despite a lack of detailed target knowledge, understanding of drug/target interaction dynamics or a solid understanding of the underlying disease pathology. Even more concerning was the fact that often the confidence in the disease target declined as the drug moved through development (see graph page 26). Yet as the project progressed, commercial confidence miraculously increased (see graph above). About three quarters of projects from 2005-2010 failed due to lack of efficacy.

It was clear that AstraZeneca had to make drastic changes if it was to improve its output. Indeed it did exactly that. Through this review it established the '5R' framework. On top of that, the new CEO Pascal Soriot, supplied the urgency and vigour needed to make the changes. Today the mantra is the right target, tissue, safety, patient and commercial potential. To successfully implement the '5Rs', they brought 'science' back into sharp focus and abolished the preoccupation with project volumes. Sharpening the company's strategic focus fosters a 'truth seeking' mentality that encourages its scientists to go out and engage with the leaders in their field and to ask, as they put it, the 'killer questions'.

As part of its engine upgrade, the pipeline was overhauled and only projects that complied with the '5R' mantra remained active. AstraZeneca has put science at the heart of target decisions. It has established: significant biomarker and personalised medicine capabilities (the right patient: 85% of projects now include a personalised healthcare strategy), better pharmacological modelling capabilities (right tissue, right drug/target engagement) and dialogue between the commercial groups and the scientific teams (e.g. house them close to each other). Importantly, people have been hired who thoroughly understand the payer and reimbursement environment (right commercial opportunity).

These principles are by no means fool proof but they have designed a framework allowing management to assess where the pressure points exist in a project. We know from our work as stock pickers that it is often crucial to know what we do not know and that success is aligned with quality work rather than quantity.

AstraZeneca has come a long way in a short time. There will be setbacks but the right pillars are in place and we are already seeing (in presentations and meetings) that this is a very different company from three years ago.

## Outlook

Our market outlook has not changed much; balance sheets are strong and will get stronger, thus acquisitions will continue. Valuations continue to be at the higher end and we remain selective. The recent wave of new listings has given us a new crop of ideas, while we are also looking to get more involved outside the US and Europe.

# Platinum International Technology Fund

**Alex Barbi** Portfolio Manager

## Disposition of Assets

| REGION | JUN 2014 | MAR 2014 |
|---|---|---|
| Asia and Other | 29% | 24% |
| North America | 24% | 20% |
| Europe | 18% | 19% |
| Japan | 13% | 12% |
| Russia | 3% | 1% |
| Africa | 2% | 3% |
| Cash | 11% | 21% |
| Shorts | 3% | 4% |

Source: Platinum. Refer to Note 3, page 40.

## Performance and Changes to the Portfolio

**(compound pa, to 30 June 2014)**

| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Int'l Tech Fund | 2% | 22% | 15% | 9% | 9% |
| MSCI AC World IT Index | 4% | 27% | 20% | 13% | -5% |

Source: Platinum and MSCI. Refer to Note 1, page 40.

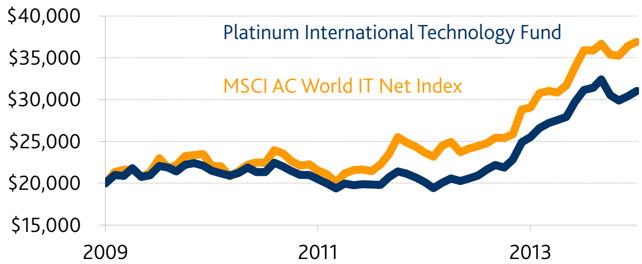
During the quarter the Fund was up by 1.7% and the MSCI World Information Technology Index (A$) was up by 4.3%. For the year, the Fund's return was 21.7% compared to 27.1% for the Index, with the net invested position at 86%.

Among the Fund's best performers and major contributors were: semiconductors stocks (Skyworks +25% and Intel +20%) and DRAMs (Micron +39% and SK Hynix +35%). Detracting from performance were: Chinese Internet stocks (Sina -18% and Sohu -11%).

Currencies detracted from performance with the Australian dollar up between 3 and 5% against major counterparts.

**Value of $20,000 Invested Over Five Years**

*30 June 2009 to 30 June 2014*




Source: Platinum and MSCI. Refer to Note 2, page 40.

During the quarter we added to ASML Holding (semiconductors), Google (Internet advertising) and Ciena (optical networking). We exited Amadeus IT Holding (software) and cut our holding in Safaricom (mobile communications) and Apple.

## Commentary

Smartphones accounted for 63% of all mobile phone shipments in first quarter 2014, up from 51% the year before. According to the International Data Corporation (IDC) Worldwide Quarterly Mobile Phone Tracker, vendors shipped more than 280 million smartphones worldwide, up 29% from the first quarter of 2013. This compares to the worldwide mobile phone market generally, where vendors shipped 449 million units, up 4% on the 2013 first quarter.

While these numbers are impressive, the reality is somewhat more complicated. After several years of strong growth, smartphones are becoming to some extent more commoditised, particularly in the lower price segment.

While high-end top selling models like Apple iPhone and Samsung Galaxy together represented more than 35% of shipments, the markets dynamics are changing to reflect the rise of China, which shipped a record 40% of the smartphones globally. China Mobile, the country's largest mobile operator, is in the early stages of a nationwide 4G network roll-out. Its competitors are likely to embark soon on similar upgrade plans. These initiatives underscore the rising importance of the Chinese consumer.

With a lower budget than their Western counterparts, Chinese mobile subscribers are now being offered smartphones at more affordable prices. According to Sina News, in May 2014, Samsung Electronics and Apple ranked number 2 and 3 respectively by market share, losing the top spot to a brand named Coolpad. In fact eight of the top spots were taken by domestic brands, with Lenovo in fourth spot, followed by vendors like OPPO, K-Touch, Huawei, ZTE, Hisense and BBK. These brands are almost unheard of outside of China.

IDC expects total smartphone shipment volumes to reach 1.2 billion units in 2014, up 19% year-over-year from the 1.0 billion units shipped in 2013. While this is still respectable growth, volumes have retreated from their 2013 highs. China is expected to be the major driver while developed markets like Europe, Japan, Korea and the US are showing signs of plateauing. Prices are declining, reflecting change in product mix and a bigger weight of lower-priced smartphones. Overall, the average selling price for all smartphones this year will reach $314, down 6% from last year's average selling price of $335. By 2018 the average price is expected to be $267.

In China, Coolpad launched a model with 4G connectivity, priced below 1000 yuan (US$160): the Coolpad 4G model 8705, costs only 799 yuan (US$130) and with good tech specifications!

The growth divergence between developed and developing markets, slower innovation pace and increased competition from China, has driven the big players to introduce mobile devices and accessories with new designs and form factors. Over the last few months we have seen examples of so-called 'wearable devices'. Samsung launched a series of 'Gear' smart-watches and fitness bands with the ability to track your daily activities (running, walking, cycling) and monitoring your heartbeat. **Google** launched its 'Glass', a wearable computer with an optically head-mounted display which presents information in a smartphone-like hands-free format. Apple will soon start production of the long awaited iWatch, which should contain ten different sensors and will be wirelessly rechargeable!

An even more drastic vision for future mobile devices is the one explored by Google with its Project Ara, developed by a small team within the company called Advanced Technologies and Products (ATAP). Staffed with some of the brightest minds at Google, mostly ex-engineers from Defence Advanced Research Project Agency (DARPA) – the birthplace of the precursor to the current Internet - Ara has a mission to make a modular smartphone. It will be very different from existing models: you will basically assemble and upgrade your phone to your own preferences, by swapping in and out every component from the camera, to the display, to the battery, in order to always have the exact phone you want.

With Ara, Google wants to build a device that will make the smartphone accessible to the billions of people who can't afford the expensive models. Google management have given ATAP a two year deadline to turn Ara into a product people can buy: they are one year from the deadline now. While it could be easy to discount this project as a pie-in-the-sky Lego-like concept with very few chances of ever being completed, if successful it could change the industry forever. It would require new types of manufacturing, new ways of buying and selling phones and its modules/changeable parts, and consumers could adapt to new ways of interacting with their devices.

Next year, Google plans to produce a so-called 'grey phone', a bare-bones device with little more than a processor, Wi-Fi module, and screen. A consumer will buy and use the grey phone, or use a built-in app to buy module upgrades or custom shells. Google is targeting a production cost of **only $50!**

Whichever the next best selling phone will be, the fact is that by 2020 there will likely be 50 billion connected devices (Ericsson's estimates). That in itself suggests that people will have multiple mobile devices and passive devices/sensors will probably represent the majority of these connections. The Internet of Things (or machine-to-machine communication) will become a new growth driver with applications as diverse as traffic management, vehicle tracking, car safety, health monitoring, energy grid management, supply chain management etc all potentially benefiting from the proliferation of intelligent data collection.

**Google Project Ara**

Source: http://www.afrik.com/IMG/arton37858.jpg

Also see video at: http://www.youtube.com/watch?v=PQqudiUdGuo

We believe the Fund with its holdings in semiconductors companies such as **Intel, Skyworks** and **Samsung Electronics** is well-positioned to benefit also from these new opportunities.

## Outlook

The Japanese market holds the best prospects of outperformance for the rest of 2014 as government institutions like the Government Pension Investment Fund (GPIF) and the Bank of Japan (BOJ) embark on unprecedented plans to stimulate the economy with unorthodox monetary policy forcing re-allocation from bonds to real assets like equities.

Recent developments in Iraq, however, could slow down economic growth in countries more dependent on imported energy and Japan is definitely one of them.

In China and Russia, valuations for the Fund's Internet stocks remain attractive after the recent de-rating and sharp sell-off triggered by macro-economic and geopolitical concerns.

In general, we are positive about technology stocks in the medium-term and the Fund is well-positioned in key investment themes (4G wireless capex, Internet/e-commerce, memories and emerging markets telecoms).

# A visit to St Helena

**Part 2**

The RMS St Helena follows the tradition of passengers making their own entertainment and we enjoy the story of one who became a Guinness World Record holder for the first mother and daughter to row across the Atlantic. There is great anticipation as the Fancy Dress competition is announced. Sadly relatively few of us line up. Captain Young reluctantly accepts the position of judge, inspects the contestants, prudently retreats to his cabin to reflect (he says), returns and announces it is too difficult to select a winner (he has done this before), and proceeds to award everyone a prize. All enjoy a convivial evening.

We overtake a pod of whales but no other ships follow this route. Three days out of Tristan, following the line of the Mid-Atlantic Ridge several kilometres below, we sight land again – the marginally less remote and larger island of St Helena some 2,000 kms from the West African coast.

The Governor of St Helena is first to disembark for Jamestown and his Office in The Castle. No clambering down the side of the ship into the strong arms of islanders is required here, to my wife's dismay. In the sheltered waters of James Bay we are off-loaded in groups to a launch. We slowly clear Immigration and Customs, the officials clearly not used to a mass influx of about 110 tourists. Jamestown is a largely unaltered Georgian town nestled in a steeply-sided valley clothed in mesh to protect from falling rocks. This part of the island is dry and the hills are brown – higher up, the island receives the weather and is green and cooler. The climate is pleasant all year round and doesn't disappoint us during our five days with only low cloud as we trek over the peaks.

The volcanic island was developed by the East India Company which protected its asset with extensive defences on all sides of the island and particularly around James Bay. Old cannon, and crumbling fortifications, camps and lookouts abound since the island was of interest to many including the French who may have attempted to rescue one of its most famous inhabitants, Napoleon.

We visit Longwood House and its grounds, Napoleon's home whilst in exile and legally French soil. Originally a farmhouse, it is somewhat neglected despite its historical significance, and we are told that much of the furniture has been returned to France 'for restoration'. The gardens he designed himself and delighted in are not particularly well maintained and an influx of tourism is required to justify improvement and return to more glorious times. We learn that Napoleon's 'exile' included the company of several of his generals and family members and the British supplied them all with many of the benefits of home. He complained of his cold, damp residence and plans were drawn up for a new one. It was never built, Napoleon died and his tomb lies in an attractive and peaceful spot he selected himself and is reached along a well-maintained path down which we amble. His body was subsequently returned to France where he now rests amongst his countrymen. Few French visit the island.

Jamestown, St Helena from the RMS in James Bay

Trade winds took English sailing ships returning from India, China and South Africa past St Helena and we read old tombstones to learn of the origins of the deceased and how they came to be buried on the island, many succumbing on their return journey to England. We read the plaque to the memory of those lost in 1941 when the RFA Darkdale was sunk in James Bay by a U-Boat. There are other shipwrecks and diving is possible.

The RMS is the only way on and off the island although after years of indecision by the British government the construction of an international airport is underway at a cost of many times the size of the local economy. We are taken by Dave 'the bug man', who is enthusiastically researching the unique insect life of the island, to view the earthworks. There is not much flat land on a small, volcanic island and much disturbance is required. Dave's from England and he enjoys filling his Land Rover with rare human visitors. He points out to us the equally rare Wirebird (a plover featured on the island's coat of arms) and explains the flora. We climb through low cloud to abandoned flax fields. NZ Flax grows well, too well, on this side of the island and farmers exported large quantities of processed flax to the British postal authorities for mailbags. In 1966 synthetics replaced natural rope and string, the contract was terminated, and the economy collapsed.

From an island that could service over a thousand sailing ships a year with fresh food in addition to its own requirements, St Helena is now dependent on imported food brought by the RMS from Ascension or Cape Town. The shops are full of packaged and frozen food from the UK and South Africa. We search in vain for fresh fruit and are tipped off by an expat resident that there is a crate of oranges at the shop in the next street. A few days later (someone has inadvertently stored perishable items in one of the ship's non-refrigerated containers delaying unloading), the RMS' cargo of fresh fruit and veg is released, an announcement is made on the radio, and Jamestown is flooded as shoppers from all over the island strip shelves bare again. The arrival of the RMS and the unloading of the ship is an exciting time for all and the narrow streets are suddenly full of small trucks distributing boxes and furniture to every shop in town.

The cost of living seems to us to be high and with a good salary apparently being £6-8,000 pa we speculate how 'Saints' survive. The construction of the airport has brought overseas workers and business to St Helena and we are told there is no more unemployment. There is expectation of a significant tourist industry but we are not so sure. Airfares will need to cover the cost of carrying additional fuel as in the

The Barracks of Ladder Hill Fort

event of bad weather the nearest airport is thousands of kms away. There is not much tourist accommodation on the island and foreign hotel groups expressing interest in construction have gone mysteriously quiet we are told. Nevertheless there is already talk of extending the planned runway and we speculate that there may be a military rationale behind the airport's construction.

We take the local bus around the island, get off outside the Governor's Residence, and chat to a member of the police force. To our surprise he's from Glasgow, a retired 'bobby' on secondment, and an exile himself but this time from a Scottish winter. He explains that many members of the force are from the UK as it is difficult to recruit from islanders who know each other too well. Crime he says is reflective of a country area with low income but this surprises us. He wishes us well and after a brief but futile look at the Residence gardens to spot the world's oldest living animal, Jonathan, we rejoin the bus on its circular route to Jamestown.

We need some exercise after many days on the RMS and ask to be dropped off at the Ladder Hill Fort which overlooks the capital. The old barracks are interesting and the officer's quarters are occupied today as private residences. We are told a hotel group has its eye on the site which is a splendid position to watch for approaching ships. We spot the plaque of the St Helena Railway Company attached to a wall. Built in 1829 the 'railway' is now a steep staircase of 699 steps on either side of which was once an inclined-plane cableway used to deliver fresh food from the fields above the town to the inhabitants below balanced by waste moving in the

Jamestown from Jacob's Ladder

opposite direction. The steps of Jacob's Ladder are high and uneven, and the ascent is 600 feet. We climb slowly down taking advantage of the iron handrail to stop us falling forward. Every year there is a race upwards. The record time is around 5 minutes. I vow to return and next day climb up in around 15 minutes – whilst stopping frequently, to take in the view and some photographs of course.

At the bottom of the steps lie the town's museum and the curator practices answering our questions. The tourists coming by plane are seen as the saviour of the island and the RMS' passengers are feted with locally grown coffee by the town's Councillors anxious to know our thoughts of the island, its facilities and what tourists will expect. Everyone is keen to contribute. We meet with Merrill, the enthusiastic and helpful Tourism Manager. We tell him why we came to St Helena, a story he finds of great interest, and he introduces us to the local Sentinel journalist. News is short and we are interviewed for its sister radio station as well.

There are several British and other foreign nationals based in St Helena, mainly working in specialist areas. We chat to one who is developing for the government a risk management plan. In 1995 another British Overseas Territory, the Caribbean island of Montserrat, required evacuation as a dormant volcano decided otherwise and lessons learned are being applied to St Helena.

Saints we meet are friendly, although we note some antagonism towards expats on salaries much greater than local rates. There is a shortage of accommodation and property prices and rents have increased significantly since the airport construction began. Government policy is to encourage the availability of rental property and empty properties owned by Saints attracted to the much higher wages and salaries offered in Ascension, the Falklands, and the UK are subject to additional local taxes unless available for rent. On return, savings are used for new homes and for improvements. Saints working overseas also bring with them their British cars and the capital's streets resemble a small, busy market town in the UK. Tax law is simple and changes affecting small business announced in the Budget are available on a single sheet in the local post office. The Bank of St Helena prints its own 'pounds and pence', its value fixed to and interchangeable with sterling. Security at the Jamestown branch is remarkably light but there is limited opportunity to escape or spend and anyway everyone is known to everyone else.

It is time to leave. The departure time is announced by radio and our hosts, from whom we have arranged the rental of a country cottage some 18 months prior, warn us, and next day collect our bags and drop us off at the Customs House on the edge of the Bay. It is a modern, well-designed building designed to blend with the historical buildings around it. Some of our fellow passengers are remaining behind and will catch the RMS on its return from Cape Town to travel northwards to Ascension from where they will catch the regular Royal Air Force flights to Brize Norton in Oxfordshire. They come to watch the ship leave and to bid us farewell. We are ferried back on board together with returning expats - the French government's representative, and a judge and barristers returning to the UK having completed a major trial on St Helena - and Saints travelling for medical treatment to South Africa. The forward decks are stacked high again but this time with empty containers.

We have another five days to Cape Town but we are now well-versed in the ship's routine. Calm seas and bright sunshine allow a game of deck cricket. The crew wins but only just. A few 'balls' go over the boundary fence into the sea which counts as a dismissal.

Captain Young, a Saint, delights us with his slides and talk of the original RMS St Helena and the chartered RMS Centaur. The original RMS became a 'Ship Taken Up From Trade' during the Falklands War leaving the island completely cut-off. Refitted with a helicopter pad on the passenger sun deck, the RMS, complete with its crew - which the Royal Navy only discovered later included several female crew members strictly against the rules of active service - was used as a supply vessel. The Centaur was chartered as a stop-gap measure (which lasted much longer than envisaged) and was anointed 'RMS' in its place. Our voyage in 1983 on the RMS Centaur from South Africa to Fremantle at the end of its charter has been described in the Sentinel article. He, together with the ship's now Chief Steward, had been with us on that journey and the Captain invites us to sign the Ships Log.

What will happen to the RMS is unknown. Its useful life has been extended once already and when the airport is operational it will be obsolete. It will be a sad passing and we speculate how items not capable of being carried by air will reach this isolated and tiny British outpost. We have thoroughly enjoyed our voyage and visit to Tristan and St Helena with plenty of memories and stories to recount.

**Part 1, visit to Tristan da Cunha, appeared in the 31 March 2014 quarterly report.**

RE Stokes
PT Funds investor

Napoleon's tomb


Jacob's Ladder

# Glossary

Japanese Government Bond (JGB)
A bond issued to investors by the Japanese Government, denominated in Japanese yen. Currently JGBs (10 year) offer a yield of about 0.56%. Bond prices have an inverse relationship to bond yields. This means that falling bond prices denote rising yields and vice versa. If the economic outlook in Japan begins to improve and long-term interest rates rise in Japan, JGB prices will fall. By short selling JGBs, the Platinum Japan Fund is positioned to benefit from an improvement in the Japanese economy.

MSCI Indices
Varying indices compiled by Morgan Stanley Capital International (eg. World, Asia, Healthcare etc) that are designed to measure equity market performance across different regions and industries.

Platinum does not structure its investment portfolios relative to a benchmark, however, the MSCI indices are used as a reference to determine how each Fund is performing in relation to the total market opportunity in which it invests.

Price to Earnings Ratio (P/E)
The ratio of a company's current share price to its per share earnings. The P/E is used as an indicator of the value of a company by comparing its share price to the amount of per-share earnings the company generates.

Quantitative Easing (QE)
A monetary policy used by Central Banks to increase the supply of money by increasing the excess reserves of the banking system.

Return on Equity (RoE)
Measures the rate of return on the ownership interest (shareholders' equity). It indicates how well a company uses investment funds to generate earnings growth.

Short Selling or Shorting
A transaction by which an investor is able to generate profit from a fall in the price of a particular company or market index. To generate such a profit an investor borrows securities and sells them, then when the price has fallen, the investor repurchases the securities at a lower price and returns them to the lender.

Platinum utilises short selling of stocks and indices for risk management (that is, to protect a Fund's Portfolio from either being invested or uninvested) and to take opportunities to increase returns.

Short selling is not undertaken for the Platinum Unhedged Fund.

**Please visit our website at:**
**www.platinum.com.au**

We have a section titled ‘The Journal’ providing in-depth commentaries on stocks, views and insights, and the fundamentals of investing.


"Yes, we have an early retirement program. We withhold two dollars from each paycheck to buy you a lottery ticket."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*The insider traders always sit together.*

## 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$20,000 invested in the relevant Fund over five years from 30 June 2009 to 30 June 2014 relative to their Index (in A$) 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.

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

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Platinum Asset Management is a Sydney-based manager specialising in international equities. The investment team uses a thematic stock-picking approach that concentrates on identifying out-of-favour stocks with the objective of achieving superior returns for our clients. We pay no heed to recognised indices. We aim to protect against loss and will hedge stocks, indices and currencies in our endeavours to do so.

The firm was founded in February 1994 by a group of professionals who had built an enviable reputation. The investment team has grown steadily and PAM now manages around $23 billion, with approximately 12% of this coming from overseas investors. The Company was listed on the ASX in May 2007 and staff remain the majority shareholders.

Since inception, the Platinum International Fund has achieved returns more than twice those of the MSCI All Country World Index* and considerably more than interest rates on cash.


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