Platinum International Health Care Fund

Bianca Ogden Portfolio Manager

Disposition of Assets

REGION	MAR 2014	DEC 2013
Europe	45%	47%
North America	23%	24%
Japan	6%	7%
South America	1%	1%
Australia	1%	2%
Cash	24%	19%
Shorts	2%	2%

Source: Platinum

Performance and Changes to the Portfolio

(compound pa, to 31 March 2014)

	QUARTER	1 YR	3 YRS	5 YRS	SINCE INCEPTION
Platinum Int'l HC Fund	0%	32%	21%	17%	8%
MSCI AC World HC Index	2%	42%	25%	14%	7%

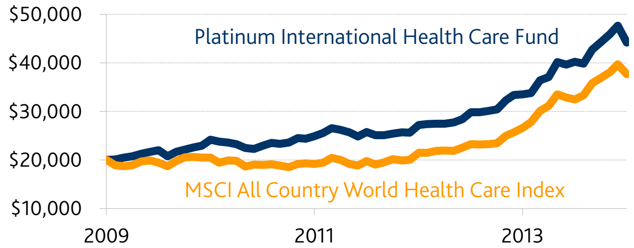
Source: Platinum and MSCI. Refer to Note 1, page 4.

Towards the end of this quarter, US biotech finally saw a decline. Tensions had been rising and the trigger in the end was a letter from the US Government to Gilead looking for an explanation as to why its new Hepatitis C virus (HCV) drug is priced as high as $84k for a 12 week course (for reference it costs $57k in the UK and $66k in Germany). It is not surprising that the US Government is starting to get a little worried; the new HCV drugs are being taken up like hot cakes and new immunotherapy drugs for cancer are being seen as multi-billion dollar drugs. Long forgotten is the consensus view that blockbuster drugs no longer exist, indeed these days they are multi-billion dollar ones!

Combine this belief with the fact that big biotechs pre-tax profit margins will rise up to 60% and one has a scenario that is not sustainable; something will have to give.

Value of $20,000 Invested Over Five Years

31 March 2009 to 31 March 2014



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

We think that the sector has entered a new innovation cycle, but sentiment has become far too positive and does require more level-thinking.

During the quarter we finally exited Gilead after a huge run. Our European holdings continue to do well, some have managed to raise money which is very rare in Europe, but indicates that the appetite for biotech in Europe has been rising. Valuations are a lot more sensible when one considers the new product cycles in the making.

Teva (up 23% for the quarter), a holding we have had for some time, has finally started to have some success. It does help to have been the cheapest company in the sector. However, its Copaxone defence strategy is paying off (from once a day to three times a week), as is its cost savings plan.

We will continue to look for investments that are neglected, but have a base business that can be built upon (e.g. AstraZeneca, a top 10 holding of the Fund). Such thinking has taken us to Japan this quarter.

Commentary

The Japanese pharmaceutical market is a decent size; about $110 billion, which is half the size of the European market. On the surface, its reputation is less exciting. Local pharmaceutical companies have been struggling; some have experienced patent cliffs overseas, others have run out of steam in the domestic market. Tight government regulations, unfavourable pricing and inefficient sales infrastructure are all being seen as the culprit of their demise.

Interestingly, this generalisation is at odds with what we have been hearing from the local Japanese heads of two UK pharmaceutical companies. They are excited about Japan and find it an environment that is favourable and easy to manage. This rather positive view is a sign that something is going on in Japan that is worth getting to the bottom of.

Japan in many ways is no different to Europe when it comes to pricing. US price flexibility does not exist; some may view this as sensible while others see it as restrictive. Remarkably, neither the Japanese companies nor the foreigners see it as bad; they simply say that one has to get the initial price right.

The Japanese government sets the initial reimbursement rate and then gradually, but progressively, reduces the price over the life of the drug. New drugs receive reasonably attractive prices, often better than in Europe. As is globally the case, the key is to introduce new drugs to maintain a healthy price-weighted product portfolio, something the Japanese companies have struggled to do. Foreigners have woken-up to this relatively protected opportunity and accelerated their Japanese product launches.

While Japanese drug prices reduce over time, a US-style patent cliff cannot occur. In Japan, the government guides generic prices and generic penetration is rising albeit at a slow, manageable pace. This has been a double-edged sword for domestic pharmaceutical companies (the foreigners see it as a luxury), who today rely far too much on their old “tail” products. So far there has been no urgency to change their sales infrastructure or their research and develoopment engine. However, we feel that this change is creeping-up and on our travels we saw hints of adjustments.

Currently, Japan has 93k sales representatives in total, including pharmaceutical and wholesale reps, meaning one rep per three doctors versus the US where the ratio is one to seven. Japan should be able to do better and M3, a Japanese company which offers virtual sales practices, is trying to tackle sales inefficiencies. Most pharmaceutical companies are signed up to M3 along with 200k doctors. eDetailing in Japan is growing nicely and so far sales rep numbers have been stable; the next step is a decline in real life reps. Foreign companies are at an advantage when it comes to sales reps; GSK and AstraZeneca as an example have a small number of sales reps in Japan (~1,900 reps each), a number that has managed to remain steady. They prefer to partner with local pharmaceutical companies and use their expertise and reps. This is a good example of the less tribal approach favoured by foreigners. Ultimately, this will bring pressure to bear on the local industry, as they are now launching a number of old drugs. Until recently most pharmaceutical companies launched their offerings to Japan years later than in their home markets. With new drugs, the foreigners will sometimes use their partners and otherwise go it alone.

Several of the Japanese pharmaceutical companies have the fundamentals of a good company, but have accumulated a lot of infrastructure and baggage. This will take time to dismantle and will require a change in thinking from the tradition-bound past. At Takeda, several French executives have been put in charge (CEO, CFO, Chief Procurement, and Chief IT) to return this company to growth. This change is being watched by many with the hope that it will be the showcase for the new style of Japanese pharmaceutical company.

Japan has a sound record of innovation; it is less vibrant than in the US and Europe, but companies like Daiichi Sankyo (a holding of ours) is seen as pretty creative. Daiichi Sankyo has been successful outside of Japan, but is struggling with its Indian subsidiary, Ranbaxy. This was acquired to try to expand geographically and to give it access to the global generic market. It has been a costly experience at several levels and has subsequently turned Daiichi into the lowest valued serious pharmaceutical company in Japan. GSK has formed a joint venture with Daiichi Sankyo dedicated to its vaccines, a big deal for GSK who considers vaccines as one of its strength.

Japanese companies can do good research, but lose the fight to successfully bring them to market and are trumped by foreigners tapping into these pipelines to licence drugs for development (e.g. Johnson & Johnson and Astellas, Biogen Idec and Eisai). Take Mitsubishi Tanabe for example. This company discovered Gilenya, Novartis' Multiple Sclerosis oral pill, while Johnson & Johnson's new diabetes drug Invokana also originates from their labs. These are two recent launches that earn Mitsubishi Tanabe an attractive royalty stream. If it can now reduce its cost structure it will become a good investment (it is another holding in the Fund). Japanese companies have also established venture funds and have been travelling more frequently to find licensing opportunities.

Outlook

It is easy to say that the progress of change in Japan will take time, but that misses the point that current valuations of several of these companies takes no account for advancements made thus far.

We believe that the pricing and rebate discussions in the US will get more coverage and that generalists in particular will review their exposure to US big biotechs. Big pharmaceutical continue to increase their cash balances; they have been wary of merger and acquisition valuations, but may start to reassess their options with corporate action. We are doing the same and remain optimistic of the various options open to us as we migrate the portfolio.

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$20,000 invested in the relevant Fund over five years from 31 March 2009 to 31 March 2014 relative to their Index (in A$) 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. Long invested position represents the exposure of physical holdings and long stock derivatives. The net invested position represents the exposure of physical holdings and both long and short derivatives.

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