# Platinum International Brands Fund

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Portfolio Manager

## Performance

**(compound pa, to 30 September 2017)**

| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Int'l Brands Fund* | 7% | 29% | 15% | 16% | 13% |
| MSCI AC World Index | 3% | 16% | 11% | 17% | 2% |

*C Class – standard fee option. Inception date: 18 May 2000.
Refer to note 1, page 4.
Source: Platinum Investment Management Limited, RIMES Technologies.
Historical performance is not a reliable indicator of future performance.

## Disposition of Assets

| REGION | 30 SEP 2017 | 30 JUN 2017 | 30 SEP 2016 |
|---|---|---|---|
| Asia | 42% | 35% | 31% |
| Europe | 17% | 17% | 27% |
| North America | 16% | 15% | 12% |
| Japan | 10% | 9% | 11% |
| Russia | 3% | 2% | 2% |
| Latin America | 3% | 5% | 11% |
| Africa | 1% | <1% | 1% |
| Cash | 8% | 16% | 5% |
| Shorts | -16% | -10% | -4% |

Source: Platinum Investment Management Limited. See note 3, page 4.

The Fund continued its run of good performance during the quarter, returning 6.6% (C Class), versus 2.8% for the Fund's benchmark (MSCI All Country World Net Index), and 1.2% for the Consumer Discretionary and -2.5% for the Consumer Staples portions of the MSCI (in AUD terms). Over the past 12 months, the Fund (C Class) has delivered a return of 29.2%, versus the benchmark return of 15.7%.

The key drivers of investment returns continue to be the strength of the Chinese consumer, together with the growing understanding on the part of investors that social media and e-commerce platforms are increasingly fundamental to individuals' day-to-day lives, and that the likely result is

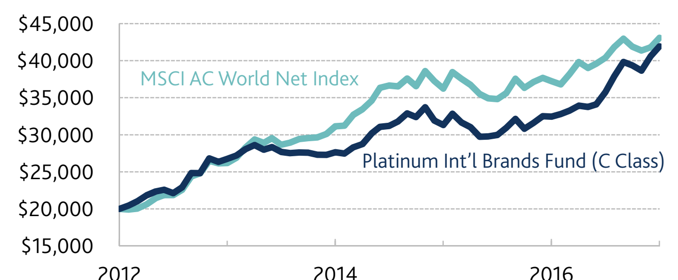
## Top 10 Holdings

| STOCK | COUNTRY | INDUSTRY | WEIGHT |
|---|---|---|---|
| Alibaba Group | China Ex PRC | IT | 4.7% |
| Asahi Group Holdings | Japan | Consumer Stap | 4.2% |
| Jiangsu Yanghe Brewery | China | Consumer Stap | 3.8% |
| Hanesbrands Inc | USA | Consumer Disc | 3.4% |
| Callaway Golf Co | USA | Consumer Disc | 3.3% |
| LVMH | France | Consumer Disc | 3.2% |
| Anta Sports Products | China Ex PRC | Consumer Disc | 3.1% |
| Sberbank of Russia | Russia | Financials | 3.1% |
| Chow Tai Fook | China Ex PRC | Consumer Disc | 3.0% |
| Sina Corp | China Ex PRC | IT | 3.0% |

As at 30 September 2017.
Source: Platinum Investment Management Limited. See note 4, page 4.

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

30 September 2012 to 30 September 2017




Refer to note 2, page 4.
Source: Platinum Investment Management Limited, RIMES Technologies.
Historical performance is not a reliable indicator of future performance.

For further details of the Fund's invested positions, including country and industry breakdowns as well as currency exposure, updated monthly, please visit https://www.platinum.com.au/fund-updates/#MonthlyUpdatesForThePlatinumTrustFunds.

exponential growth in revenues and profits for the winners in this space. The performance of Weibo (+47%), Sina (+35%) and Alibaba (+22%) reflected both these themes. Continued growth in consumer demand for their products drove performance at sports apparel maker Anta (+29%), dairy producer Mengniu (+43%), liquor maker Jiangsu Yanghe (+22%), and jewellery retailers Chow Tai Fook (+18%) and Luk Fook (+21%). Other major contributors to performance in the quarter included leading Russian bank Sberbank, which rose +38% as the Russian economy stabilised; golf equipment maker Callaway, which rose +13% as its latest "Epic" addition to the "Big Bertha" range of woods hit the mark with consumers; and Gucci-owner Kering (+13%), as the market continued to appreciate its strong sales growth and high returns on incremental sales.

The addition of several short positions in the packaged food space toward the end of the June quarter and into the September quarter proved timely and benefited performance. Consumers are increasingly moving away from traditional brands in processed foods toward niche brands perceived as "better for you", as well as substituting canned soup and dried mac & cheese with fresh, chilled alternatives. Social media has reduced barriers to entry for small brands that can now market to consumers without the giant TV advertising budgets of yesteryear. Meanwhile Amazon provides instant national distribution in many Western markets, which allows small brands to reach consumers and gain sales volume without paying large "slotting" fees for positions on supermarket shelves.

Supermarkets are responding to these trends and are taking shelf space away from traditional manufacturers, dampening their sales and profits. Increased competition from Aldi and others is also driving supermarkets toward improved own-brand offerings and lower prices, which in turn add further pressure on the traditional manufacturers. Amazon's recent acquisition of Whole Foods and its move to make Whole Foods' much loved own-brands available online intensifies this dynamic further.

Some "value" investors may be tempted to dip their toes in the water here as stock prices have fallen and P/E ratios now look more reasonable when one uses broker estimates as the "E" in the ratio. We are of the opinion, however, that the shift away from traditional processed food is likely a long-term consumer trend, and that these stocks may prove to be "value traps" when actual future earnings fail to meet the forecasts. Of course, in any given quarter short-term swings in market sentiment toward these stocks may be negative for the Fund's performance.

There were several long positions that fell in value during the quarter, but no single position in the top 30 holdings of the Fund fell by more than 10% in local currency – a satisfactory result. Performance was, however, somewhat hindered by a sizeable rebound in the stock prices of two of our retail shorts following market excitement over their "less-bad-than-expected" results and management plans to cut costs and return to growth. We expect this price action to reverse over the medium term as the rapid progress of e-commerce continues to eat away at the profits of traditional retailers.

The rationale for this is simple: General merchandise and apparel retailers still earn juicy pre-tax profit margins of 6%–10%. Their store-based cost is mostly fixed regardless of sales volume, while each sale they make online comes with attached delivery costs and costs in relation to managing returns of unwanted merchandise. These costs are becoming increasingly expensive as Amazon leads a race to faster (and free) delivery and more convenient return options. However, the price a retailer sells for online is generally the same as in store, if not lower. As consumers buy less in store and more online, the retailer's profit margins mechanically move downward, even in circumstances where the retailer retains the sale through its own online channel and avoids losing it to Amazon, which is definitely not always the case! Many retailers make a loss or are barely break-even in their online businesses (often this includes market-leader Amazon!). Further, price comparisons are now a click away on our phones for any product across a multitude of retailers, meaning that prices both online and in-store are under constant pressure, which adds to the retailer's margin woes. Cost reductions to offset these factors can only go so far before customer service suffers and the loss of sales worsens.

Overall, our short positions were a 0.4% headwind to the Fund's performance in the quarter, but continued to provide a useful hedge against any potential market downturn.

## Changes to the Portfolio

The pace of change in the composition of the portfolio slackened this quarter as the review of all positions in the Fund has largely concluded. Positions closed included several small stakes in Emerging Market stocks with deteriorating competitive positions – Indonesian retailer, Ramayana, and soft-drink bottler Pepsi-Cola Products Philippines. Leading Kenyan blue-chip East African Breweries was another sale in the quarter as its valuation broadly matched its outlook. Larger positions closed included jeweller Tiffany, which brand has lost some of its lustre in the eyes of millennial consumers who prefer to spend on selfie-worthy "experiences" and the latest iPhone to capture them, as well as leading Mexican convenience retailer FEMSA which, while being a fantastic business, trades on an elevated valuation in reflection of that fact.

New positions added during the quarter were out-of-favour stocks that represent solid-to-excellent value propositions. The automotive sector is trading on depressed valuations in response to a number of concerns – a peaking sales cycle in the US and Europe, potential losses in automakers' lease finance books, and fears over the rise of electric and automated vehicles. This has created many prospective opportunities for contrarians, and the Fund has built positions in a much-unloved auto manufacturer and a very cheap auto financier. The latter has the added attraction of being a fast growing online bank, which allows it to decrease its funding cost as deposits grow. The third major position added in the quarter is a leading brewer with exposure to a cyclical rebound in Latin American economies. It should deliver strong earnings growth over the medium term.

## Outlook

The Fund is directly positioned to take advantage of the disruption caused by the growth of e-commerce and social media via stakes in leading internet platforms as well as short positions against traditional retailers and packaged food companies. The remainder of the portfolio is also built with these long-term shifts in consumption habits kept in mind. Long positions held in the Fund can be assigned to three broad categories:

1. Digital platforms – e.g. Alibaba, Sina and Weibo, Schibsted.
2. Consumer service providers, unlikely to be disrupted – e.g. Wynn Resorts, Mandarin Oriental, Sberbank.
3. Consumer brands with unique heritage or performance characteristics that are likely to continue to be in demand online and offline – e.g. Callaway, Louis Vuitton Moët-Hennessy (LVMH), Jiangsu Yanghe, Pernod Ricard, Samsonite, Hanesbrands.

The outlook for the consumer sector is one of continued rapid change that will dramatically affect many companies. We believe the Fund's portfolio will be resilient to, and in many cases benefit from, these changes.

## Notes

1. The investment returns are calculated using the net asset value unit price of C Class (standard fee option) of the relevant Fund and represent the combined income and capital return of C Class for the specified period. Returns are net of fees and costs (excluding the buy/sell spread), are pre-tax, and assume the reinvestment of distributions. The investment returns shown are historical and no warranty can be given for future performance. Historical performance is not a reliable indicator of future performance. Due to the volatility in the Fund's underlying assets and other risk factors associated with investing, investment returns can be negative, particularly in the short-term.

   The MSCI index returns have been sourced from RIMES Technologies. Index returns are in Australian dollars and include dividends, but, unlike the Fund's returns, do not reflect fees or expenses. The net MSCI index is used, except, where applicable, the gross MSCI index was used prior to 31 December 1998 as the net MSCI index did not exist then.

   For the purposes of calculating the "since inception" returns of the MSCI index, the inception date of C Class of the Fund is used.

   Platinum does not invest by reference to the weighting of the index. Underlying assets are chosen through Platinum's individual stock selection process and, as a result, the Fund's holdings may vary considerably to the make-up of the index. Index returns are provided as a reference only.

2. The investment returns depicted in this graph are cumulative on A$20,000 invested in C Class of the Fund over the specified five year period relative to the relevant net MSCI index in Australian dollars.

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3. The geographic disposition of assets (i.e. the positions listed other than "cash" and "shorts") represents the Fund's exposure to physical holdings (equity and corporate fixed income securities) and long derivatives (of stocks and indices) as a percentage of the Fund's net asset value.

4. The table shows the Fund's top 10 long stock exposure (through physical holdings and long derivative positions) as a percentage of the Fund's net asset value.

5. Sector breakdown represents the Fund's net exposure to physical holdings and both long and short derivatives (of stocks and indices) as a percentage of the Fund's net asset value.

6. The table shows the Fund's major currency exposure as a percentage of the Fund's net asset value, taking into account any currency hedging.

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