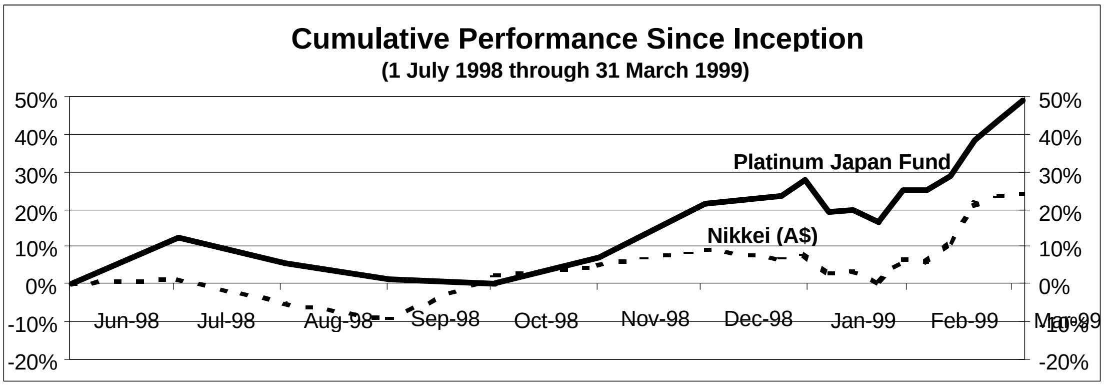
P L A T I N U M ASSET MANAGEMENT

The Platinum Japan Fund

Quarterly Report

31 March 1999

Performance



The Japanese market came out of the blocks with a burst this quarter led by the over-the-counter market. The enthusiasm spread to the banks, information technology sector and continued to broaden throughout the period under intense foreign buying pressure. Over this last quarter foreigners bought ¥2.2 trillion of stock, equivalent to just under half the total net acquisition by foreigners over the full year of 1991, the highest year on record. The consequence of this pressure in the face of continual offloading by domestic companies and banks of their cross holdings, was to raise the Nikkei 225 index by 13%. The fund had positioned itself well having had the luxury of acquiring some solid positions in quieter times. Some of these stocks have subsequently been anointed as internet plays. The consequence was the rise in the unit value of 21% which results in the return over the nine months since inception of 49% in $A. By way of comparison, the Nikkei has risen by 23% since July 1998.

Commentary

The following are probably the most important underlying factors which explain the sudden surge in foreign interest in the Japanese market.

1. Intervention by the Bank of Japan at the short end of the money market to flood the system with liquidity and thereby take pressure off the bond market.

   The eventual agreement between the Financial Reconstruction Commission (FRC) and the banks which resulted in a more realistic assessment of their bad loans and the subsequent submission of detailed recovery plans. In exchange, all the major banks, except the strongest (Tokyo Bank Mitsubishi), received an infusion totalling ¥7.5 trillion to augment their capital reserves.

3. Some evidence that the economy may have begun to stabilise. First by virtue of stocks being run-down against a background of stabilising industrial production, (statistics on consumer spending, department store sales and the like are still negative showing year-on-year declines of around 2.5%). Wages, which include bonuses, have seen their first year-on-year fall since the 1940s.

4. The almost daily announcement of corporate restructuring and evidence of merger and acquisition activity. The highlight was Sony's press conference where it emphasised the

need to cut staff and streamline activity and Renault's announcement that it was taking a 37% stake in Nissan, the country's second largest auto and truck maker.

Having long tried to brush their problems under the carpet, there is a growing realisation among the Japanese that their system needs to be overhauled. The Prime Minister has established an advisory body of leading industrialists and it is interesting to note the recent release making reference of the need to alter the supply side of the economy. Bearing in mind the consensus based nature of Japanese politics, it is very clear that the ground work is being laid to prepare the nation for more unemployment and lower investment by the corporate sector. This will not give much joy in terms of levels of published activity but as we have highlighted in the past, the most important variable investors need to watch is the relative share of the rewards between labour and capital. As noted earlier, over the nine years since the bubble, labour has continued to enjoy rising real wages while capital has been earning ever lower returns. This is unsustainable and is the basis of our enthusiasm for specific Japanese companies.

Outlook

The sheer ferocity of foreign buying over the last three months is bound to subside. Many foreign investors who had neglected Japan must by now have returned to normal weightings (so extreme was this neglect that earlier this year the London Stock Exchange had a higher market capitalisation than that of Japan notwithstanding the former having an economy approximately a quarter the size of the latter). However, in a world where sophisticated markets tend to be fully valued, we should expect further purchases by foreign investors as signs of economic stabilisation emerge.

At the same time, the shift of pension fund assets to more professional management within Japan and perhaps a reweighting towards equities and away from bonds, should absorb the continued release of cross holdings into the market. The latter still constitute some 40% of the market's capitalisation and is expected to leak out at around ¥3.5-4 trillion per annum.

Our assessment is that the initial buying panic is coming to an end and from here one can see managers assembling portfolios in a more measured manner. There are still plenty of very interesting companies to be unearthed.

In our next quarterly, we will spend some time describing these enterprises.

Disposition of Portfolio (Fund Size $12.6M)

Categories	Examples of Stocks	Holding
High Growth	Mobile Telecoms – DDI, DoCoMo Outsourcing – AIM Services, Trans Cosmos	22%
Steady Growth	Coca Cola Bottlers Drug Wholesalers and Pharmaceutical Companies	11%
Cyclical Growth	Sony, Kyocera, Ushio	29%
Restructuring	Toshiba, Hitachi	16%
Deep Value Cyclicals	National House, Taikisha	11%
Korea	Samsung Electronics	3%
Cash		8%