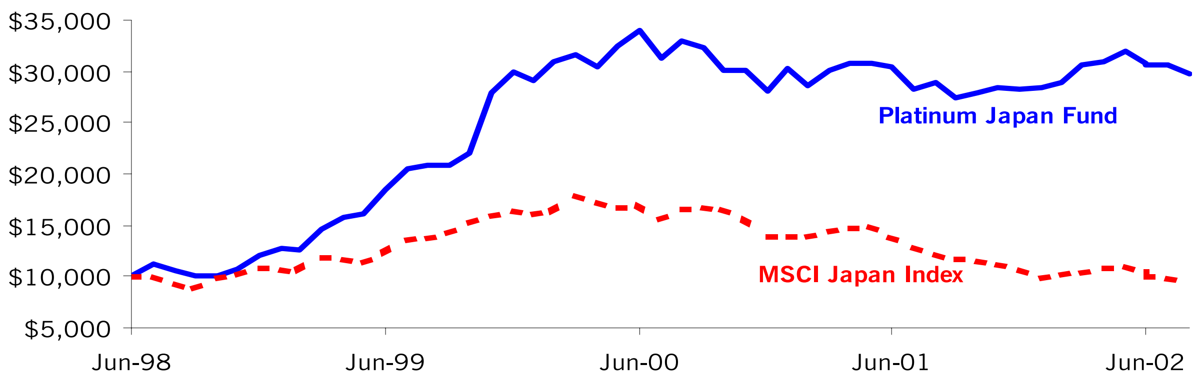
Platinum Japan Fund

Performance

REDEMPTION PRICE: $1.6919

VALUE OF $10,000 INVESTED SINCE INCEPTION (1 JULY 1998 – 30 SEPTEMBER 2002)



Source: Platinum

The Japanese and Korean markets were negatively impacted this quarter by the deterioration in global investor sentiment as a result of weakening global growth and geopolitical fears. In Japan, the Topix declined by 9% in local currency terms whilst in Korea the Kospi fell by 13%. However it should be noted that these markets still performed better than the US and European equity markets, perhaps because they never really saw the bull market excesses that characterised these markets. The one bright spot was Japanese banking stocks which rose by 8% over the quarter as there was speculation that the government would shore up their finances by injecting public funds. Exchange rates were relatively stable over the quarter.

The Fund fell by 3.5% (A$ terms) which was better than the 9.1% decline in the MSCI Japan index. The Fund was protected by its short positions and cash holdings. Within the stocks owned by the Fund, Shimano, Olympus and Korea Telecom did very well on company specific news whilst on the negative side many of our smaller stocks had large falls as investors reduced exposure to riskier, smaller capitalisation shares. For the year to 30 September 2002 the Fund rose 8.3%, comfortably ahead of the MSCI Japan which declined by 18.7%.

Changes to the Portfolio

DISPOSITION OF ASSETS

Region	Sep 2002	Jun 2002
Japan	65%	68%
Korea	24%	20%
Cash	11%	12%
Shorts	13%	18%

Source: Platinum

There were quite substantial changes in the Japanese segment of the portfolio as the market decline presented opportunities. Generally we were adding positions in higher quality, larger capitalisation issues with good records at the expense of companies where we were uncomfortable either because they were trading positions or their fundamentals were questionable in a difficult economic environment. We added positions in Takeda, Yamanouchi, Ushio, Olympus and Fuji Photo. We also increased positions in Credit Saison and Aiful. These stocks have been hurt by the rise in delinquencies as a result of the weak economy but are now very cheap for the type of growth rates they can attain. However if the economy continues to deteriorate they will be subject to some downside. To finance these purchases we sold our entire positions in Sekisui Chemical, Fujikura Kasei, Hitachi Capital, Enix, TOC and Nippon Broadcasting.

Fundamentally we are defensive in our thinking due to our feeling that global economic growth will go through a "payback" period for the high growth rates experienced in the late nineties capital spending boom. In this environment companies promising too much into the future (high PE's), having lots of debt and subject to management uncertainties will not be treated favourably by the market. Small companies on balance will probably struggle to gain a foothold in the industrial consolidation. When we look at how defensively we are positioned we take into account many factors, some of which we have outlined below.

	% of total portfolio
Cash and Shorts	24%
High Debt/Equity Stocks (mostly utilities)	13%
Financial Stocks (primarily Japanese credit card companies)	12%
High PEs (companies with losses such as MEI)	10%
Small companies	6%

Source: Platinum

As is clear we are shying away from the riskier parts of the market. A new addition to the portfolio was Ushio Denki. It is a specialist in the field of industrial lighting, supplying high powered lamps and equipment to clients over a broad range of industries covering office automation, semiconductors, visual imaging and specialty lighting. The company has focused on light applications since its inception and holds very significant market positions with about 70% of its product lines having greater than 50% world market shares. For example, the company holds 65% of the world market for exposure lamps used in copiers and printers and it holds 50% of the world market for high powered projection lamps for cinema projectors. Recently the shares were sold down because of its classification as a light source supplier to stepper makers but in reality this is a much broader company (less than 10% of sales in this area) and is heavily weighted toward consumable supplies of lamps which are much more stable than equipment sales. We see interesting growth potential for the company in stepper light sources and cleaning lamps for LCD screens as well as in digital cinema as the old fashioned film based analog projectors are replaced. In addition the use of light is a highly effective, clean and safe method for manufacturing in the nanotechnology world which we are rapidly entering.

Commentary

The most interesting piece of news out of Japan this quarter was the announcement by the Bank of Japan (BoJ) that it would buy some cross shareholdings from the banks. These are shares held as assets by the banks in their clients listed shares and because of their magnitude (about A$370 billion) they represent a real threat to bank solvency as the equity market declines. Central banks almost never buy equities because of the moral hazard it creates so it certainly marks a significant new chapter in Japan's struggle with depression. At this stage, given the relatively small amount of money involved (perhaps up to A$45 billion), it seems that the BoJ is trying to deflect criticism of its inaction back onto the politicians by invoking a sense of financial crisis and forcing the lawmakers to inject public funds into the banks. One needs to recall earlier protests by the public regarding the use of taxpayer funds to bail out the banks. Its aim would seem to be to nationalise the problem by putting the banks on a sounder footing. Simultaneously, this could be expressed in looser monetary policy which could help boost the real economy. We remain of the view that Japan's main problem is deflation and with general price levels having adjusted to western levels, the onus is on the BoJ to act. Putting the banks on a more stable footing may just give the BoJ the chance to allow its monetary policy to work. However, it probably needs to do more in terms of quantitative easing and it has said nothing about this at this stage.

In Korea we continue to run a somewhat defensive position. This is in contrast to our more positive medium term view and reflects a number of factors including the good performance of the market in the past year, slowing export growth and the prospect of tighter monetary conditions as a result of the recent consumer boom. Traditionally the time to sell Korea is when everyone is positive (which largely they are) and after a good cyclical run in the economy. Further grist to the mill has been provided by the recent government moves to guide the banks to rein in credit card lending and for the banks generally to raise provision levels. In addition a lot of the positive comments about Korea derive from the very good performance of Samsung Electronics in global markets which we think is probably well discounted and may see some slowdown. Having said that we remain positively disposed to the market and buyers on weakness as the market seems to be discounting a 40% decline in earnings next year which is probably about as bad as it could get. In the meantime the utilities may do quite well. Korea Telecom and particularly Korea Electric Power look very attractively priced investments.

Another interesting aspect to the Korean market has been the flurry of activity surrounding North Korea. Recently the North significantly raised prices and wages for a large part of the population which may be the first moves to a market-based economy. In addition there has been high level diplomatic activity with visits made by senior leaders to China and Russia as well as the historic visit by Japanese Prime Minister Koizumi to Pyongyang. The North and the South, despite the recent naval clash, have agreed to reopen the border with a train service and take other measures to generally reduce tensions. It is not entirely clear what is driving this action but on the whole the reduction in tensions is positive. The hurdle at present is the US which named the country in its “axis of evil” and it is possible that the North is making these efforts mindful of being on the wrong side of US foreign policy.

Outlook

We continue to believe that we have a portfolio of very attractive stocks. However, the global outlook continues to deteriorate and this will make it hard for us to achieve much absolute performance. We have seen some major deterioration in prices of stocks, but there are still some names that probably have further to fall. In addition, there is the prospect that equity losses sear investor’s confidence and that asset preferences move away from equities. On balance, the odds favour a defensive portfolio at present. We will remain nimble and alert to changes in central bank policy and global conditions.

Jim Simpson
Portfolio Manager