# Platinum Unhedged Fund

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Portfolio Manager

## Performance

**(compound pa, to 31 March 2018)**

| | QUARTER | 1YR | 3YRS | 5YRS | SINCE INCEPTION |
|---|---|---|---|---|---|
| Platinum Unhedged Fund* | 0% | 24% | 12% | 19% | 12% |
| MSCI AC World Index | 1% | 14% | 8% | 16% | 7% |

*C Class – standard fee option. Inception date: 28 January 2005.
Net of accrued fees and costs. 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 | 31 MAR 2018 | 31 DEC 2017 | 31 MAR 2017 |
|---|---|---|---|
| Asia | 41% | 42% | 35% |
| North America | 21% | 20% | 24% |
| Europe | 19% | 19% | 24% |
| Japan | 7% | 9% | 9% |
| South America | 1% | 1% | 0% |
| Russia | 1% | <1% | 2% |
| Cash | 10% | 9% | 6% |

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

## Top 10 Holdings

| STOCK | COUNTRY | INDUSTRY | WEIGHT |
|---|---|---|---|
| Raiffeisen Bank International | Austria | Financials | 4.2% |
| Jiangsu Yanghe Brewery | China | Consumer Staples | 3.4% |
| Kweichow Moutai | China | Consumer Staples | 3.3% |
| KB Financial Group | Korea | Financials | 3.1% |
| Applus Services | Spain | Industrials | 3.0% |
| ENN Energy Holdings | China | Utilities | 2.9% |
| PayPal Holdings Inc | USA | IT | 2.9% |
| Alphabet Inc | USA | IT | 2.8% |
| 58.com Inc | China | IT | 2.5% |
| IHS Markit Ltd | USA | Industrials | 2.5% |

As at 31 March 2018.
Source: Platinum Investment Management Limited. See note 4, page 4.

For further details of the Fund's invested positions, including country and industry breakdowns and currency exposure, updated monthly, please visit https://www.platinum.com.au/Investing-with-Us/Investment-Updates.

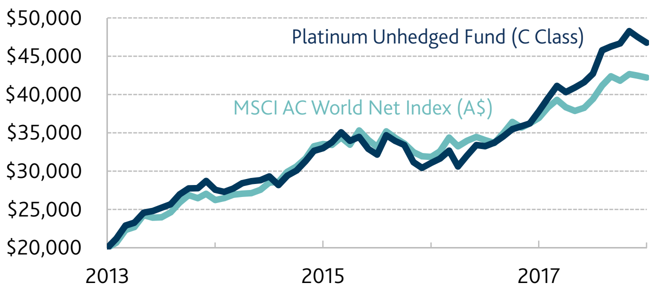
2018 brought with it a return of volatility, with the US market falling -10% in the first week of February. The selling in the US triggered a follow-on response around the world with the European (-8%), Japanese (-12%) and Chinese (-12%) markets all falling in unison.

Why did this happen? The accepted narrative is that the prospect of higher inflation in the US (a result of stronger wage growth) sparked the initial selling, which was later fuelled by the Trump administration's announcement of trade tariffs against China.

Subsequently we saw most markets rebound in March and recover some of the losses. Despite being the source of the concerns, the US market fell the least, down -0.8% for the quarter. Elsewhere, both Japan (-5%) and Europe (-4%) posted moderate declines while China (+2%) finished the quarter in positive territory (in local currency terms).

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

31 March 2013 to 31 March 2018




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

Overall the Fund (C Class) returned (+0.2%) over the quarter, compared to its benchmark MSCI index which returned (+1.0%) (in Australian dollars).

## Changes to the Portfolio

In previous reports, we have discussed our investment approach of seeking out situations of temporary uncertainty, where expectations around the future of a company's business and its stock price are dampened due to some problem. Another source of ideas is when an industry or business is undergoing significant change. Our cognitive biases make it difficult for us as investors to fully envision a world that is immensely different to the one we are used to, and hence companies undergoing change often become mispriced.

An example of this change is the advancement in artificial intelligence (AI), where increasingly we are seeing software algorithms make ***better decisions*** than humans. One of the most high-profile applications of AI is autonomous vehicles, but there are many more subtle examples in the background. Take banking and insurance, important decisions around who to lend to and how to price policies were once handled by human agents and used to take days, but are now increasingly performed by algorithms in seconds.

Artificial intelligence and automation are only as good as the data that powers it, and hence quality data becomes more valuable in this new world. A recent addition to the Fund that benefits from this trend is **Equifax**.

Equifax collects data on consumers and sells it to businesses. Its two largest data categories are consumer credit history (e.g. did you repay your previous debts and do it on time) and employment and income verification.

The business has benefited from two major tailwinds, which have allowed Equifax to consistently grow its profits at 10-15% per annum over the last few years.

1. As commercial activity has moved online, the frequency of access to its data has increased. For example, a customer might visit three lenders and fill out applications when looking for a loan in the old days. Now, they fill out one form online and receive quotes from 10 lenders, each of whom will query Equifax's database.

2. As more industries have embraced AI and looked to automate decisions, Equifax's user base has broadened. Credit data, once only used by banks, is now being utilised by insurers to predict which customers are more likely to make a claim. Elsewhere, governments are using Equifax's employment and income data to spot social security fraud.

Our position in Equifax was built in September 2017, after the stock fell 35% in response to the news of the data breach Equifax had suffered. In the immediate aftermath, Equifax faced immense media pressure, fines and increased cyber security costs. However, what is important is that the company's core position as a data bureau has not been compromised and that its customers still rely heavily on its data.

While the stock has quickly risen above our entry price, given the tailwinds noted above, we expect there is more to come. Equifax is a good illustration of how both pillars of our investment approach – mispricing due to temporary uncertainty and opportunities created by structural change – are applied in practice.

Another new holding that is benefiting from significant, though under-appreciated, secular change is **Microchip Technology**. Microchip makes microcontrollers (MCUs), which are essentially a complete computer (albeit a simple one) on a single chip that is dedicated to one function. For example, your microwave will contain a MCU to detect button presses, turn on the magnetron tube and sense if the door is open. In addition, MCUs can also be a part of larger systems, such as controlling a particular function in the navigation system of a Boeing jet.

Rarely seen as a play on the sexy tech themes of the day, Microchip nonetheless is a beneficiary of many secular growth stories. The growing electronic content of automobiles, alongside the greater desire for connected devices (the so called Internet of Things or 'IoT'), is driving consistent growth in MCU demand.

Another positive is that Microchip operates in one of the more attractive niches in semiconductors. More than 60% of sales are to the industrial and automotive sector, where a 2-3 year 'design in' time is followed by 10-15 year product lifecycles.[1] As the MCU is designed specifically for a single end product, the quality of its associated developer tools (along with having a large base of developers who are already comfortable using them) is more important to its customers (the makers of the end products) than having cutting edge processing power. The high switching costs and customer loyalty allow the business to have operating margins of around 40%.

The stock's recent -20% fall on fears of a cyclical slowdown in the semiconductor market gave us the opportunity to buy this high quality grower on 15x earnings.

1 This is in stark contrast to the competitive smartphone market where chip makers are required to 're-win' their place in the device every 1-2 years.

## Outlook

Given the historical dominance of the US market in size as well as media coverage, it is common to view the outlook for international equities from a US-centric perspective. What one finds in the US is a combination of a long bull market, high starting valuations, rising interest rates and increasingly unpredictable politics. Sounds pretty worrying!

But what if we instead focus on the conditions and outlook in the rest of the world? We find China emerging from a three-year slowdown after reducing excess capacity in real estate and many heavy industries. We find India set to accelerate its growth momentum as its banks start to lend again after a five-year clean-up of the bad debts in the banking system which had suppressed growth. We also find both Europe and Japan in the middle – rather than the later stage – of an economic recovery where interest rates are still supportive and valuations are not stretched. Suddenly the picture looks a lot more sanguine.

Notwithstanding all the headlines around US-China trade tensions, our primary concern for markets remains higher interest rates in the US and the pressure this will place on consumer spending and equity valuations. Currently, close to 70% of the portfolio (without taking into account the 10% cash holding) is invested outside the US where valuations are more attractive and where we still see good prospects for earnings growth.

## Notes

1. Fund returns are calculated using the net asset value per unit (which does not include the buy/sell spread) of the stated unit class of the fund and represent the combined income and capital returns of the stated unit class over the specified period. Returns are net of accrued fees and costs, 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.

   Index returns are in Australian dollars and assume the reinvestment of dividends from constituent companies, but do not reflect fees and expenses. For the purpose of calculating the "since inception" returns of the MSCI index, the inception date of C Class of the fund is used. Where applicable, the gross MSCI indices were used prior to 31 December 1998 as the net MSCI indices did not exist then. Fund returns have been provided by Platinum Investment Management Limited; MSCI index returns have been sourced from RIMES Technologies.

   Platinum does not invest by reference to the weightings of any index or benchmark, and index returns are provided as a reference only. A fund's underlying assets are chosen through Platinum's bottom-up investment process and, as a result, the fund's holdings may vary considerably to the make-up of the index that is used as its reference benchmark.

   The stated portfolio values of C Class and P Class of the Platinum International Fund (PIF) do not include funds invested in PIF by the Platinum International Fund (Quoted Managed Hedge Fund), a feeder fund that invests primarily in PIF. The stated portfolio values of C Class and P Class of the Platinum Asia Fund (PAF) do not include funds invested in PAF by the Platinum Asia Fund (Quoted Managed Hedge Fund), a feeder fund that invests primarily in PAF.

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

   Fund returns are calculated using the net asset value per unit (which does not include the buy/sell spread) of C Class of the fund and represent the combined income and capital returns of C Class over the specified period. Returns are net of accrued fees and costs, 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.

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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 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 positions (through physical holdings and long derivatives) 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 currency hedging.

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Some numerical figures in this publication have been subject to rounding adjustments. References to individual stock performance are in local currency terms, unless otherwise specified.

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