



Platinum
World Portfolios
Japan Fund

Quarterly Investment
Manager's Report

30 June 2016

Platinum World Portfolios - Japan Fund



Scott Gilchrist Portfolio Manager

Disposition of Fund Assets

REGION	JUN 2016	MAR 2016
Japan	88%	77%
Cash	12%	23%
Shorts	-1%	-2%

Source: Platinum. Refer to note 2.

Sector Breakdown

SECTOR	JUN 2016
JAPANESE INTERNATIONAL FOCUS	43%
Electronics (Canon, Nitto Denko, Ushio)	24%
Industrials (JSR)	8%
Autos (Toyota, Nissan, Sumitomo Electric)	7%
Energy (Inpex, JAPEX)	4%
JAPANESE DOMESTIC FOCUS	45%
Internet (NTT DoCoMo, Recruit, Rakuten, Nexon)	22%
Financials (Mitsubishi UFJ)	11%
Health Care (Ain, Hogy Medical)	5%
Property	4%
Consumer	3%
GROSS LONG	88%

Currency Position

Japanese yen	88%
US dollar	12%

Source: Platinum

Performance

(compound pa, to 30 June 2016)

	QUARTER	SINCE INCEPTION
PWP - Japan Fund (Class D USD)	0.1%	-0.9%
PWP - Japan Fund (Class A USD)	0.3%	0.2%
MSCI Japan Net Index	1.0%	-5.1%

Source: Platinum and MSCI. Refer to note 1.

Portfolio performance for the quarter was positive as the strong Yen offset weakness in the equity market. Weak performance of economically sensitive holdings and exporters was counter-balanced by strong performance from a range of defensives and stock specific developments.

Changes to the Portfolio

The portfolio remains predominantly invested in Yen-based equities. Toward the end of the quarter, additional equity purchases reduced cash holding to around 12%. As the Yen strengthened, some currency exposure was hedged into USD. All but one of the short positions were closed.

Commentary

Many will remember the peak of the Japanese stock market in late 1989 at a level brushing 40,000. Weary veteran participants in today's market may also remember when small sections of Tokyo property were worth more than the real estate of the entire State of California. The subsequent 27 years saw a 60% nominal (and real) fall in the stock market which provides important context for the current Japanese financial environment.

Moving on from the past, toward the future.

While many aspects of Japan important to investors are likely to change significantly, the future of the country is likely to look similar to the last few decades in many other ways. It is hard to see a major change in the political environment. For the moment, Prime Minister Abe is held in decent regard by the general populace who feel rising employment and experience a moderate Gini coefficient. External risks lead to a focus on continuity. Further, while there have been significant improvements in corporate governance over the

last two decades, it is difficult to see a fundamental adjustment significant enough to change the path of the country. The demographic challenge is well understood and counter-measures will be undertaken.

Negative bond yields around the globe hint at deflation and a need for surety in a complex world. However, in Japan, there is only one way to think of this phenomenon – it's a fixed market as one large buyer has a mandate to acquire 100% of gross government bond issuance regardless of price. There is virtually no price discovery mechanism in the Japanese Government Bond (JGB) market, reminiscent of prior periods when governments around the world have subjugated market forces to their own needs. The second and third order effects of this activity are not yet visible, and definitely not predictable. For the moment, it seems benign, but complex systems often produce unusual Darwinian outcomes. It is certain that this monetary experiment will eventually have a significant influence on the currency, the equity market and price levels. The **Cantillon Effect** is where expansionary monetary policy effects a transfer of purchasing power away from those who hold old money to whoever gets new money. Richard Cantillon was at the heart of the Mississippi Company with John Law. This seems pertinent today where the Japanese, Europeans and others are expanding the money supply at a rapid pace. There is some discussion that China's current efforts dwarf even Japan's rate of 16% of GDP per annum. The alternative of a Debt Jubilee as inscribed on the Liberty Bell in Philadelphia seems attractive but antiquated. The original Liberty Bell cracked due to poor alloying and material selection. Hark Helicopter Money. While the Bank of Japan (BOJ) and other government entities own almost half of the outstanding stock of JGBs, ownership of the various stock market indices is well below 5%. A move toward extending the "fixed price menu" to a wider range of financial assets seems a foregone conclusion.

As expected after a long bear market like the one experienced over recent decades in Japan, the general public and also the wider investing community are wary of the stock market. This is reflected in their asset allocation which is dominated by cash and bonds. Further, cash continues to accumulate in the financial system and thus the loan to deposit ratio keeps falling. The psychology of investors and the madness of crowds is always difficult to predict and timing is awkward, but even a small shift in asset allocation could be very significant for the equity market. Recent discussion of tax rates, especially in the important context of inheritance taxes, indicates that there is a government push toward equities.

Global trade has been tepid post the 2009 financial upset and shows no signs of accelerating. Consequently, competition for market share through competitive currency devaluation dominates the current environment. This is just one aspect of a rapidly evolving global environment buffeting Japan and rippling through its domestic economy. China's transition beyond an industrial phase, India's nascent industrialization, ASEAN's youthful population, Europe's internal tensions and global emerging markets are just some of the significant influences on Japan's future path.

Sumitomo Metal Mining (SMM) is an integrated producer of copper, nickel and gold in addition to owning a diverse materials business. To SMM's great credit, they have been the first in the world to commercialize high pressure acid leach (HPAL) technology at their Coral Bay and Taganito facilities in the Philippines, in contrast to the failed attempts by many esteemed competitors over the last two decades. After Indonesia banned the export of raw nickel ore to China's nickel pig iron producers, it now appears that the newly elected Filipino government might follow a similar path. The current high level of nickel inventories could reduce quickly. Current nickel prices are unsustainable with almost half of the production base losing money on a cash basis. The dynamics of the copper market over the medium-term are attractive. SMM has been working with Panasonic for many years and their NCA (nickel, cobalt, aluminium) material for lithium ion cathodes has been selected as virtually the sole source supplier by Tesla, one of the two leading global electric vehicle companies. SMM also supplies Toyota. SMM owns two of the lowest cost gold mines in the world with combined production of roughly 500,000 ounces per annum. Global gold mine production is falling and demand is surging for a product where there appears to be limited incremental addition to the existing stock. Perhaps gold should be valued as a zero-coupon perpetual bond with a single repayment of undetermined value at a flexible maturity, implying considerable option value. The valuation of SMM is at the lowest level seen for perhaps fifty years.

Valuation dispersion in Japan has been a feature of the market for the last year. It has continued to widen. The valuation gap between defensives versus cyclicals is now wider than the two previous peaks in 1998 and 2008. The valuation gap between a group of the most expensive stocks in the market and the cheapest stocks in the market is approaching previous extremes seen in 1989 and 2000 and the differential is accelerating. The negative interest rates in the bond market are being mirrored in select parts of the equity market.

History shows that mean reversion eventually works to reverse these phenomena. Behavioural finance theory is an inexact discipline.

Quite a number of stocks in the Fund's portfolio have a negative enterprise value after considering their cash and other assets. In a few cases, the companies have more net cash than their current market capitalization in addition to reasonably-positioned operating businesses. Where we can find more of these companies, they will be added to the portfolio in addition to further purchases of current holdings.

While Quantitative Easing and Negative Interest Rate Policies (acronymised as "QE" and "NIRP" respectively) – including J-NIRP – are the current trend within global investment banking circles, the first negative effects could perhaps be surfacing. Money is in oversupply and there is relatively less demand for new loans as seen in falling net interest margins globally. Some interest rate markers are at 5,000 year low interest rates. While this may be seen as a positive for consumers and the like, it perversely has the potential to reduce propensity to lend. Banks are unlikely to proffer loans which don't cover credit risk, let alone operating costs. If the current spiral continues, then the end of the current global business cycle could be approaching from over the horizon.

Outlook

The conundrum we face is that there are more than enough high quality, cheap stocks with attractive medium term prospects available for sale in Japan to fill a diversified portfolio and give adequate consideration to a range of risk metrics. These are the species one expects to encounter on the savannah at the aftermath of a long bear market. The offset is the uncertain global macro environment which is both affecting animal spirits and returning the Yen to its role as a safe haven currency. This combination is awkward for an outward facing trading nation such as Japan despite the best efforts of Abe and Kuroda to change the domestic paradigm. The recent move in the Yen is already somewhat extreme relative to other past shifts and sentiment has reversed. The shift in the Yen has been in concert with an extended period of foreign selling of the equity market. While much of Japan's future path is based on the inherent nature of its people and its history, it looks likely that Abe and Kuroda have enough leeway to navigate. They certainly have the will, even if they are somewhat constrained for the moment. While it is late in the business cycle and many key indicators are trending down, recent readings are positive and suggest reasonable equity returns in contrast to prevailing negative sentiments.

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An umbrella fund with segregated liability between sub-funds
Company Registration Number: 546481

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Notes

1. The Fund's total returns are calculated using its net asset value attributable to the relevant share class (where applicable) and represent its combined income and capital returns for the specified period. The Fund's total returns are pre-tax and are net of fees and expenses (excluding investment performance fees, if any). 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 in the underlying assets of the Fund and other risks associated with investing, investment returns can be negative (particularly in the short-term).

The index represented is the MSCI Japan Net Index (US\$) (the "Index"). Index data has been sourced from MSCI Inc. Index returns include dividends but, unlike the Fund's returns, do not reflect fees or expenses. It should be noted that the Investment Manager does not invest by reference to the weighting of the Index. Underlying assets of the Fund are chosen through the Investment Manager's individual stock selection process and, as a result, holdings vary considerably to the make-up of the Index. The Index is provided as a reference only.

The portfolio inception dates for each active share class of the Fund are as follows:

Class D USD (Accumulating) (ISIN: IE00BYRGRJ67): 16 November 2015

Class A USD (Accumulating) (ISIN: IE00BYRGRF20): 11 January 2016

The inception date for the purpose of calculating Index returns, as contained in this publication, is taken to be the inception date of Class D of the Fund.

2. Invested position represents the exposure of physical holdings and long stock derivatives.

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