Platinum Japan Fund

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Overview

- The Japanese electrical power sector looks likely to be a key growth sector over the next few years as Japan builds out the infrastructure required to meet its growing energy needs – needs that notably come from new semiconductor plants and datacenters. Our holding in **Hitachi** is partly based on this growth outlook, but also on Hitachi's success in trimming down and refocusing its businesses and operating structures.
- Corporate governance reforms, positive news around the return of moderate inflation, rising business investment and restructuring within Japanese corporates have boosted Japanese returns over the past few years. Navigating currency devaluation risks appears to be one of the administration's key challenges for the future.

Performance

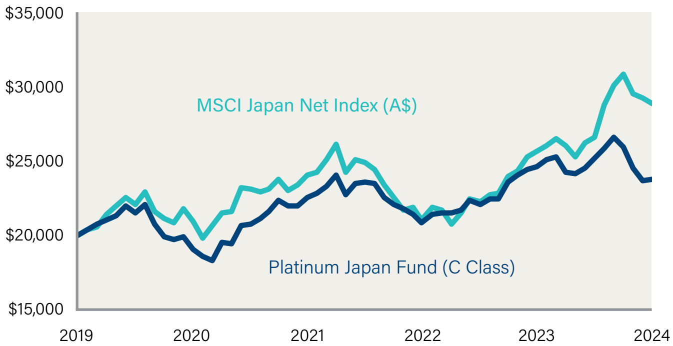
compound p.a.+, to 30 June 2024

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum Japan Fund*	-8%	-3%	2%	4%	12%
MSCI Japan Index^	-6%	13%	6%	8%	4%

+ Excludes quarterly performance.
* C Class – standard fee option. Inception date: 30 June 1998.
After fees and costs, before tax, and assuming reinvestment of distributions.
^ Index returns are those of the MSCI Japan Net Index in AUD.
Source: Platinum Investment Management Limited, FactSet Research Systems.
Historical performance is not a reliable indicator of future performance.
See note 1, page 5. Numerical figures have been subject to rounding.

Value of $20,000 invested over five years

30 June 2019 to 30 June 2024



After fees and costs, before tax, and assuming reinvestment of distributions.
Historical performance is not a reliable indicator of future performance.
Source: Platinum Investment Management Limited, FactSet Research Systems.
See notes 1 & 2, page 5.

Japanese equities took a breather in the June quarter, with the MSCI Japan Index down -6% in $AUD terms, though up 3% in Yen terms.

Key contributors to the portfolio were **MS&AD** Insurance (+35%), **Hitachi** (+30%) and the conglomerate, **Kurabo Industries** (+40%).

Key detractors were **Shift** (-39%), **Toyota Motor** (down over 10%) and **Toyota Industries** (-13%).

We continued to make portfolio adjustments during the quarter, exiting several smaller positions and initiating holdings in some opportunities we believe are attractively priced. These are companies with strong business capabilities who are focused on improving balance sheet efficiency and their competitive market positions.

MUFG is Japan's premier megabank. We are positive on the outlook for loan spreads as the Bank of Japan (BOJ) slowly exits from ultra-easy monetary policy. For banks, a steepening yield curve (where long-term interest rates are higher than short) boosts interest income. Further, Japan's corporate restructuring now creates higher-margin lending opportunities for banks such as M&A transactions, LBO, MBOs etc.[1] Meanwhile economic growth and strong real estate markets are underpinning loan demand. We think this growth could be further augmented as the corporate sector increases its investment activity.

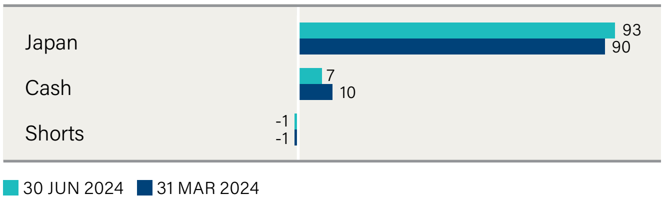
Murata is the global leader in Multi-Layer Ceramic Capacitors (MLCCs). MLCCs act as 'dams' that charge and discharge electricity and are crucial components in electric devices, smartphones and PCs. The latest smartphones can have over 1,000 MLCCs, while EVs and AI servers can have 10,000 or more. Murata has half the global market and is highly profitable. MLCCs have been in oversupply for the past 18-24 months on slower auto, PC & smartphone shipments. This saw prices falling and weaker capacity utilisation rates led to higher inventories and lower margins. We expect a potential demand upcycle for AI-enabled hardware to result in higher MLCC volumes and prices. The stock has underperformed the market since 2021, providing an attractive entry opportunity.

We reinitiated a position in **Unicharm** given the strength of its brand and signs that channel inventory in the important China feminine care category has improved. Recent earnings have been stronger than expected, underscoring the value of their brand. Pricing power and growth across several markets continue to impress. We expect structural growth for disposable hygiene to continue with strong margins due to innovation, premiumisation and the company's shift from low margin baby diapers to the higher margin 'femcare', adult incontinence and petcare categories.

Fast Retailing is the owner of **UNIQLO**, a clothing brand with well designed, high quality basics with built-in fabric functionality (eg Airism, Heattech). In many ways UNIQLO is the Toyota of the apparel industry. We think their mid/value price points appeals to a broad range of consumers globally and they have a highly efficient supply chain. UNIQLO has quietly become a genuinely global brand in a highly fragmented industry and its rising market share implies further growth. Their market presence is higher in Japan, China and Asia, but Fast is now concentrating on building out their North America and Europe businesses.

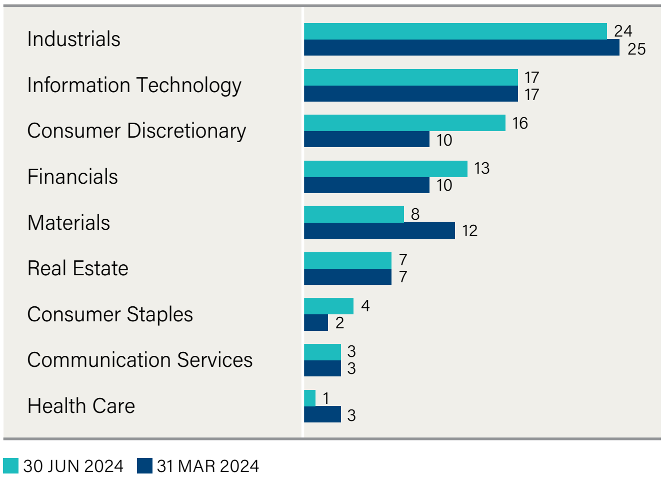
1 Mergers and Acquisitions, Leveraged Buyouts, Management Buyouts.

Disposition of Assets %



See note 3, page 5. Numerical figures have been subject to rounding.
Source: Platinum Investment Management Limited.

Net Sector Exposures %



See note 4, page 5. Numerical figures have been subject to rounding.
Source: Platinum Investment Management Limited.

Top 10 Holdings

COMPANY	COUNTRY	INDUSTRY	WEIGHT
Toyo Seikan Group	Japan	Materials	5.0%
Taisei Corp	Japan	Industrials	4.6%
Hitachi Ltd	Japan	Industrials	4.6%
GMO Payment Gateway Inc	Japan	Financials	4.4%
Mitsubishi UFJ Financial	Japan	Financials	4.4%
MS&AD Insurance Group	Japan	Financials	4.3%
Sony Corp	Japan	Cons Discretionary	4.3%
Toyota Motor Corp	Japan	Cons Discretionary	3.9%
Keyence Corp	Japan	Info Technology	3.8%
Toyota Industries Corp	Japan	Industrials	3.8%

As at 30 June 2024. See note 5, page 5.
Source: Platinum Investment Management Limited.

Commentary – Who has the power?

Japan's demand for electricity has been declining steadily since 2007, which is perhaps understandable given Japan's post-industrial economy, improving efficiency and steadily declining population.

Japan's Organization for Cross-Regional Coordination of Transmission Operators (OCCTO), takes data from regional electricity distributors across Japan to issue forecasts for long term electricity demand every year. Unsurprisingly, projections of continued decline in demand have been the norm for several years. Yet in January this year, the report issued a surprising forecast of rising electricity demand for Japan over the next decade. The reason is the emergence of new industrial demand for energy – notably from new semiconductor plants and datacenters.

There is increasing realisation that Japan's aging electricity transmission and distribution grid, constructed decades ago and approaching their end of useable life, are not up to the task of supplying this emerging power demand.

This means a new wave of grid infrastructure modernisation and investment is urgently required. Electrical utilities are already increasing grid capex spending, implying a sustained boom ahead with several years of demand growth for grid equipment such as transformers, cables and transmission lines, substations, interconnection facilities etc.

This is one of the reasons we own Hitachi, a company uniquely positioned to benefit in both Japan and globally through its strong position in supply of critical power infrastructure.

Hitachi has also been undertaking structural reforms for over a decade. Its core competitive positions had been steadily eroded by more agile competitors, it was saddled with excessive headcount and debt, had an overly diversified, unfocused business portfolio and suffered four years of consecutive net losses from 2007-2010.

Under the leadership of then CEO Nishimura, Hitachi then began a series of reforms, actively divesting several non-core businesses while acquiring complementary businesses such as the well-timed ABB Power Grids purchase in 2020 (completed in 2022) and GlobalLogic in 2021. Hitachi is now a lean, competitive portfolio of businesses benefiting from increased IT spending and grid modernisation.

Outlook

The Japanese market has enjoyed a strong year and is now back on the radar screens of global investors. We have previously written of the corporate governance reforms, broadening inflation, rising business investment, increasing shareholder returns and portfolio restructuring as key drivers of this reappraisal.

We believe these changes are a watershed, creating a positive environment for investing in Japan and we have aligned the portfolio in recognition of this shift. However, one concern remains a front-of-mind issue for the market now that inflation has returned. How and to what degree will any Bank of Japan (BOJ) exit from ultra-accommodative monetary policy undermine equity gains?

So far, with new Governor Ueda, the BOJ still appears to be reluctant to raise rates as the economy still has areas of weakness. There are already inflationary pressures emerging and increased pressure on the BOJ to raise rates yet we think the bank is likely to be more measured than expected. During the quarter, we increased our currency exposure to USD and AUD to incorporate this view.

The drop in the value of the Yen in recent months appears to be an outcome of the BOJ's stance and policy makers are beginning to express concerns. While welcomed by tourists, a weak Yen also has the effect of raising imported inflation, thus suppressing real wage growth for Japanese households (and lowering dollar based returns for foreign investors). We have already seen the Ministry of Finance undertake unilateral currency intervention in April and May, but this has only temporarily slowed the currency's decline. Conversely, any tightening of monetary policy by the BOJ could see the Yen strengthen as carry-trades unwind and interest rate differentials narrow. This could have negative knock-on effects on the stockmarket and economic activity.

While the Yen is objectively "cheap" (on Purchasing Power Parity analysis) we remain circumspect. The prevailing wisdom is that the interest rate differential between Japan and other countries has driven down the value of the Yen. We believe there are structural reasons for this weakness. For example, capital outflows and declining Balance of Payments surpluses in goods and services as Japanese households invest in higher returning foreign markets (particularly the US). These factors could be contributing to the recent breakdown in one of the most reliable correlations in financial markets – the link between the spread on the 10-year Japanese Government Bond vs US Treasuries and the USD/JPY exchange rate.

There is little doubt a weak Yen has helped lift exporter earnings and, given the high weighting of such companies in the index, the Japanese stock market overall. How long this period of Yen weakness continues is uncertain. We do not think it is the sole driver of market performance and we remain upbeat.

Notes

Unless otherwise specified, all references to "Platinum" in this report are references to Platinum Investment Management Limited (ABN 25 063 565 006, AFSL 221935).

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

1. Fund returns are calculated by Platinum using the net asset value unit price (i.e. excluding the buy/sell spread) of the stated unit class and represent the combined income and capital returns over the specified period. Fund returns are net of fees and costs, pre-tax, and assume the reinvestment of distributions. The MSCI index returns are in AUD, are inclusive of net official dividends, but do not reflect fees or expenses. [The gross MSCI index was used prior to 31/12/98]. MSCI index returns are sourced from FactSet Research Systems. Platinum does not invest by reference to the weightings of the specified MSCI index. As a result, the Fund's holdings may vary considerably to the make-up of the specified MSCI index. MSCI index returns are provided as a reference only. The investment returns shown are historical and no warranty is 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.
2. The investment returns depicted in the graph are cumulative on A$20,000 invested in C Class (standard fee option) of the Fund over the specified period relative to the specified MSCI index in AUD.
3. The geographic disposition of assets (i.e. other than "cash" and "shorts") shows the Fund's exposures to the relevant countries/regions through its long securities positions and long securities/index derivative positions, as a percentage of its portfolio market value. Country classifications for securities reflect Bloomberg's "country of risk" designations. "Shorts" show the Fund's exposure to its short securities positions and short securities/index derivative positions, as a percentage of its portfolio market value. "Cash" in this table includes cash at bank, cash payables and receivables and cash exposures through derivative transactions.
4. The table shows the Fund's net exposures to the relevant sectors through its long and short securities positions and long and short securities/index derivative positions, as a percentage of its portfolio market value. Index positions (whether through ETFs or derivatives) are only included under the relevant sector if they are sector specific, otherwise they are included under "Other".
5. The table shows the Fund's top ten positions as a percentage of its portfolio market value taking into account its long securities positions and long securities derivative positions.

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