

# PLATINUM EUROPEAN FUND



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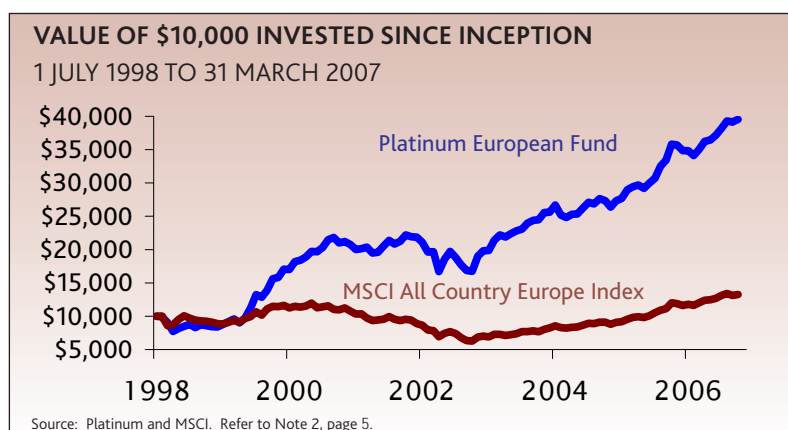
## PERFORMANCE

### Marginal headway amidst swirling conditions

European markets exhibited considerable variability in the last few months, with the continuing rally at the start of the year swiftly reversed in late February, before a wary resumption in the last few weeks left markets marginally ahead for the quarter. Predictably, small stocks and cyclicals/basic materials bore the brunt of the setback (they had, after all led the charge); more surprisingly perhaps many of these areas participated in the March recovery – often a change of leadership is evident at such times.

For the quarter overall, strong areas of the market were autos (+17%, with Porsche continuing to increase its stake in VW, and Daimler (Mercedes) receiving strong bid indications in the planned sale of its problematic Chrysler division), auto parts (+13%) and food retail (+12% reflecting activity on Carrefour's share register, as well as bid speculation over Sainsbury of the UK). Computer software (-8%, including SAP -17%) was the only sector to record a notable decline for the period. Overall European markets were +2.5% for the quarter, a stronger Australian dollar versus the European currencies gave an MSCI A\$ return of +1.2% for the quarter.

The Platinum European Fund progressed 3.6% for the three months to 31 March 2007, with good performances from several “mid-sized” (up to euro 2bn market capitalisation) German companies in the portfolio: TV group Premiere (+28%), DIY retailer Hornbach (+27%), and financial advisory group MLP (+25%). The Fund has about 2.5% in each of these stocks as we write. Those good performances were partly offset by losses in Alcatel (-19%) which is a small (sub 1%) position today. By implication, a lot of the portfolio was little changed over the quarter (although this end result masks some turbulence en route!).



## COMMENTARY

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### Europe company meetings: TV, advertising and the power of the sun

We had fifty meetings in Europe over the last two weeks of March, focusing on several areas including businesses in the television/advertising/market research area, and also in the photovoltaic (solar power) industry. In general, economic conditions in Europe seem roughly as we have intimated in recent quarters: gathering evidence of consumer growth and confidence in Germany, while France is better than the commentators suggest, the habitual pre-election introspection notwithstanding! The UK remains subdued, although the slightly alarming inflation data does seem to be a coincidence of energy prices and exchange rate effects which should moderate in the coming months. A nice surprise was Italy, where domestic conditions seem okay despite the calamitous loss of competitiveness in recent years.

Also, as we have suggested for some time, while overall stock market conditions are at a worrying level of speculative excitement, we are still finding a number of prospective investments in selected areas of the market.

Before readers panic that we have abandoned our **neglect** approach to stock analysis, please note that the visits to the **solar companies**, an area of feverish stock market excitement, were aimed at readying ourselves for the inevitable periods of weakness and disillusion that will come in this promising but still subsidy-dependent (and thus vulnerable) industry. In addition, we have a couple of ideas *around* the solar companies which are not participating in the share price action, and these needed to be assessed (one of these has been added to the Fund in recent days).

**Solar.** The overall task facing the solar industry is to develop the product to the point where it is competitive without subsidy against current forms of electricity. While it is clear that the true costs of coal-sourced electricity are greater (possibly calamitously greater) than today's market price, it

is equally clear that solar will remain marginal until it can compete unsubsidised with fossil fuels. Until then only subsidy or individual preference (for those willing to ignore the extra cost) supports the solar industry.

But in the case of Germany, whose government effectively decided to industrialise the solar research effort, what a subsidy! In recent years, a system of high "feed-in tariffs" (ie. guaranteed high prices for solar electricity fed into the grid) has ensured that demand far exceeds supply for solar panels. In fact the system quickly developed to the stage where installation companies merely needed a farmer's signature to install a system (on part of the farm or on the shed roof) with a guaranteed rate of return over 15-20 years: time was/is of the essence, as the feed-in tariff automatically declines for panels installed as each year passes. Indeed such is the scale of uptake, that the government may increase to -10% from -5% the annual decline of the feed-in tariff. Note that for example the 2005 installations, however, get the 2005 feed-in price for the duration of the contract, so that there is no risk to those already installed.

This system, though, has had several interesting effects: 1) It has elevated not-terribly-sunny Germany above also-not-that-sunny Japan to the top of the solar electricity generation league – arguably a perverse outcome. 2) It has made Germany home to four of the top six or eight companies in the industry: by exploiting the "learning-is-in-the-doing" truism, this industry policy has been a remarkable success: there are literally thousands of jobs in the German solar industry today. 3) The declining tariff regime (not to mention the need to offset the silicon price) cleverly requires the industry to lower its costs constantly to stay "competitive" with other electricity sources. In this regard the solar industry reckons it is running at a 17% "learning curve" effect (ie. each doubling of output decreases costs by 17%). In addition to that, costs decline further with the scale economies of greater volume. These measures show how effectively the German government has short-circuited (!) the

development time of the industry by telescoping the volume and network learning effect. There is now feverish competition for engineers etc in the industry.

However, the rush caused by the (declining) subsidy system has meant that demand has exceeded supply, and the key bottleneck has been in the availability of “solar-grade” (ie. extremely pure, if not quite semi-conductor purity) silicon. Thus the big money has been made in the “upstream” (silicon) part of a complex production process, and also by those further along the chain who were lucky/clever enough to have locked in silicon supply at reasonable prices (like euro 40-50/kg – the spot price today is over euro 200/kg). This bottleneck has in turn accelerated the pace of development of less silicon-intensive techniques, for example the logically appealing “thin film” technologies including amorphous silicon on glass (ie. by deposition). By comparison the standard technique of “growing” silicon blocks and then slicing them into ever thinner wafers wastes a lot of silicon in the cutting.

However, the crucial metric of energy efficiency (% of received sunlight converted to electricity) is at around 17% for “traditional” wafer production (28-29% is apparently the theoretical maximum), far above the thin film techniques which are currently stuck below 10%. Of course the key is the cost of a solar panel *relative* to its efficiency, and a cheap lower efficiency solution is perfectly okay for a farmer's paddock, while an urban roof requires high efficiency panels given the space constraint. Other developments include breakthroughs in (relatively abundant) metallurgical silicon (once considerably purified), so that perhaps a 50-50 mix of metallurgical and solar grade silicon may ease the supply constraint – the catch at the moment is the energy intensity of the purification process of the metallurgical grade material!

The holy grail, as the industry currently sees it, is to halve the electricity generation cost of solar power from today's euro 25cents/kWh (assuming 1,800 hours of sun pa), to euro 12cents/kWh, at which point it is competitive with retail electricity

prices. Note that one of the advantages of solar power is that the retail power price (not the wholesale price) is the relevant benchmark: producing energy where it is used removes the need for the costs/losses/maintenance etc of transmission and distribution networks.

From an investment perspective, it became clear as we met the various players in Norway and across Germany, that the unavailability of silicon had led several of the wafer, cell and module makers to panic and sign 10-year fixed price supply deals with the (relatively powerful) silicon companies, including 30%+ down payments to secure the contracts! The cell/module companies have in turn tried to sign balancing output agreements with their customers, but it is clear where the power lies (and the downstream customers may not honour the contracts if prices are much lower in five years' time).

The point of all this is that under a scenario, for example, of oil prices falling back to \$40/bbl, and the internet-bubble-esque enthusiasm for renewable energy plays leaving the stock markets, we will see dramatic declines in solar company share prices (today they are extravagant multiples of handsome profits), just as we saw a few years ago with the wind power companies. We now have a reasonable idea of which companies to invest in given the chance, because of course the development of the technology will be ongoing and eventually it will be viable (at least in sunny countries that care about emissions!).

**IV.** We saw leading free-to-air TV companies in the UK, France and Italy. These companies continue to be penalised in the stock market by investor concerns over audience fragmentation, delivery technology changes, and losses of viewers and advertising revenues to the Internet. While each of these concerns is well-founded, they all ignore the principle that leading channels remain the single best way to reach a broad audience, and indeed retain an advertising price premium over smaller TV stations. This premium exists for the simple reason that with effective ad viewing of 4-7 times (for a given advertisement), there is little point in continually “hitting” the same tightly

defined but small audience (say 1 or 2% of viewers) on a highly specific new theme channel, while a broad channel with 30% audience share gives far more efficient spread.

More interesting perhaps is that in a world of record corporate profitability, vigorous brand competition and solid consumer spending, there has been limited evidence of an advertising “cycle” in western Europe. While this may reflect the concerns over the medium outlined above, it at least provides comfort that this “cyclical” industry is not stretched like many of the capital goods and materials sectors.

We have nearly 10% of the Fund invested in media companies in Europe, and a further 6% in advertising and market research businesses.

### Prospects and positioning

As repeatedly stated, the uncritical enthusiasm for acquisitions leaves us with nagging worries over the broad market. However, in building and managing a portfolio “stock by stock”, it is clear that we are still finding reasonably priced investments in Europe, so that for the moment hope remains ascendant over despair.

We are excited to see the spreading consumer strength in Germany: our long held DIY (hardware) retail operator in Germany, Hornbach, reported strong sales through the usually dull winter months, and our main concern is that Germany has many world beating exporters listed on the stock market, but not so many ways to play the domestic consumer recovery.

Elsewhere, the “technology” shares such as Ericsson, and now perhaps SAP, look modestly priced given their market positions and growth prospects in the coming years. While the definition is inevitably blurred, the Fund has 10-12% in the technology area as we write. Please note also that Ericsson and SAP are a subset of a wider phenomenon currently prevailing: the very largest companies (by market capitalisation) are now clearly the worst performers – worldwide, and especially in Europe (refer chart on page 3). This situation is highly appealing to us as we look for investments away from the mainstream takeover speculation zone (say up to euro 20bn market capitalisation), and indeed with investments also in Siemens, Carrefour, Vivendi etc the portfolio has been steadily tilted toward these modestly rated giants.

The currency exposures are little changed in recent months: 36% of the Fund is exposed to the Australian dollar (which is slowly gaining against the Europeans), while the exposure to the euro is 50%, and the remainder is in the Scandinavian currencies and the Pound Sterling (for the first time in quite a while the Fund holds no Swiss stocks!). Including (predominantly German DAX Index future) shorts, and put options, the Platinum European Fund was 68% net invested at the end of March 2007.

#### BREAKDOWN OF FUND'S LONG INVESTMENTS BY INDUSTRY

CATEGORIES	EXAMPLES OF STOCKS	MAR 2007	DEC 2006
TECH/MEDIA	INFINEON, ERICSSON	24%	26%
CHEMICALS/MATERIALS	UPM, SHELL	17%	18%
CAPITAL GOODS	SIEMENS, RIETER, METSO	15%	17%
CONSUMER/RETAIL	HENKEL, HORNACH, CARREFOUR	16%	14%
FINANCIALS	CREDIT AGRICOLE	5%	5%
PHARMACEUTICAL/BIOTECHNOLOGY	NOVOZYMES, EUROFINS	3%	4%
MISCELLANEOUS SERVICES	GFK	4%	2%

Source: Platinum

## NOTES

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1. The investment returns are calculated using the Fund's unit price and represent the combined income and capital return for the specific period. They are net of fees and costs (excluding the buy-sell spread and any investment performance fee payable), are pre-tax and assume the reinvestment of distributions. The investment returns shown are historical and no warranty can be given for future performance. You should be aware that past performance is not a reliable indicator of future performance. Due to the volatility of underlying assets of the Funds and other risk factors associated with investing, investment returns can be negative (particularly in the short-term).

2. The investment returns depicted in the graphs are cumulative on A\$10,000 invested in the relevant Fund since inception relative to their Index (in A\$) as per below:

Platinum International Fund:  
Inception 1 May 1995, MSCI All Country World Net Index

Platinum Unhedged Fund:  
Inception 31 January 2005, MSCI All Country World Net Index

Platinum Asia Fund:  
Inception 3 March 2003, MSCI All Country Asia ex Japan Net Index

Platinum European Fund:  
Inception 1 July 1998, MSCI All Country Europe Net Index

Platinum Japan Fund:  
Inception 1 July 1998, MSCI Japan Net Index

Platinum International Brands Fund:  
Inception 18 May 2000, MSCI All Country World Net Index

Platinum International Health Care Fund:  
Inception 10 November 2003, MSCI All Country World Health Care Net Index

Platinum International Technology Fund:  
Inception 18 May 2000, MSCI All Country World Information Technology Index

(nb. the gross MSCI Index was used prior to 31 December 1998 as the net MSCI Index did not exist).

The investment returns are calculated using the Fund's unit price. They are net of fees and costs (excluding the buy-sell spread and any investment performance fee payable), pre-tax and assume the reinvestment of distributions. It should be noted that Platinum does not invest by reference to the weightings of the Index. Underlying assets are chosen through Platinum's individual stock selection process and as a result holdings will vary considerably to the make-up of the Index. The Index is provided as a reference only.

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Before making any investment decision you need to consider (with your financial adviser) your particular investment needs, objectives and financial circumstances. You should consider the PDS in deciding whether to acquire, or continue to hold, units in the Funds.

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