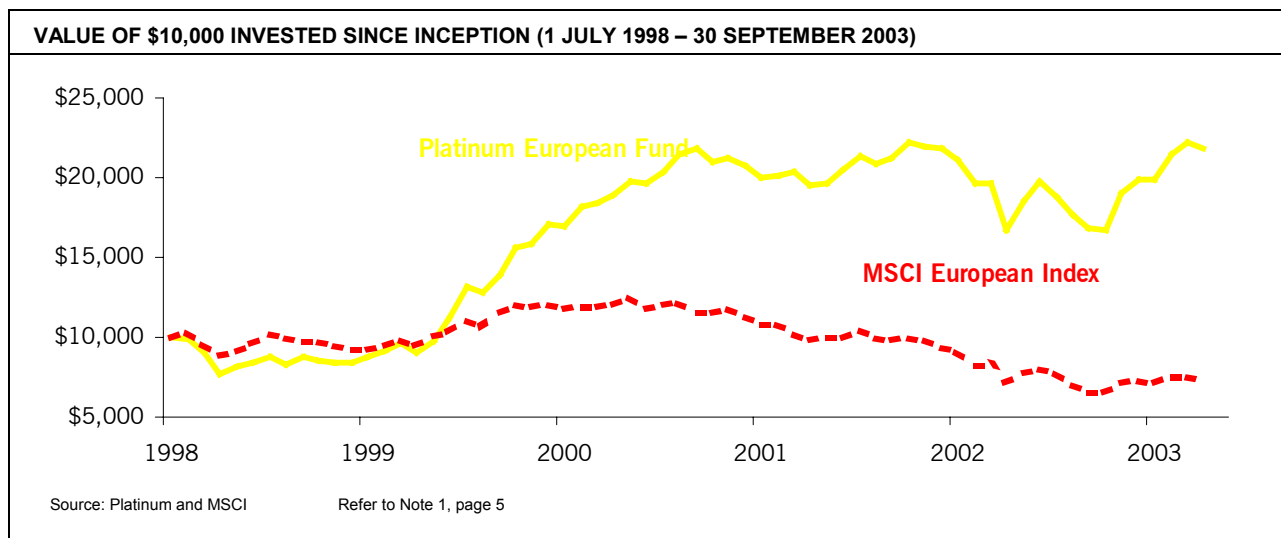


Platinum European Fund

Performance

REDEMPTION PRICE: \$1.6368



Surging global freight rates, both for container vessels and bulk carriers, emphasise that while western world GDP figures paint a mixed picture, there is activity aplenty, including quickly changing regional production patterns. The peculiar balance of savings-rich Asian (and continental European) countries supporting the engaged consumers of US/UK/Australia continues to be predicated upon the paradox of managed currencies (Asia) amidst “free market” globalisation. The old world of (continental) western Europe sits somewhat bewildered in the middle of the chaos – dull rates of domestic economic growth continue, with strengthening European currencies and intermittent efforts to reform labour markets. Interest rates are low – though not as low as the US and Japan – and are most likely heading lower.

The three months to 30 September 2003 have seen little direction in share prices overall in Europe – the MSCI advanced 10-12% from its end-June lows, before giving most of the gains back to finish

marginally (0.5%) positive for the quarter. In fact most stocks, and most sectors were up 5% or more, but a dull (flat to -5%) showing by the (index-heavy) defensive sectors of media, electricity utilities, oil companies, banks, and pharmaceuticals explains the flat overall result. A marginally weaker A\$ against the European currencies left the MSCI Europe at +3% for the quarter.

The Platinum European Fund returned 10% for the quarter. Good performances from Infineon (memory chips, +33% this quarter), Ericsson (+31%), SGS Surveillance (inspection and testing +30%), Schindler (lifts, +30%), Siemens (+20%), and Heidelberg Cement (+40% vs our entry price in July), offset much of the portfolio which made little progress over the quarter. The three short stock positions in the fund subtracted from performance; we also initiated a 10% hedge in the German DAX when we feared the market was tiring, but subsequently removed it (incurring a small loss from the exercise).

Commentary

Strong currencies, subdued economies – what sort of investments in Europe might work?

Notwithstanding widespread optimism that the US economy can “recover” (a sharp US manufacturing recession occurred while consumers continued the spending rampage), it seems that strong European currencies will make for subdued growth on the continent. Since the February/March 2003 lows,

cyclical (ie heavily economically sensitive) companies have seen strong share prices, such that most of their valuations are at least consistent with

buoyant economies. Technology companies have in a way become the most “cyclical” of all – to the extent that consumption now dominates western economies, the “investment” component of the economy represents an assessment by firms that the

consumer is ready for more! Thus a decision to add capacity to a mobile phone network, or to upgrade the software in a retail chain, are arguably more than ever pro-cyclical events - and these are the decisions which drive the fortunes of the big technology suppliers. From admittedly desperate levels, the

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technology stocks in Europe have, in the last 11 months, rebounded a very long way. So where else to look if not the “cyclicals”?

The classic “defensives” are the food retailers, the branded goods companies, pharmaceuticals, and utilities. These will in general benefit from low (and falling?) interest rates – “annuity streams” being worth more at lower discount rates. However the offset to this is the large US\$ exposure of the branded goods companies – consider L’Oreal’s huge US (and Asian) hair colorants market share, or Heineken’s position in the global premium beer segment. And of course the untiring efforts of the European drug companies to build their US businesses (where pricing is more generous and demand robust) means the weak US\$ weighs on their results.

Without wishing to resort to “last man standing” theme generation, the reason for this sort of categorisation is to cover the risk that (some) valuations are pushed up again to surprisingly high levels. Why? Well why are there valuation bubbles in many western world property markets? Cheap money, combined with confidence (or hope or greed) seems to be having a more profound effect than could have been predicted. Indebted consumers not only do not pay down their mortgage – they add to it! Debt is cheap to service, so instead of targeting an amount of debt, people seem to be comfortable targeting an amount of interest paid. Assets (and further consumption) are the flip side of this coin. Hence the property bubble – but on this logic, why not another share price bubble? This could happen if the US in particular continues to be faced with low interest rates courtesy of the ongoing relocation of global manufacturing to China. And if there is a bubble in (defensive) US stocks, then there will be in parts of the European market – hence the need to imagine where money directed to shares may flow when lots of sectors are being tactically excluded. Thus domestically-focused defensive businesses (not least utilities) may be one place to be invested. Our positions in Veolia Environment (based in Paris) – the world’s largest water utility, and German detergent powerhouse Henkel make sense (anyway, but perhaps especially with the above scenario in mind).

Of course there are other areas where structural changes and modest starting valuations overcome currency and economic headwinds. We are investigating the merits of the various European (and global) oil companies – obviously the majors themselves, but also the exploration technology,

extraction and storage equipment companies, gas to liquids opportunities etc. Our starting point is that reserve replenishment is becoming more costly and more difficult (in fact is not really being achieved by the majors). Thus even with unrealistically modest

assumptions about energy demand growth in China and India, the oil price may well be US\$10-15 higher in the coming 3-5 years than today’s US\$30/barrel (rather than US\$10-15 lower as many commentators forecast). More immediately, it is interesting that over the weekend President Bush has asked the Congress for a further US\$87bn for the “rebuilding” of Iraq – a fairly direct concession that Iraqi oil will not flow soon enough to pay the bills as originally intended.

More interesting still is the question of the natural gas (and by extension, LNG and gas-to-liquids) businesses as the US and China become huge net importers of gas, to power their gas-fired electricity plants. Shell has been slowly shifting its focus from oil to gas over the last decade; British Gas is a more focused play on various aspects of the natural gas industry. We shall be visiting these companies during a forthcoming trip to Europe, as well as many peripheral companies to try to round out the investment theme.

Germany – no excitement yet in the property market, but the cement companies are seeing something...

German house prices rose during the “reunification boom” a decade ago. Since then they have stagnated, and the property bubble seen in Australia, US, UK, Netherlands etc is certainly one “problem” not facing Germany today. Construction more generally has had a miserable ten years in Europe’s largest economy, with high profile bankruptcies, hundreds of thousands of job losses, and a forlorn cement sector.

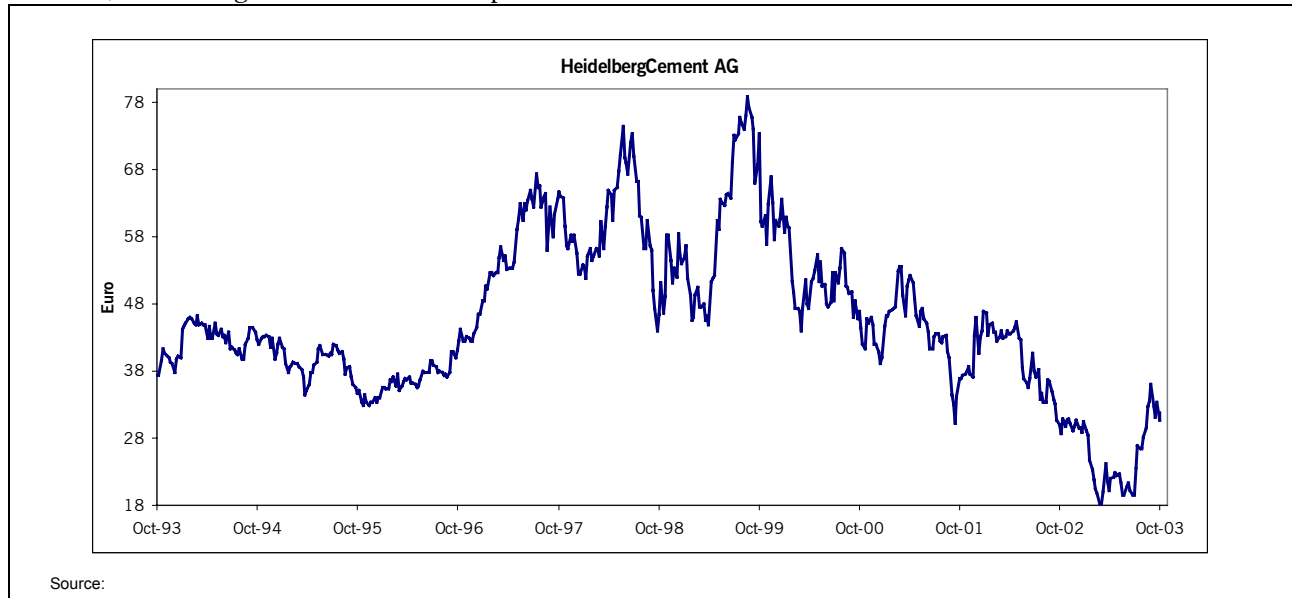
Aside from the special cases of China and India, Germany has among the most fragmented cement industries in the world: in the year 2000 thirty companies supplied a product which is, in many industrialised countries, supplied by 3-5 players. None of the companies has been making an operating profit (ie even before financing charges) in Germany in recent years, and the huge fines (E250mn for HeidelbergCement alone) which resulted from the cartel investigation of 2001 were a bitter outcome for the industry. (In fact this investigation revolved around attempts to keep imports out rather than actual price fixing). Production capacity peaked in 2001 (!) at 57mn tonnes; actual production peaked in 1999 at under 38mn tonnes (Germany was a net importer of over 2mn tonnes in 1997, this year it will net export about that amount). The average capacity utilisation rate has thus fallen from a low 72% in 1998, to lethal levels around 58% since 2000.

Prices have halved in the last 18 months, from E70 (which tends to be the general European “regional” price) to E30-35 as the industry has decided to consolidate the hard way. Progress has been made with 21 players left standing today, and production capacity is down over 10% to 51mn tonnes. In

recent weeks it has become clear that Heidelberg and Holcim (the old Swiss-based Holderbank) are

price increases and other players are tending to follow the lead. More interesting is that the various acquisitions Heidelberg has made in the last two years (especially if the RMC acquisition proceeds) transforms the German market into one where at least in the key regions, there is a reasonable level of concentration.

negotiating to take RMC out of the market. In addition, Heidelberg has announced E20 per tonne



Understandably, after years of horror, commentators have tended to take a cynical view of industry developments in Germany, and of Heidelberg's efforts in particular. We would make the point that as usual it is a question of price, and the shares of the company were so low by June/July of this year that the changes in the industry attracted us to the stock. We paid E23 (note that the broad stock market recovery had largely taken place in Germany by this point in early July), and a few months later the price

is E10 higher and industry conditions continue to slowly improve.

It would be better to be able to report that current cement demand in Germany implies a more general economic pick-up; this is not yet the case but clearly Heidelberg is seeing enough signs of some demand improvement to execute its grand plan now (its balance sheet is stretched enough that it does not have the luxury of being wrong by five or ten years).

Changes to the Portfolio

Major new additions to the portfolio in recent months include (old friend) *Epcos*, a German passive components maker (similar to its ex-Siemens sister company Infineon, this electronics business became very cheap over the last twelve months as the German stock market appeared to temporarily ignore the signals coming from Japan and Korea on these areas). *Heidelberg Cement* was added as mentioned; we also bought a position in *Rieter*, the world leader in very high speed textile spinning machines. The textile industry – having migrated steadily around the world for decades – is currently in China and India. Our thesis is that as those countries are producing for export (and competition is unimaginable) they are, perversely given their labour

cost advantage, forced to invest in the top quality (automated) machines. This fact, and the behaviour of a distressed seller of Rieter shares who had pushed the stock down below fair value, gave us our investment. However after only a 20-25% appreciation we are lightening the position as in fact the copying skills of the Chinese are such that Rieter was horrified to see that even their *name and logo* were faithfully reproduced on local machines at a recent Chinese trade show. This begs the more general question of the practical value of patent protection in today's world, and hence some of the high valuations which attach to many western world "technology" businesses.

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BREAKDOWN BY INDUSTRY			
Categories	Examples of Stocks	Sep 2003	Jun 2003
Miscellaneous Services	Hagemeyer, SGS Surveillance	18%	14%
Capital Goods	Océ, Schindler, Siemens	15%	12%
Retail	Hornbach, Douglas	11%	7%
Pharmaceutical/Biotechnology	Novozymes, Novartis	10%	16%
Financials	Alleanza	9%	5%
Chemicals/Materials	Linde, Merck KGaA	8%	7%
Consumer	Adidas, Michelin	7%	9%
Tech/Media	Ericsson, Infineon Tech	7%	10%

Source: Platinum

We have also invested in logistics/transport giant (and post office!) *Deutsche Post*, German spectacle (and contact lens) retailer *Fielmann*, and in *British Gas*. These various acquisitions were funded by reducing the positions in many of the currency sensitive cyclicals, in particular in Germany and Switzerland, which have performed very strongly since March.

The Platinum European Fund is currently 85% long, 15% cash and 3% short for a net exposure of 82% in European equities. The A\$/Euro exchange rate has fluctuated mainly between E55c-E60c for the last three years; we took advantage of one of the moves to the high end of this range to reduce the A\$ hedge from 54% in June to 31% today, with 46% of the fund in Euros and the remaining 23% in various other European currencies.

Toby Harrop
Portfolio Manager

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

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2. NOTES

- (a) The returns represent the combined income and capital return for the specified period. They have been calculated using withdrawal prices, after taking into account management fees (excluding any performance fees), pre-tax, and assuming reinvestment of distributions. The returns shown represent past returns of the Fund only. 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, returns can be negative (particularly in the short-term).
- (b) The investment returns depicted in this graph are cumulative on A\$10,000 invested in the Fund since Inception relative to the its index(in A\$) as per below;

Platinum European Fund:

MSCI Europe Accumulation Net Return Index in A\$. The inception date of the fund was 1 July 1998.

The investment return in the Fund is calculated using withdrawal prices, after taking into account management fees (excluding performance fees), pre-tax and assuming 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 Index. The Index is provided as a reference only.