Platinum European Fund

Clay Smolinski Portfolio Manager

Nik Dvornak Portfolio Manager

Performance

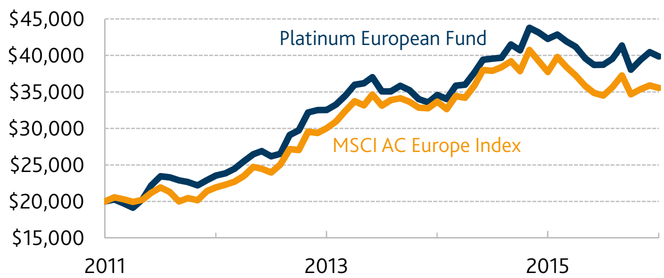
(compound pa, to 30 September 2016)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum European Fund	5%	-6%	7%	15%	11%
MSCI AC Europe Index	3%	-6%	6%	12%	2%

Source: Platinum and MSCI. Refer to note 1, page 5.

Value of $20,000 Invested Over Five Years

30 September 2011 to 30 September 2016



Source: Platinum and MSCI. Refer to note 2, page 5.

Disposition of Assets

REGION	SEP 2016	JUN 2016	SEP 2015
Germany	24%	21%	16%
UK	18%	15%	22%
Austria	9%	6%	5%
Italy	7%	7%	5%
France	6%	6%	5%
Spain	5%	6%	6%
US *	4%	4%	4%
Russia	4%	4%	3%
Netherlands	3%	2%	1%
Hungary	3%	2%	2%
Switzerland	2%	2%	5%
Norway	2%	2%	2%
Sweden	1%	1%	1%
Turkey	0%	0%	1%
Cash	12%	22%	22%
Shorts	-2%	-1%	0%

* Stocks listed in the US, but predominant business is conducted in Europe.

Source: Platinum. Refer to note 3, page 5.

Top 10 Holdings

STOCK	COUNTRY	INDUSTRY	WEIGHT
Raiffeisen Bank International	Austria	Financials	4.7%
IHS Markit Ltd	USA	Industrials	4.4%
Carnival Plc	UK	Consumer Disc	4.2%
GfK SE	Germany	Consumer Disc	4.1%
Erste Group Bank	Austria	Financials	3.9%
Applus Services SA	Spain	Industrials	3.3%
Intesa Sanpaolo SpA	Italy	Financials	3.1%
Sartorius AG	Germany	Health Care	3.0%
OTP Bank Plc	Hungary	Financials	2.9%
ING Groep NV	Netherlands	Financials	2.9%

Source: Platinum. Refer to note 4, page 5.

For further details of the Fund's invested positions, including country and industry breakdowns as well as currency exposures, updated monthly, please visit https://www.platinum.com.au/fund-updates/#MonthlyUpdatesForThePlatinumTrustFunds.

European shares have now recovered most of the ground lost since Britain's vote to leave the European Union (EU) on 23 June 2016. The UK (+7% over the quarter, in local currency) was one of the strongest of the major European markets, helped by a weak British pound which boosted export stocks. Italy (+1%) was the weakest of the major markets, reflecting concerns over the upcoming referendum and the solvency of the Banca Monte dei Paschi di Siena.

The Platinum European Fund returned 4.8% for the quarter and -5.7% for the year (in Australian dollar terms). This compares to 2.5% and -5.8%, respectively, for our benchmark.

Our bank holdings made the largest positive contribution to the Fund's performance, led by **Erste Bank**, up 30% this quarter. Detracting from our performance were our healthcare stocks which are experiencing price pressure in the US and market research company, **GfK**, whose turnaround is proving trickier than anticipated.

Commentary

Deutsche Bank's balance sheet is nearly three times the size of Lehman Brothers' and one and a half times the size of Australia's annual economic output. Will Deutsche Bank fail? Will the German government bail it out? And what are the implications for the financial system, Europe and the global economy, if they don't? (See Appendix on page 4.)

Such are the imponderables with which European investors are currently being bombarded. A few weeks ago all the focus was on Banca Monte dei Paschi. Before that, Brexit, Greece, sovereign debt, youth unemployment, migration, populism, Russian revanchism, you name it. This litany of angst contributes to the perception that Europe's recovery from the Global Financial Crisis is constantly being derailed, in contrast to the experience across the Atlantic.

Thus, investor sentiment towards Europe remains decidedly negative. It is perfectly natural that investors should feel fatigued and be wondering whether it is all just too hard and whether they should focus their efforts on 'easier' regions like the US or Asia.

Such emotions create opportunities for disciplined investors. Consider for a moment that, for all the weeping and gnashing of teeth, Europe hasn't come apart at the seams as was widely predicted. Greece is still a member of the Euro currency bloc. The fiscal position of Spain, Ireland, Portugal and Italy (and indeed Greece!) is being repaired. Britain has elected to leave the EU without triggering a recession. Most European banks are in sound financial health. European structures have certainly been tested. And they're proving to be surprisingly resilient.

And then there's the economy. We suspect some readers will be surprised to learn that **Europe's economy is actually growing faster than America's**. You would certainly not think it from the headlines and prevailing 'expert' commentary. Economic data is the closest thing we have to objective facts. Given the negativity of sentiment, we think it may be helpful to walk through these.

Gross Domestic Product (GDP) is the most widely used measure of the size of an economy. On an inflation-adjusted basis, European GDP (+1.8%) is growing significantly faster than US GDP (+1.3%). Indeed, European GDP growth is pretty much in line with its 20-year average (+1.7%). Were it not for the extraordinary quantum of stimulus being applied, you could even describe the situation as 'normal'.

GDP GROWTH (INFLATION-ADJUSTED)	EU-28	USA
2016Q2 compared to 2015Q2	1.8%	1.3%
Average 1996-2015	1.7%	2.4%

Source: FactSet

Furthermore, the data tells us that Europe's growth is broad-based with consumption (+2.1%) and investment (+1.9%) both contributing nicely. Households are confident enough to spend (retail sales +3.6%, car sales +10.4%) and borrow again (household borrowing +1.9%). Corporate lending is flat (-0.1%), but this is deceptive. It is actually strong in core economies like Germany and France, but is dragged down by debt repayment in more indebted economies like Spain. This is actually quite healthy.

Most important of all, unemployment is 8.6% and falling steadily. It's true that there remains a wide disparity between countries, with unemployment being very low in Germany (4.3%) and very high in Spain (20.1%), for example. The silver lining, however, is that it is falling almost universally across all 28 EU member states and it is falling fastest in those countries where it is highest.

% CHANGE FROM A YEAR AGO (INFLATION-ADJUSTED)	JUN 2016
GDP	1.8%
Private consumption	2.1%
Investment	1.9%
Non-food retail sales (excluding cards and fuel)	3.6%
Vehicle sales	10.4%
Private sector loans	1.0%
Household	1.9%
Corporate	-0.1%

UNEMPLOYMENT RATE	%
2016Q2	8.6%
2015Q2	9.6%

Source: FactSet; Eurostat.

In summary, the European economy is recovering. Growth is broad-based. The pace is respectable. And disparities are closing. It's true that the pace is slower than what we grew accustomed to before the Global Financial Crisis. But this is true for most economies. And more importantly, the growth we are seeing today is arguably higher quality growth because it is being achieved concurrently with falling, rather than rising, imbalances and indebtedness. Put differently, the economy is not just getting bigger, but is also better able to withstand shocks.

Changes to the Portfolio

We were astonished by the way that our Italian and Austrian banks were treated in the aftermath of the British referendum on EU membership. These stocks fell to levels that were simply incongruent with the commercial reality that the underlying businesses faced, driven by what we suspect was a panicked reassessment of the political risk that was always there, but was brought into sharp relief by Brexit. We added significantly to our positions in **Intesa**, **Mediobanca**, **Raiffeisen**, **Erste** and **ING** during the sell-off.

Cooler heads soon prevailed and by the end of August the Euro Stoxx Banks Index had recovered to just shy of its pre-Brexit level. Following this rally, we trimmed positions in **Intesa** and **Lloyds**.

We are satisfied with our overall exposure to banks which currently accounts for 25% of our capital, but we do not want to increase it beyond this point. Our bank holdings remain roughly evenly split between Western European banks and those active primarily in the Emerging Markets of Eastern Europe.

It is important to draw this distinction because, while in the short-term these positions may be correlated, over the medium term, valuations will reflect the evolution of each investment case. And this differs markedly between our Eastern and Western European banks. Our Eastern European banks are growth stocks that should also experience a cyclical rebound in profitability. Our Western European banks are income stocks that are unlikely to grow and may face declining profitability, but will pay high dividends which we expect will more than compensate for this.

Outlook

While markets have digested the Brexit shock and recovered much of the ground lost, investor sentiment towards the region remains negative. Such sentiment stands in contrast to the economic data which paints a picture of steady, if not spectacular, recovery. The headlines continue to focus on a handful of problem banks which drive market volatility while, in reality, most European banks are in good financial health and are now supervised to a common high standard by the European Central Bank rather than their more politically attuned national regulators.

The combination of a supportive economic backdrop and investor disillusionment makes it easier to find good investments. The shortcoming is valuation, which remains frustratingly high in many segments of the market. However, we continue to find attractive investments in the handful of segments that remain reasonably valued, including Banking, Insurance, Energy and Industrial Services.

Appendix

Why Deutsche Bank is no Hindenburg

Banks fail because they are 1) illiquid, 2) insolvent, or 3) both.

Deutsche Bank does not have a liquidity problem. They hold EUR200 billion of highly liquid assets (12.5% of the balance sheet) which are enough to withstand a serious bank run. But ultimately it doesn't matter, because the European Central Bank (ECB) can and will provide unlimited liquidity support to the bank, if needed.

The solvency question is more nuanced. Normally banks become insolvent because they can't recover money from borrowers or counterparties; they don't have as many assets as they thought. But the value of Deutsche Bank's assets isn't being questioned. Rather, it's the value of their liabilities that has the market in a spin.

According to its latest disclosure Deutsche Bank faces 14 sets of legal actions. These are contingent liabilities because Deutsche only has to pay if it loses a case. Both the probability of losing those cases and the amount they would have to pay are unknown today. Deutsche makes an estimate and has set aside EUR5.5 billion for these contingencies. It recently emerged that the US Department of Justice (DOJ) has offered to settle the largest of these actions for EUR13 billion.

Of the EUR5.5 billion Deutsche has provisioned for these contingent liabilities, EUR3.5 billion is thought to be ear-marked for this particular case. This leaves Deutsche Bank EUR9 billion short. It also raises the question of whether the EUR2 billion of reserves set aside for the remaining 13 cases is sufficient or if more will be needed.

Answers are not forthcoming, most likely because they are unknowable. Remember, this is a proposed settlement, not a penalty awarded by a court. And the DOJ has a history of 'high-balling' and then negotiating down. For example, Goldman Sachs was hit with a similar figure and ultimately settled for US$5 billion. EUR9 billion is therefore a worst case scenario.

Against this EUR9 billion claim and 13 other outstanding cases, Deutsche Bank has EUR120 billion of loss-absorbing capital and, under basic assumptions, around EUR4 billion in annual earnings. There is simply no reasonable chance that these litigation costs will cause a loss to the bank's depositors, clients or counterparties, let alone trigger a systemic crisis.

It is possible, however, that shareholders and the holders of some equity-like instruments may end up taking a hit. This relates to a second problem. While Deutsche meets its capital requirements today, the required level of capital will ratchet up each year until 2019; it's a moving target. By the end of 2019 the bank will need EUR49 billion of capital, and it currently has EUR43.5 billion. This leaves a EUR5.5 billion shortfall that has to be progressively closed over three-and-a-half years.

With EUR4 billion of annual earnings, this would not be a problem. But if they also need another EUR9 billion to settle with the DOJ, then it becomes a very close call (they would need to earn EUR4.1 billion each year: (EUR5.5 billion + 9.0 billion) / 3.5 years).

There are a lot of moving parts. They may end up settling for well under EUR13 billion with the DOJ. But equally, earnings are volatile in this business and may end up being significantly lower than EUR4 billion. There is little in the way of a margin of safety, particularly where fear-driven clients choose to close accounts or cut relationships because of bad press.

However, this is reflected in the stock price. The shares are currently trading at roughly a **75% discount to book value**. This indicates that the market is pricing in a reasonably high likelihood of a dilutive capital raising.

Holders of some hybrid instruments are at risk if the bank's capital falls below a certain trigger level, which would trigger the automatic conversion of these bonds into equity. This seems unlikely under current circumstances as it is hard to see how the issues described above would erode capital so much as to trigger a conversion. However, they are now vulnerable should the bank experience a second or third unexpected shock.

Platinum does not currently own Deutsche Bank in any of its portfolios.

Notes

1. The investment returns are calculated using the relevant Fund's unit price and represent the combined income and capital return for the specified 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 historical performance is not a reliable indicator of future performance. Due to the volatility in the underlying assets of the Funds and other risk factors associated with investing, investment returns can be negative (particularly in the short-term).

   The inception dates for each Fund are as follows:

   Platinum International Fund: 30 April 1995
   Platinum Unhedged Fund: 28 January 2005
   Platinum Asia Fund: 4 March 2003
   Platinum European Fund: 30 June 1998
   Platinum Japan Fund: 30 June 1998
   Platinum International Brands Fund: 18 May 2000
   Platinum International Health Care Fund: 10 November 2003
   Platinum International Technology Fund: 18 May 2000

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

2. The investment returns depicted in this graph are cumulative on A$20,000 invested in the relevant Fund over the specified five year period relative to the relevant benchmark index (in A$) as per below (the "Index"):

   Platinum International Fund - MSCI All Country World Net Index
   Platinum Unhedged Fund - MSCI All Country World Net Index
   Platinum Asia Fund - MSCI All Country Asia ex Japan Net Index
   Platinum European Fund - MSCI All Country Europe Net Index
   Platinum Japan Fund - MSCI Japan Net Index
   Platinum International Brands Fund - MSCI All Country World Net Index
   Platinum International Health Care Fund - MSCI All Country World Health Care Net Index
   Platinum International Technology Fund - MSCI All Country World Information Technology Net Index

   The investment returns are calculated using the relevant 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.

3. Regional exposures (i.e. the positions listed other than "cash" and "shorts") represent any and all physical holdings, long derivatives (stock and index), and fixed income securities.
4. The table shows the relevant Fund's top ten long stock positions. Long derivative exposures are included. However, short derivative exposures are not.

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