Platinum European Fund

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Performance

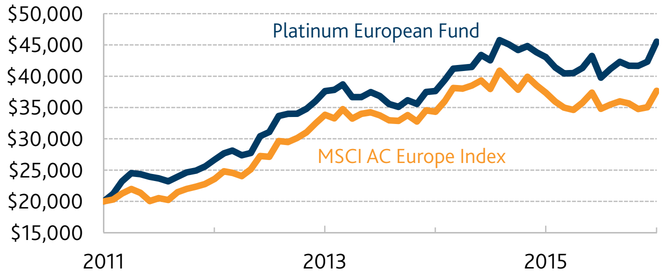
(compound pa, to 31 December 2016)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum European Fund	9%	6%	7%	18%	12%
MSCI AC Europe Index	6%	1%	4%	13%	2%

Source: Platinum and MSCI. Refer to note 1, page 4.

Value of $20,000 Invested Over Five Years

31 December 2011 to 31 December 2016



Source: Platinum and MSCI. Refer to note 2, page 4.

Disposition of Assets

REGION	DEC 2016	SEP 2016	DEC 2015
Germany	24%	24%	16%
UK	16%	18%	21%
Austria	9%	9%	5%
Italy	6%	7%	4%
France	7%	6%	4%
US *	4%	4%	4%
Russia	4%	4%	4%
Spain	3%	5%	5%
Hungary	3%	3%	2%
Netherlands	3%	3%	1%
Norway	3%	2%	1%
Switzerland	2%	2%	3%
Sweden	1%	1%	1%
Cash	15%	12%	29%
Shorts	-1%	-2%	0%

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

Source: Platinum. Refer to note 3, page 4.

Top 10 Holdings

STOCK	COUNTRY	INDUSTRY	WEIGHT
Raiffeisen Bank International	Austria	Financials	5.8%
IHS Markit Ltd	USA	Industrials	4.2%
Erste Group Bank	Austria	Financials	3.6%
Mediobanca SpA	Italy	Financials	3.4%
Applus Services SA	Spain	Industrials	3.4%
Hornbach Baumarkt AG	Germany	Consumer Disc	3.3%
Carnival Plc	UK	Consumer Disc	3.3%
OTP Bank Plc	Hungary	Financials	3.3%
Kering	France	Consumer Disc	2.9%
Sanofi SA	France	Health Care	2.8%

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

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.

Instead of triggering the expected flight to safety, the election of Donald Trump as the 45th President of the United States catalysed a rotation from defensive to cyclical assets. As investors reassess the prospects for growth and inflation, bond yields are moving sharply higher. The extreme crowding in bonds and equity market 'bond proxies' seems to be unwinding. These developments underscore the peril of following the crowd and overpaying for safety.

In the past three months, stock prices in Europe continued their post-Brexit recovery. Cyclical sectors led markets higher, with Materials, Energy and Financials being the best performers. Former safe havens, including Utilities, Property and Staples, fared poorly. So too did Healthcare stocks as investors agonise over what a Trump presidency means for US drug prices. Highly-valued growth stocks also fell out of favour as a cyclical recovery diminishes their scarcity value.

The Fund returned 9.3% for the quarter and 5.8% for the year (in Australian dollar terms). This compares to 5.6% and 0.8%, respectively, for our benchmark. Bank stocks contributed strongly to our quarterly performance with **Mediobanca** (+34%) and **Raiffeisen** (+28%) being outstanding performers. Market research company, **GfK**, another large holding, appreciated 40% following a buyout offer. Detracting from our performance were structural growth stocks, healthcare stocks and Swedish telecom equipment provider, **Ericsson** (-14%).

Commentary

In November 1992, Kerry Packer bought 10% of Westpac for just over $2.50 per share. A decade later, Westpac shares were worth six times as much and had paid a handy dividend along the way. A great investment in hindsight (had he held on).

But a little foresight may have served one just as well. At the time, Australia was emerging from a recession. Westpac traded at six times earnings. Risk was low at this point with the recession and sky-high interest rates having already shaken out the riskier borrowers. Meanwhile, the growth prospects were appealing. Australian households had little debt while their incomes would grow and interest rates would fall over coming years, allowing them to greatly increase their borrowing. Moreover, foreign banks were pulling out, reducing competition in the industry. All in all, it was a good environment to be buying banks in.

For Australian investors, such opportunities are rare. For international investors they are more common. We can't take our readers back in time to buy Westpac in 1992, but we can take them to present-day Eastern Europe where the economic and banking environment has many parallels to Australia's in the early 1990s.

Eastern Europe comprises a collection of emerging economies at various stages of development. Like most emerging markets, these economies have the potential to grow rapidly due to a combination of competitive labour costs and an abundance of unexploited opportunities to deploy capital.

But Eastern European economies also have some attributes that other emerging markets lack. They have a highly educated labour force. They receive steadfast, long-term, investment from the European Structural and Investment Funds. And, as members of the European Union (EU) or as part of the EU accession process, they subordinate themselves to EU law and oversight, meaning that they essentially 'import' strong, independent civic institutions from Western Europe to uphold the rule of law and citizens' rights.

The above setting provides very fertile ground for economic development and Eastern Europe enjoyed rapid economic expansion from the mid-1990s to 2008. The problem was that large current account deficits were allowed to persist during this period, resulting in the accumulation of foreign debt. This left the region vulnerable when the Global Financial Crisis (GFC) struck. In the absence of generous labour protections and welfare states, markets were allowed to clear. Jobs, wages and hours were cut aggressively. Unemployment spiked and consumer spending fell sharply. Most countries in the region suffered two harsh recessions in 2009 and 2012-13.

Through this painful episode, competitiveness was restored. Exports have grown strongly and current accounts are now balanced or in surplus. Since 2014 both growth and unemployment have returned to their pre-GFC levels. Debt has been aggressively repaid (or defaulted on), leaving household and corporate balance sheets in excellent shape. Wage growth is now picking up with little effect on inflation.

Hungary is a case in point. The economy contracted by a devastating 7% in 2009 and another 2% in 2012-13 with weak growth in the interim. However, since 2014 the economy has been growing at 3-4% annually and output has comfortably surpassed its 2008 level. Unemployment spiked to 11% and stayed there for a couple of years, but is now under 6%, lower than before the GFC. The current account has swung from a 7% deficit to a 4% surplus. Bank loans have been shrinking for seven years, leaving households and businesses with very low levels of debt, while interest rates have fallen from 8% in

2008 to under 1% today. The private sector's capacity to assume debt and repay it is excellent and, with growth returning, they are likely to do so.

OTP Bank is the leading bank in Hungary with a 25% market share. The foreign-owned banks that it competes with have cut their staff and branch numbers by 33-50% since 2009, reducing competition in the industry. There is very little risk left on its balance sheet simply because around 20% of loans have been written off. The 80% that are left have survived six years of recession and are, therefore, owed by exceedingly creditworthy borrowers. OTP is very conservatively funded and has very low leverage for a bank. Its growth prospects are excellent with the economy recovering, interest rates at rock bottom and customers having hardly any debt. OTP Bank in 2016 has many parallels with Westpac in 1992.

We bought OTP 18 months ago, paying under 8x earnings and 1.1x book value. This is significantly cheaper than most banks globally even though it has far-better-than-average growth prospects and much-lower-than-average risk. By way of comparison, Westpac today trades on 14x earnings and 1.8x book value.

Currently, approximately 13% of the Fund's capital is invested in banks that operate primarily in Eastern Europe. These comprise **OTP Bank, Erste Bank** and **Raiffeisen Bank International**.

Changes to the Portfolio

In response to recent share price appreciation and our large exposure to the banking sector, we trimmed a number of our bank holdings during the quarter. While we believe significant upside remains, it is not as asymmetric as it once was. We also reduced our position in cruise-operator, **Carnival**, and sold our stake in Spanish airport manager, **Aena**. Both positions have delivered excellent returns for the portfolio, but valuations now adequately reflect their prospects.

Our holding in market research company, **GfK**, was also sold in full. Here things have not gone as we had hoped. The business had struggled to turn around a challenged division and lost its CEO in the process. However, our entry price allowed considerable room for error and we ultimately sold out at a hefty profit, following a tender offer by private equity firm KKR.

Outlook

European economies are undergoing a broad-based recovery and incoming data suggests ongoing improvement. Investor sentiment has markedly improved in recent months, evidenced by a rotation into cyclical sectors and the ease with which markets absorbed the rejection of Matteo Renzi's reform agenda for Italy. It is therefore quite possible that this rally has further to run.

Yet, the political and economic risks have become no less menacing.

In the year ahead, the market will need to navigate higher bond yields and rising short-term rates in US dollar-linked economies. Considering the level of stimulus being applied, the European recovery remains tenuous. Rebalancing and reform in China also remains elusive (dare we say: illusive) while credit growth continues unabated and the stakes mount.

The new year will bring elections in the Netherlands, France and Germany as well as much rumination on the breadth of popular disenchantment with Liberalism, Internationalism and other principles fundamental to the European Project. Investors should, therefore, be prepared for some turbulence ahead but also understand that the best opportunities arise when hysteria reigns.

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 as a percentage of net asset value.

4. The table shows the relevant Fund's top ten long stock positions as a percentage of net asset value as at 31 December 2016. Long derivative exposures are included. However, short derivative exposures are not.

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