Platinum Capital Limited 30 June 2009
Investment Manager's Report

Performance

The mood of investors brightened as the realisation set in that the downward spiral of economic activity, attributable to massive but short-lived de-stocking, would be arrested by concerted government deficit spending. The measures adopted are unprecedented with huge government transfers augmenting incomes and massive asset purchases greatly assisting the resuscitation of bank and company balance sheets. The spreads on corporate paper shrank while money moved away from government bonds towards higher risk assets.

World stock markets came tearing out of the blocks in the second quarter led by emerging markets. Countries such as India, Indonesia and China were particularly strong, being identified as having less vulnerability to external factors than the developed economies. In the earlier sell-off these same markets had borne the brunt of selling as fund managers, and hedge funds in particular, sought to raise cash in the context of ever dwindling pools of liquidity. The developed markets were also lively with those industries most adversely affected in the preceding quarter, such as financials, home builders and other economically sensitive companies, recovering the most. The trading floor describes this as 'putting the risk trade back on!' but, interestingly, after the initial surge in April there was a flattening out as the quarter progressed.

Platinum Capital Limited has performed very strongly due to successful stock picking and heavy exposure to Asia. In fact, in each geographic area we outperformed the index by a handsome margin, although we surrendered some of that gain to losses made on shorts. Overall the Company outperformed the MSCI by 7.6% for the quarter, 15.8% for the six months and 34.5% for the year.

In absolute terms, our net assets rose by 12.7% (pre-tax) for the quarter, 9.9% for the six months and 18.4% for the year.

MSCI* WORLD INDEX SECTOR PERFORMANCE (AUD)

Sector	Quarter	1 Year
Financials	20%	-21%
Materials	10%	-33%
Industrials	7%	-22%
Consumer Discretionary	6%	-6%
Information Technology	4%	-7%
Energy	2%	-29%
Utilities	-1%	-16%
Consumer Staples	-1%	2%
Telecommunications	-3%	-9%
Health Care	-6%	2%

* Morgan Stanley Capital International

Source: MSCI

The following Platinum Net Asset Value figures (cps) are after provision for tax on both realised and unrealised income and gains.

30 April 2009	31 May 2009	30 June 2009
128.01	131.48	132.58

Source: Platinum

Currencies

The A$ has been a star performer since the beginning of 2009. The ideal position would have been to be fully hedged back into the A$ out of the Yen, US$ and Euro. In the six months to 30 June 2009 the A$ appreciated by 26%, 23% and 13% respectively against these currencies.

We at Platinum have been far too conservative, believing that Australia's overseas obligations would weigh heavily on the exchange rate even though our government's total net indebtedness is negligible and our banks are relatively sound. As a consequence we held only about 30% in the A$. By the end of the quarter, we had reduced this further to 24% of the portfolio, the concern being that as the pro-growth trade loses momentum the A$ will lose some support. Our disposition of currencies is shown in the table below.

CURRENCY POSITION

Region	**Jun 2009**
Europe (Euro, Norwegian kroner)	26%
Australia	24%
Asia (HK dollar, Taiwanese dollar, Korean won etc)	22%
North America	14%
Japan	13%
Other	1%

Source: Platinum

Shorting

We entered the quarter with the lowest short position for years and, happily, the defensive names that constituted the bulk of our shorts barely moved up as investors used them as funding to purchase more economically sensitive entities. As this occurred, we began to shift the positions out of the defensives into more cyclical stocks, the latter having been significantly up-valued in relation to defensives. We further believed that in the current uncertain climate the defensives would continue to gain support.

At quarter end our shorts represent 18% of the portfolio and are mainly in economically sensitive companies.

Changes to the Portfolio

GEOGRAPHICAL DISPOSITION OF PLATINUM ASSETS

Region	Jun 2009	Mar 2009
Japan	24%	24%
Asia and Other	23%	25%
Europe	21%	21%
North America	20%	21%
Cash	12%	9%
Shorts	18%	19%

Source: Platinum

There is not much overall change in the portfolio as our transactions have been largely in smaller holdings. Several purchases that were made into the teeth of the sell-off subsequently climbed sharply and were reversed. These included China Mengniu Dairy, which we described in March regarding melamime contamination and which then doubled, Wumart (China retail), Mosaic (fertiliser), Metso (plant engineering), Corning (substrate glass and poly silicon) and Rohm (analog chips). The proceeds were redirected into our larger holdings. The top 20 holdings now account for nearly 37% of our longs.

A large company with very interesting prospects that was added, is China Resources Enterprise. This is a Hong Kong listed subsidiary of a state owned enterprise (SOE) with diverse interests in supermarkets and hypermarkets, beverages (beer and bottled water), rented commercial property and infrastructure. The businesses that caught our attention were retailing and beer. Both have been increasing sales in the high teens and profits are starting to follow. Each area is highly competitive and we have reservations about the business acumen of many SOEs. However, the group has teamed up with a highly experienced partner in beer, namely SABMiller, while in retailing they are following a model of trying to dominate specific regions, and with the help of experts lured from experienced international competitors, seem to be building a successful business. The company is not a complete gift being priced on about 17 times this year’s earnings and 1.5 times book, yet the profit potential of its consumer businesses is alluring.

PLATINUM CAPITAL LIMITED – TOP 20 STOCKS		
Stock	**Industry**	**Jun 09**
Microsoft	Technology	3.6%
Mitsubishi UFJ Financial	Financial	3.3%
Cisco Systems	Technology	2.3%
Siemens	Electrical	2.2%
Denso Corp	Auto	2.0%
Hutchison Whampoa	Telco/Transport	2.0%
Bangkok Bank	Financial	1.9%
Henkel	Consumer Goods	1.9%
Henderson Land Dev	Property	1.8%
Anglogold Ashanti	Gold	1.7%
Samsung Electronics	Electrical	1.7%
Sumitomo Real Estate Sales	Property	1.7%
Micron Technology	Technology	1.5%
Kanto Denka Kogya	Chemicals	1.4%
En-Japan Inc	Technology	1.4%
Sanofi-Aventis	Health Care	1.3%
International Paper	Paper	1.3%
Merck & Co	Health Care	1.3%
BMW	Auto	1.3%
Veolia Environnement	Utility	1.3%

Source: Platinum

Commentary

Being conscious of the fact that most readers have probably had their fill of media coverage of the "world economic crises", we will try to follow a different course. Before we do, though, let's remind ourselves of important observations made in our earlier communications:

- We are in uncharted water and cannot know how the individual will respond to the uncertainties.
- The fiscal and monetary response by a host of nations is unprecedented in scale and scope and is partially experimental.
- The de-stocking cycle that probably bottomed-out in the first quarter of 2009 led to unbounded fear, even panic, and this was expressed in a collapse in the valuation attributed to risk assets; shares, commercial paper and property.
- While reassuring, the recent rally in risk assets does not necessarily mean the system is healed and the pattern of the last thirty years is about to resume. As we noted last quarter, the banks are mostly bereft of equity, aggregate corporate profits had reached extreme levels world-wide and trade imbalances are at huge and probably unsustainable levels.
- Those countries with strong fiscal balances and high savings are likely to recover the quickest.

As we write the conventional view is that the emerging countries of the world are best placed to drag the "world train" out of the shunting yard.

Among the people we met in Beijing on a recent trip to China was a well-regarded Chinese economist who had served the IMF in various postings around the world. He felt the stimulus package of Rmb 4 trillion, some 25% of GDP, together with the massive growth in bank lending, up 30% year-on-year in the first six months of 2009, would allow China to decouple from the industrialised countries. Also, that the changing destination of Chinese exports to Asia, Africa and Latin America would compensate for weak demand elsewhere.

When talking about prospects for growth, among the other BRIC (Brazil, Russia, India and China) economies he argued that India's prospects were sub-par on account of its inadequate infrastructure. This notion has great appeal for those who go to India frequently, as we do, but it depends on your "perspective". While true at first sight, it remains a fact that India has a strong judicial system, cumbersome and creaky though it may be, and a representative system of government. This is still a dream for China. Whether a modern capitalist economy needs representative government is for readers to judge but what is surely not in dispute is the need for a sound judicial system.

This difference in perspective recurred on several occasions during our ten day visit. The most striking was the meeting with investor relations representatives from China South Locomotive and Rolling Stock Corp (CSR). This recently listed SOE, together with its still unlisted northern twin, the CNR, are principal beneficiaries of the massive infrastructure programme just launched by the Central Government. Sadly for us, the meeting started on the wrong foot when we asked why we should share the general enthusiasm for the company's profit prospects. Closer inspection of the presenter's business card would have revealed that apart from being a board member he was also head of the CPC department of propaganda. Our lack of perspective worsened when we persisted in delving into the terms and conditions under which foreign giants like Siemens are required to transfer their technology in order to gain market access. Not that we are unsympathetic to a reversal of roles harking back to the days of the treaty ports[1], but the divergence of views on protectionism and selection on grounds other than commercial merit was a source of friction. Our final opinion was that there will be a lot of trains built but that the sort of profits the brokers are projecting is probably unrealistic.

With the banks having been instructed to lend copiously, credit is exploding in China, in marked contrast to the developed world where credit growth is slowing, notwithstanding government urging, and delinquencies have reached record levels. Interestingly, anecdotal evidence from those Chinese who do not face the daily chatter of markets, fear that this will lead to inflation. Property speculation is snowballing into a frenzy. As in Hong Kong, land development in China requires the payment of a development premium governed by size of the approved floor space (square meters built). The price

[1] Generally accompanied by military superiority/victories in the nineteenth century, the Western powers entered into unequal treaties in countries such as Japan, Korea and China to gain access to their markets.

levels of recent land sales in Beijing are astounding observers. In the most recent auction, a site close to the fourth ring road[2] went for Rmb 15,000 per m^2. Considering that building costs of medium grade residential property are approximately Rmb 4,000 per m^2, the bidder, an SOE, is evidently relying on substantial price appreciation in order to break even. The same pattern is occurring in the other major cities and there is a massive revival of interest in the HK property scene[3].

The most encouraging aspect of this development activity is the insistence by the authorities that development is accompanied by ample green space calculated at 60% of each site area. This is resulting in Beijing being an unusually green metropolis. Few modern cities have achieved such a balance and each time one visits Beijing one is reminded of the success of the town planners in having embedded the amenities that are rare in great conurbations. Our accompanying broker thought it was a waste of good building space, another example of the differences in the way of looking at things.

Outlook

Markets have rallied strongly in response to the realisation that the world is no longer looking over the edge of an abyss but this does not alter the fact that a resumption of a high level of economic growth will remain a challenge for most Western countries. The emerging economies will probably do somewhat better though burdened by weaker exports. With this in mind we are puzzled by the strength of commodity markets and believe they are being driven by short-term anomalies which include strategic stockpiling in a world where most currencies are suspect.

Coming off a severely depressed base, profits will improve but utilisation levels are unlikely to be strong, meaning that a recovery to the super profits of earlier years is highly unlikely. The most encouraging aspect of all this uncertainty from our point of view is that there are now plenty of opportunities to find companies that are priced below their potential. Such investments are not confined to those areas of the world that are likely to grow strongly. There are many companies that, while registered as having their head offices in Europe or America, in fact derive a great part of their profit from emerging economies. Their share price sometimes does not reflect this fact.

We have adopted a relatively cautious stance and are delighted at the price at which we can acquire companies of unusual quality that are relatively low risk. We have identified a number of companies well placed to benefit from the stimuli to the system afforded by central bank largesse and government infrastructure spending.

[2] The fourth ring road built in 2001 is about 8kms from Tiananmen Square. The farthest complete ring around the city is the sixth ring, about 18kms from the centre.

[3] Top end residential property in both Shanghai and Beijing is certainly no longer cheap with prize locations, say within the second ring road in Beijing, selling for Rmb 50 to 60,000 per m^2; over A$10,000 per m^2. This contrasts with the average residential selling price recorded in the first five months of 2009 of Rmb 4,450 m^2 for China as a whole and around Rmb 11,300 per m^2 for the first tier cities of Beijing, Shanghai, and Shenzhen in the New Territories. The average for Hong Kong is HK$45,000 per m^2 and the top end is 3 to 5 times this figure.

It is likely to be several years before the consequences of the credit crisis have fully played themselves out. With an earthquake of such magnitude it would be surprising if there were not after-shocks. We will use shorts to exploit the anomalies that are being created by those investors who believe that it was all a bad dream and that the system is nearly fully repaired.

Whether or not matters turn out better than we presently believe, we feel those companies geared to world growth will achieve results superior to those with essentially defensive qualities.