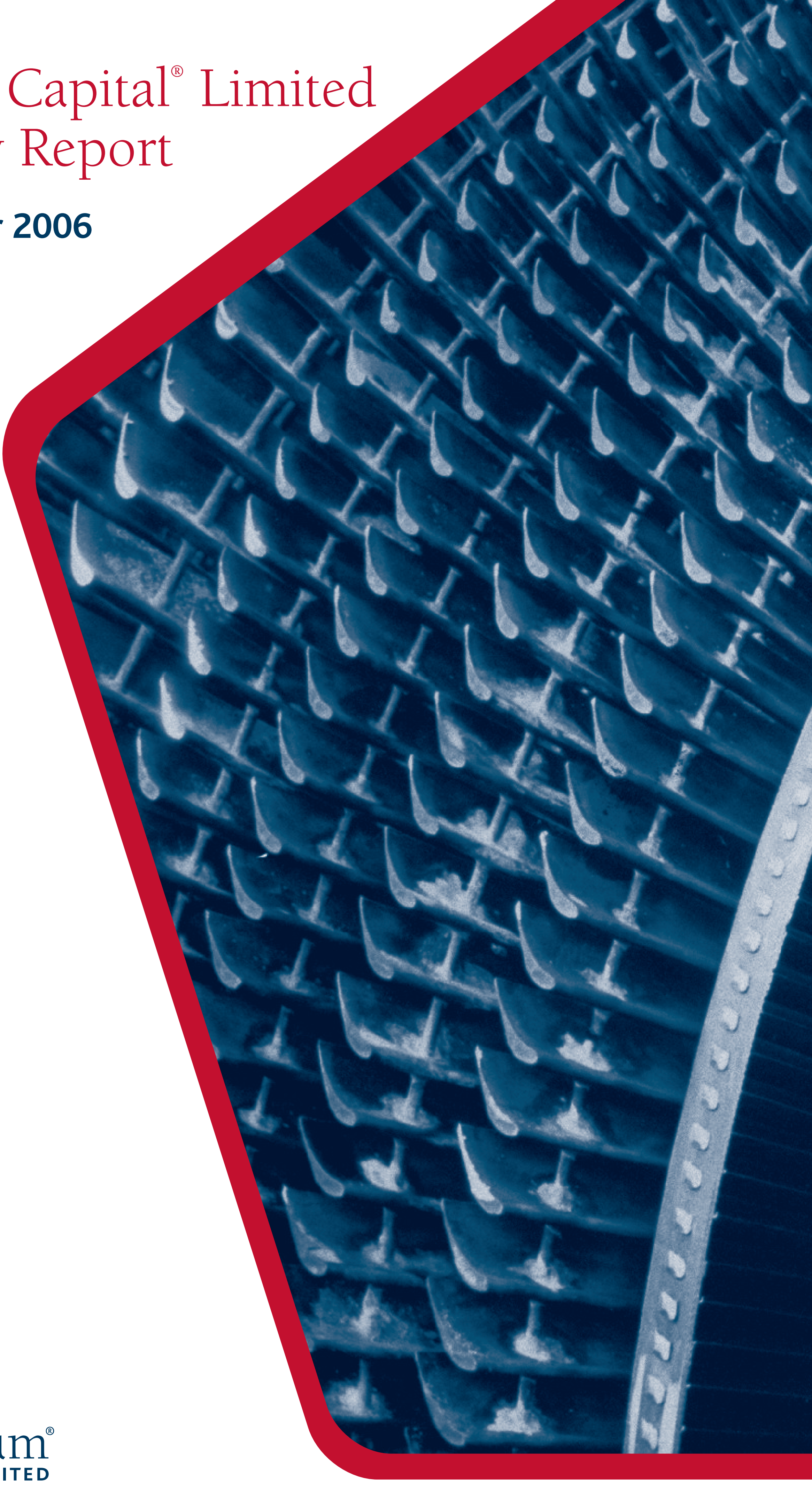
Platinum Capital® Limited Quarterly Report

30 September 2006



Platinum® CAPITAL LIMITED
ABN 51 063 975 431

PERFORMANCE

It has been a most testing quarter. Poor early sentiment was gradually replaced by renewed confidence which culminated in a burst of enthusiasm based on very aggressive acquisition activity.

Initially all eyes were on interest rates and most discussion counted on whether the US Federal Reserve Board would continue the cycle of rate increases faced as it was, with continued strong consumer sentiment and retail demand. In the event, however, the Fed held rates steady and the focus shifted to other economic variables, movements in which supported the view that the pace of economic growth was slowing. Evidence of a sharp downturn in the property market helped long bond yields to fall and steepened the reverse yield curve, with short rates higher than long, which in the past has been a good indicator of impending economic recession.

Another variation of sentiment occurred as oil and gas prices changed trend, falling more than 20% from an oil price high of $78 per barrel. This was seen as a boost to corporate profits through lower input prices and as a direct stimulus to consumer spending; a recovery in equity prices began from mid-July onwards. Towards the end of the quarter there were a number of very large takeovers and acquisitions, notably the US$32bn leveraged buyout of HCA, and markets kept rolling upwards.

The main debates now are as to whether the US will have a hard or soft landing and whether this will be offset by renewed growth in Europe and Japan.

The outcome for the MSCI has been a rise of 4% for the quarter and 17.3% for the last 12 months. Most of the larger markets have herded around these figures with the exception of Japan which was conspicuously weak at -1.2% for the quarter, although a respectable 15.8% for the year. As was to be expected, emerging markets sold off the most but have also been the strongest to recover. The Company's performance over this period was 2.2% pre-tax for the quarter and 16.0% for the full 12 months, somewhat trailing the markets but not too bad given the Company's net market exposure of only around 50-60%.

The high level of momentum activity in markets is clearly demonstrated by the accompanying industry group analysis. Note the poor showing

MSCI* WORLD INDEX INDUSTRY PERFORMANCE (AUD)

SECTOR	QUARTER	1 YEAR
ENERGY	**-4%**	**5%**
MATERIALS	**-1%**	**25%**
INDUSTRIALS	**1%**	**19%**
CONSUMER DISCRETIONARY	**4%**	**15%**
HEALTH CARE	**6%**	**13%**
CONSUMER STAPLES	**6%**	**17%**
FINANCIALS	**6%**	**26%**
INFORMATION TECHNOLOGY	**6%**	**11%**
UTILITIES	**8%**	**22%**
TELECOMMUNICATIONS	**9%**	**15%**

Source: Factset
* Morgan Stanley Capital International All Country

of energy and materials in the last three months while former laggards are back in favour.

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

NET ASSET VALUE (CPS)	
31 JULY 2006	169.43
31 AUGUST 2006	172.07
30 SEPTEMBER 2006	173.97

Source: Platinum

CURRENCIES

Some interesting theories have circulated about the persistent weakness of the Japanese yen. For the moment we are content with the argument that until there are signs of a more aggressive stance on Japanese interest rates the yen will tend to remain subdued. In the absence of any other input, though, we are disinclined to reduce our exposure given the strengthening we are now seeing in the Chinese currency. The A$ was virtually unchanged against the US$ point-to-point for the three months but gained 3.6% versus the weak yen. There have been no changes to our currency posture.

CHANGES TO THE PORTFOLIO

We were relatively inactive over the quarter, completing the sale of Daiwa House, Sharp and Mitsubishi Chemical in Japan, and some small holdings in India. The principal purchases were Cisco, eBay, and Singapore Airlines.

We are of the view that changes in technology take a long time to be implemented in full. Our investments in Ericsson and Alcatel reflect our belief that there is a long cycle ahead in the supply of cell telecom systems and our recent purchases of Cisco are supported by our expectation of large future expenditures on internet infrastructure. The existing copper wire based backbone of the telcos seems unlikely to be a long-term solution with the emergence of optical switching and the like. The rapid adoption of video intensifies the need for greater bandwidth. By way of illustration, a one minute clip of video uses approximately 20 times the amount of capacity as the same time of voice traffic. Cisco experienced a 50% net profit collapse at the end of the dot.com. boom, only to bounce back two years later to produce new record profits and by 2005 to have achieved net profits some 46% ahead of those at the peak of the bubble. This highlights the convergence of the telco and internet protocols and the company's leading position in the network operating system.

GEOGRAPHICAL DISPOSITION OF PLATINUM ASSETS

REGION	SEP 2006	JUN 2006
NORTH AMERICA	27%	23%
WESTERN EUROPE	27%	26%
JAPAN *	25%	26%
EMERGING MARKETS (INCLUDING KOREA)	13%	13%
CASH	8%	12%
SHORTS	36%	34%

Source: Platinum
* The Company also has a 10% short position in Japanese Government Bonds

BREAKDOWN OF PLATINUM'S PORTFOLIO BY INDUSTRY

CATEGORIES	EXAMPLES OF STOCKS	SEP 2006	JUN 2006
CYCLICALS/MANUFACTURING	TOYOTA INDUSTRIES, SCHINDLER, SIEMENS, INTERNATIONAL PAPER	29%	28%
FINANCIALS	CREDIT AGRICOLE, SUMITOMO MITSUI INSURANCE, SAMSUNG FIRE & MARINE	15%	15%
RETAIL/SERVICES/LOGISTICS	HORNBACH, CARREFOUR	10%	9%
TECHNOLOGY/HARDWARE	INFINEON TECH, SAMSUNG, SUN MICROSYSTEMS	10%	8%
SOFTWARE/MEDIA	LIBERTY MEDIA	7%	7%
CONSUMER BRANDS	HENKEL, BEIERSDORF, PERNOD RICARD	6%	7%
TELECOMS	ALCATEL, SK TELECOM, ERICSSON	6%	6%
GOLD AND OTHER RESOURCES	SHELL, BARRICK GOLD, NEWMONT MINING	5%	6%
MEDICAL	PFIZER, MERCK & CO	4%	3%

Source: Platinum

Though we regard Cisco as having a marketing culture its sheer size relative to its principal competitors and its commitment to R&D, at 13.5% of sales, means that it outspends the combined effort of the next three players, excluding Alcatel. The market seems to tire of the highly promotional nature of the company's communications at times but the moves it has made with Scientific-Atlanta and a stream of small but interesting acquisitions suggests that it can maintain its pattern of very high profitability and growth.

eBay is another high growth company but one the market fears is facing new challenges. The issue is that the rate at which it is acquiring new users has been falling and is presently down to around 10%. At the same time there has been a proliferation of suppliers clogging the site with fixed price common merchandise of limited appeal. The company's response has been to put up its usage charges but this has annoyed some existing users.

We felt that the halving of the share price over the last two years was unduly harsh treatment for a company that attracts 80 million active and 200 million registered users thereby creating an almost unprecedented network effect. While the strongholds in the US, Germany and the UK are slowing, there are still exciting prospects in other markets, particularly France, Italy and China.

Internet selling is not a business without risks, such as on-line fraud and counterfeit goods, but the user feedback mechanism has proven effective to date. Longer-term, the acquisitions of PayPal and Skype offer novel solutions in an age of technological flux and could become significant in their own right.

Singapore Airlines is a more straight forward case of a perfectly respectable company that has historically grown at a market-type rate of 6% pa yet because of the high oil price was selling at one of its lowest valuations ever. There is certainly some new, and perhaps carelessly funded, competition on its long-haul routes from some Persian Gulf carriers, but the growing opportunities in China and India are a fully compensating factor. Moreover, the deferred delivery of the Airbus 380 will tighten supply in the near term. For those of us who use long sector flights regularly there is no doubt about the quality of the service due in no small part to the company having the youngest fleet in the air – an average of five years old. It is our experience that buying a company like this when it is selling at close to book value gives an attractive return once the near term issues subside.

COMMENTARY

We have previously highlighted the importance we attach to looking for and researching broad themes within the investment context. We seek to establish positions in unfashionable or relatively undervalued areas wherever we believe there is adequate evidence that a change in circumstances can occur and a return to fashion be enjoyed. Flying in the face of majority opinion like this sometimes involves a degree of risk but the returns can be large. We are pursuing four of these themes at present: paper, other soft commodities, quality large capitalisation companies, and the capital spending cycle within information technology. By far the most significant of these is paper.

From an emotional view point, it feels very uncomfortable to have around 8% of the portfolio in an industry that in North America has experienced 14 consecutive quarters of losses. Moreover, the demand for the commodity is notorious for its economic sensitivity and some indicators suggest we are on the cusp of the down-leg of an economic cycle. The sector is further depressed by the evident decline in western and particularly American newspaper readership due to the rise of the internet and diminishing readership among the young. Worse still, the industry habitually adds to capacity at the margin which ensures sub-optimal returns. This time around it has been in Latin America that capacity has been added. Here fast growing, high yielding hardwood species and other favourable factors ensure a 10 to 15% cost advantage over the average northern hemisphere integrated mill.

So how can we justify investment in this can of worms? Firstly we need to establish some facts. Historically the global use of paper has grown at around 3% pa, with the lower income countries tending in recent years to accelerate their use of paper by around 4.5% pa while wealthy countries are seeing usage rise by around 0.5% a year[1]. The realignment of currencies and untapped fibre potential has favoured Latin America recently and resulted in additional low cost capacity of pulp and paper but over the last 15 years only about 10 million tons of net new pulping capacity has been commissioned, while the demand for paper has risen by some 100 million tons. The shortfall has been met with recycled material.

There has been a boom in the building of de-inking plants as the pressure on land fills and action by green-minded municipalities has seen the recycling rate of paper rise to about 55%[2]. The integrated mills, which require an investment of about $2 in plant for each annual $1 of sales they generate, have been struggling, closing or consolidating but scrap-based mills have been enjoying a bonanza. Cheap scrap (old newspapers – ONP, or old corrugated containers – OCC)[3] and relatively light investment in plant have spawned mills near their principal markets, while the traditional integrated producers have faced losses and high transport costs.

Change is happening. So severe is the financial plight of many mills that closure and planned shut-downs now entail more capacity than new commissionings. Prices of most grades are starting to reflect the higher cost of energy as mills are operating at

1 The declining segment is newsprint but with few exceptions, finer grades are growing, while packaging grades are galloping. "Developed world" total paper use is around 250kg per head pa while China uses 40kgs and India 10kgs per capita pa.

2 There is a wide range of experiences here with the likes of Japan and the Nordic countries already achieving 70% recycling rate.

3 There are many grades of paper with old newsprint for example being available at $US125 per ton while newsprint sells at around $US600 pt.

close to peak levels and are passing on cost increases. Demand is strong and in a world of ultra-enthusiasm about the China economic miracle, paper together with grains, are the only commodities that fail to be mentioned[4].

Importantly, as societies enjoy higher standards of living their propensity to consume paper grows disproportionately. Of equal importance is the observation that both China and India are fibre poor, bagasse or dry pulp notwithstanding, and although the level of global paper recycling is still shy of its potential of, say, 70%, this may only be reached with higher price inducements.

It will be interesting to see how this story unfolds. About 70% of our investment is in companies that are currently profitable and provide useful dividends even at current depressed paper prices, with the spice being provided by pure pulp makers and some integrated newsprint producers. In this manner we are attempting to control the timing risk yet still to reap the benefits of the prospective tightening of the merchant pulp market. Should the rate of global activity slow considerably there is the risk that we have bought too early but there are several finer points that may yet surprise and support the paper companies.

OUTLOOK

We have written often about abundant liquidity, but who would have thought that two and a half years after short-term rates began their ascent the yield of long dated bonds would have fallen? Further, equities earning yields now exceed those of bonds – a rare event indeed. In these circumstances it is not surprising that the more aggressive participants in capital markets are seizing opportunities in the risk spread. When, in what circumstances and with what consequences this behaviour will be interrupted we cannot say. What we are certain of is that the economic cycle has not been banished permanently.

Kerr Neilson
Managing Director

4 China is now the world's third largest producer at 55mt pa of all grades. Demand is seemingly rising by no less than 5 to 6mt pa. Global output is around 350mt pa.

Platinum® CAPITAL LIMITED

Level 8, 7 Macquarie Place
Sydney NSW 2000
Australia

Telephone: 02 9255 7500
or 1300 726 700 (Australia only)
or 0800 700 726 (New Zealand only)

Facsimile: 02 9254 5590
Email: invest@platinum.com.au
Website: www.platinum.com.au