The Platinum Trust Quarterly Report

30 June 2002

Incorporating the:

International Fund
European Fund
Japan Fund
International Technology Fund
International Brands Fund

PERFORMANCE RETURNS TO 30 JUNE 2002

Fund	30 June Distribution (cpu)	Fund Size	Quarter	1 Year	2 years (compound pa)	3 years (compound pa)	5 years (compound pa)
International Fund	**12.73**	**$1,869mn**	**-3.8%**	**9.8%**	**16.1%**	**26.9%**	**22.2%**
MSCI * World Index			-13.6%	-23.2%	-15.0%	-3.7%	6.5%
Japan Fund	**14.97**	**$74mn**	**0.7%**	**1.1%**	**-4.9%**	**18.6%**	**-**
MSCI Japan Index			1.3%	-24.6%	-21.3%	-4.7%	-
European Fund	**11.27**	**$99mn**	**-5.0%**	**5.4%**	**11.4%**	**33.9%**	**-**
MSCI European Index			-9.2%	-16.1%	-12.1%	-0.7%	-
International Technology Fund	**18.42**	**$33mn**	**-17.2%**	**-18.7%**	**11.4%**	**-**	**-**
MSCI Technology Index			-31.1%	-43.7%	-47.1%	-	-
International Brands Fund	**8.85**	**$62mn**	**1.7%**	**25.2%**	**25.6%**	**-**	**-**
Brands Index			1.7%	-9.7%	-2.8%	-	-
* Morgan Stanley Capital International							
Micropal average int'l fund return (601 funds surveyed)				**-27.2%**			

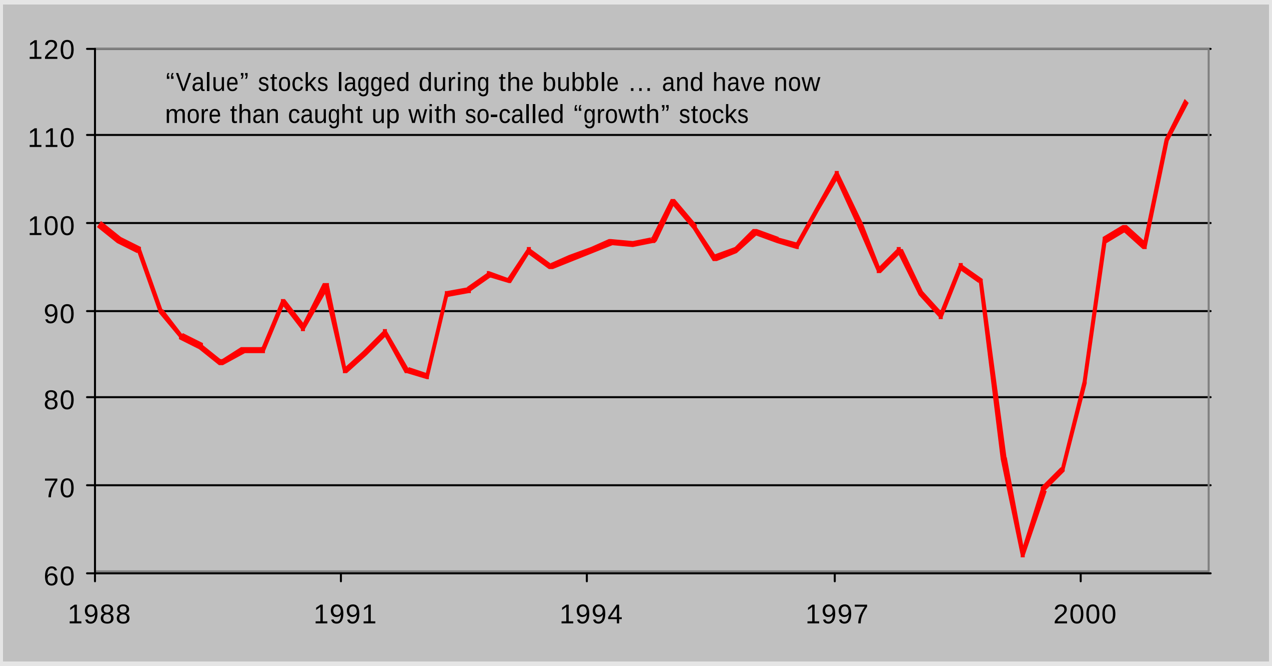
(Source: MSCI, Platinum)

HISTORIC RATIO OF DOW JONES INDEX TO THE GOLD PRICE

Source: Bloomberg

Information about the units on offer in the Platinum Trust are contained in the Platinum Trust Product Disclosure Statement (PDS) No. 1 issued on 11 June 2002. Persons wishing to acquire units must complete the application form from the current PDS. Reliance should not be placed by anyone on this document as the basis of making any investment, financial or other decision. Past performance is not indicative of future performance. Platinum Asset Management does not guarantee the repayment of capital, payment of income or the performance of the Funds.

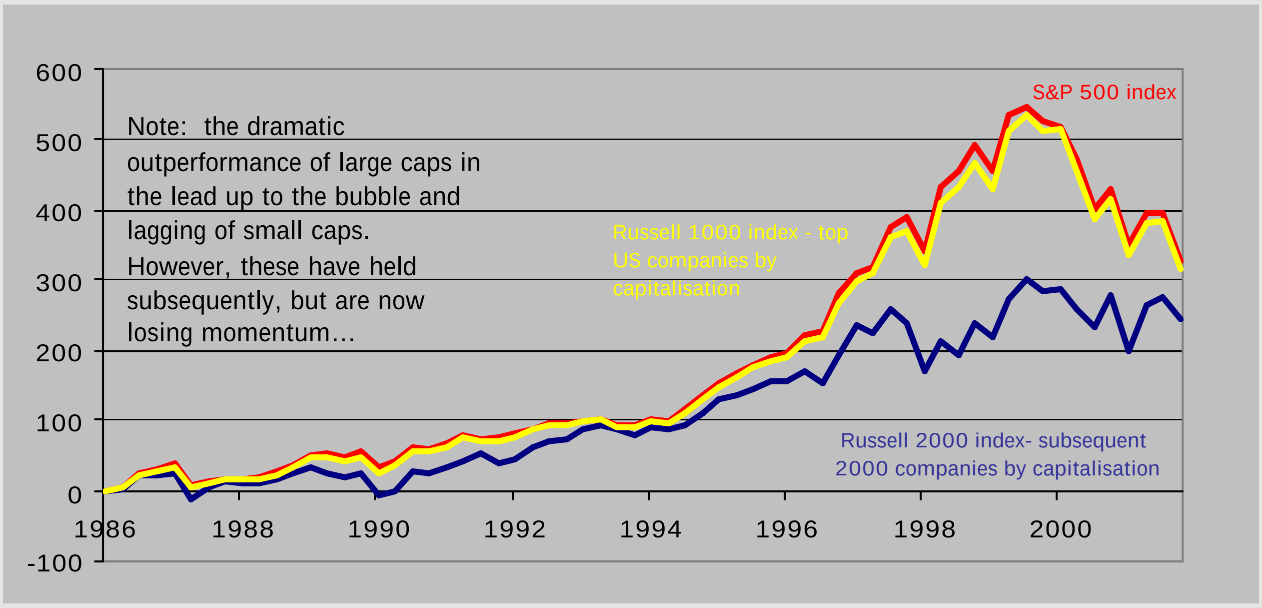
RELATIVE PERFORMANCE OF LOW PE SHARES TO HIGH GROWTH SHARES *



Source: Morgan Stanley

* Lowest 20% of stocks on PE versus highest 20% of stocks on the four year growth rate.

RELATIVE PERFORMANCE OF LARGE COMPANIES VERSUS SMALL COMPANIES



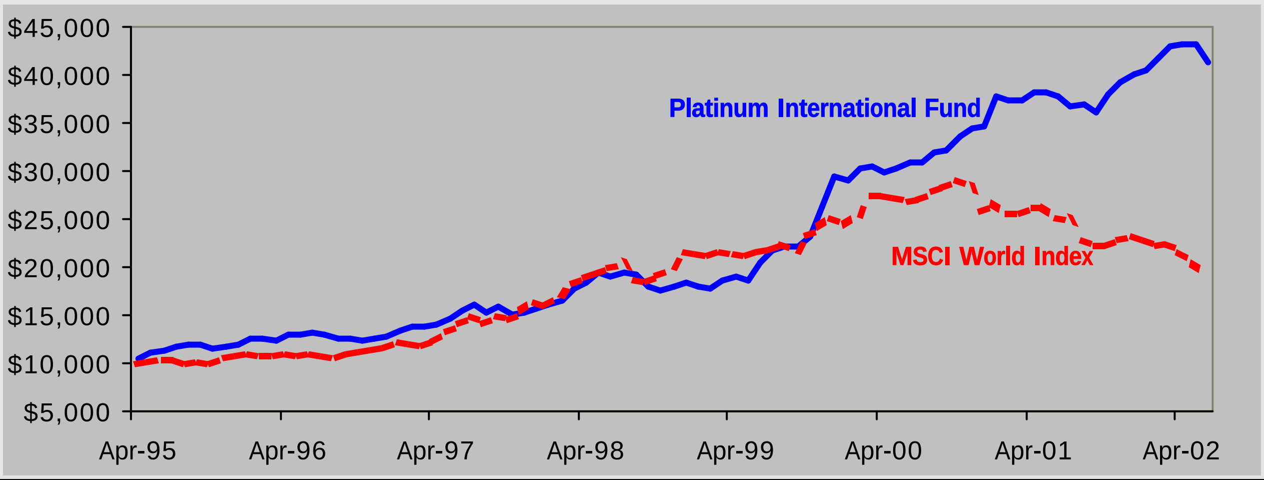
Source: Bloomberg

Platinum International Fund

Performance

REDEMPTION PRICE: CUM $1.8028 EX $1.6758

VALUE OF $10,000 INVESTED SINCE INCEPTION (1 MAY 1995 – 30 JUNE 2002)



The revelations regarding the excesses that accompany any worthwhile financial mania have rained down on the optimists and called into question the very institutions that were so fervently praised in the aftermath of the demise of central planning. Once again the worst affected sectors were IT and telecom, but there were no hiding places in a sectoral sense. By geography, the bright spots were Japan and Greece. This has left the MSCI down by 13.6% for the quarter, -16.9% for the six months and a withering -23.2% for the year.

We have not come out unscathed as the upward re-rating of smaller capitalisation shares came to an end and some shares were marked down on growth fears. Our short sales were a mitigating factor and contributed some 3% to the quarterly return. Thus the last three months saw the Fund decline by 3.8%, while it rose by 3.4% for the six months and increased by 9.8% for the last 12 months. Readers may be interested to note that the average return from 601 managers in the Micropal survey of International equity funds lost 27% this last 12 months.

MSCI WORLD INDEX – INDUSTRY BREAKDOWN

Sectors	3 months	1 year
Information Technology	-29.3%	-43.4%
Telecommunications	-25.1%	-42.6%
Health Care	-17.1%	-21.0%
Consumer Discretionary	-14.8%	-26.3%
Industrials	-13.3%	-25.2%
Utilities	-10.2%	-26.7%
Financials	-9.3%	-20.2%
Energy	-8.3%	-10.0%
Consumer Staples	-4.8%	-1.9%
Materials	-3.6%	-4.1%

Source: MSCI

Changes to the Portfolio

Once again we progressively added to existing positions. Our eagerness to start accumulating positions notably in EDS (IT outsourcing) and Ericsson has cost us money as these companies sold off with the techs. Other significant additions were mainly Japanese companies: Takeda, Sky Perfect Communications, Credit Saison, Aiful and Denso.

With the exception of the latter, these are domestic plays that are largely unaffected by the movement of the yen. This provides balance to the export component of the portfolio and exposes the Fund to the growth industries in the moribund Japanese economy. Takeda is the country's principal drug producer, with an interesting portfolio, and has sold off in sympathy with its international peers. Trading on around 20 times earnings with 20% of this capitalisation in cash, it is close to its cheapest valuation ever.

DISPOSITION OF ASSETS

Region	Jun 2002	Mar 2002
Western Europe	38%	37%
Japan	18%	15%
Emerging Markets (incl. Korea)	12%	15%
North America	10%	11%
Australia	1%	1%
Cash	20%	21%
Shorts	20%	15%

Sky Perfect was IPO'd with all the fanfare of the internet boom and has subsequently fallen over 65%. This entity was one of several licence holders to broadcast digital TV via satellite but as time has passed it has merged with JskyB, and another competitor, DirectTV Japan, has terminated its service. Sky is now the sole communications satellite digital platform over Japan, aggregating some 180 channels, with nearly three million subscribers. By the nature of this business, its costs are front-end loaded which means that at the current net sign-on rate of around 40,000 per month, it will break even by year-end. This is an unattractive proposition to many institutions in Japan given the clear emphasis on solvency and free cash flow. We believe this is the main suppressant on the share price, as subscriber growth has been good, a competing analog station providing two movie channels is losing ground, and in the next few months there will be the added attraction of a horse racing channel with on-line betting facilities. Should Sky eventually gain say, six million subscribers (out of 46 million households), the share will prove to be a gift.

Credit Saison and Aiful are a means to participate in the growing credit card market in Japan. Obstructing the acceptance of cards are the high merchant fees and social values. However this is changing, particularly among those below 30. Both companies have excellent growth records throughout this last 10 years of recession. Credit Saison is aiming to be the leading card processor in the country while Aiful will continue to develop its traditional short term lending business through the offering of credit cards. Both have very low balance sheet gearing, borrowings to equity being around five times and as credit markets expand in Japan, the potential for leverage, as witnessed in Korea, is enormous.

Lastly, Denso is one of the reminders of why one invests in Japanese companies. Its commitment to product excellence and innovation is partly revealed by its R&D budget of 9% of sales. Further, it is targeting to reduce its costs by 30% by 2003. At the same time it is at the leading edge of auto electronic technology. Sales growth, while partly linked to Toyota's fortunes, can be greater because of the adoption of electronics in autos. For example, Denso is the leader in car navigation and will ship close to half a million sets this year. More importantly though, the company will benefit from the intensifying digitisation of cars, be it in pollution abatement or mobile communication and control. Best of all, its recently spun off competitors such as Visteon (from Ford) and Delphi (General Motors) are showing signs of capitulating to expediency in the face of investor short-termism!

Turning to shares sold, we removed Coke, Kimberly-Clark, Lagadere, Tokyo Broadcasting, Sony and Zhejian Highway. These shares have each been profitable as investors sought the sanctuary of defensive plays. They no longer offer good value.

On the short selling front, we have gradually migrated from the technology sector such as Intel and the chip making companies to financials and consumer sensitives such as Sears and the government sponsored enterprises, Freddie Mac and Fannie Mae.

Currency

Almost every currency appreciated against the US$ in this period. The latter is now seen as risky and notwithstanding their problems, the Euro and even the Yen, for a while, look more compelling. The Fund was relatively well positioned having held by our long term preference for the A$ and the Europeans. At the end of June, 65% of assets were hedged into A$; 22% held in European currencies, with the rest mainly in Korean Won.

BREAKDOWN BY INDUSTRY

Categories	Examples of Stocks	Jun 2002	Mar 2002
Cyclicals/Manufacturers	RMC, Bayer, Linde, Océ	17%	22%
Retail/Services/Logistics	Hornbach, Jones Lang LaSalle, Fraport, Stinnes	12%	10%
Financials	Deutsche Boerse, Alleanza	10%	8%
Consumer Brands	Adidas Salomon, Lotte Confectionary	10%	8%
Technology/Hardware	Toshiba, Samsung, AMD	8%	10%
Software/Media	Mediaset, Nippon Broadcasting, Seoul Broadcasting	6%	6%
Medical	Draegerwerk, Merck KGaA, Novartis	6%	6%
Telecoms	NTT, Verizon, Ericsson	6%	5%
Gold and Other	Gold Fields, Newmont Mining	5%	3%

Commentary

An interesting feature of the unfolding of this bear market is the synchrony across the major markets of the world. From the coverage given on bubble vision (CNBC) one might think that the excesses were confined to US corporations. The trouble is that the excitement of the Internet mania was a world-wide phenomenon and adversely affected the business judgment of management and investors alike. Far from being limited to the new floats of the *neuer markts* of the world, the Panglossian tide swept across the boardrooms of Europe and Asia submerging reason with the promise of a brave new world which required flair and decisiveness. The consequence has been stunning losses of investor equity even in formerly staid giants such as France Telecom 73%; Vivendi 61%; Marconi 99%; Ericsson 73% ; Swiss Life 71%; Reuters 62% (these figures reflect the share price losses in just the last six months!!).

Yes, it is true that US companies probably do deserve recognition as the premier performers in the contest for director self-enrichment and the most creative accounting, but they are not alone. Many great companies are now over-leveraged and operating in markets that are over-supplied. They have lost their operating flexibility and in some instances have surrendered formerly impregnable positions to previously weak adversaries. They are much riskier entities and many will not survive in their present form. Auditor and public scrutiny will reach fever pitch and new legislation will follow. This is leading to a **general de-rating of equities** in all major markets.

The second factor weighing heavily on equities is **currency imbalances.** Like the great empires of the past, the United States now finds itself carrying an imperial burden. Big government is back and the weight on the exchequer is growing. History leads us to believe that the currency is entering a weak phase and the cost of debt (long interest rates) will trend higher.

Over the last few years we have held the view that the unlocking of the potential of the vast labour pools of Asia and in particular China, would suppress the price of traded manufactured goods and thereby cap an important element of inflation. Further aiding this tendency is the falling price of communications which has promoted the development of services which can be performed remotely at low cost (eg. call-centres or software development in India). This would all be fine in an environment of stable exchange rates but as the US dollar cheapens, it may have a **deflationary effect** on world aggregate demand and prices abroad. (US producers are able to win back some export markets while at home, US consumers feel the bite of more expensive imports and associated price rises.)

If one is swayed by the argument that Asia is unable to grow without the help of strongly growing export markets, perhaps deflationary pulses will continue.

We tend to take the opposite view about **Asian growth prospects**, though expecting a lower trajectory than hitherto. The bigger emerging countries of the region have seen their net external indebtedness decline since the '98 crises and bank loan-to-advance ratios have improved markedly. Company balance sheets are much improved and inter-regional trade is flourishing. To be sure, weak currencies have helped to spur exports but an important new development is emerging. Extensive use of consumer credit has changed the balance between domestic growth and that generated by external demand. In Korea for example, spending on capital formation has dwindled from over 35% of GDP in the early 1990s to around 28%, and in its place the consumer's share of the economy has been bolstered to over 64%, from 55% formerly. A strong rise in consumer credit and real wages have driven this but because of the competitiveness and improved solvency, trade is in surplus and net foreign assets have been rising.

The interesting question relates to **commodity prices**. Having now retested the lows last seen in the 1930s in real terms, do they skid further or will tepid growth in the West and improving living standards of Asia result in a gradual shift upwards on account of marginal incremental demand? In nominal terms the emerging economies of Asia seem too small to have an impact, representing about 9% of world output. However, if one looks at output on the basis of **purchasing power parity** (PPP) to take account of their unduly cheap currencies and to give weight to the physical content of their output, one can draw a very different conclusion. Far from being insignificant, a study by Morgan Stanley suggests that China and India on a PPP basis, together account for 17% of world GDP, representing more than twice that of Japan at 7% and just ahead of Euroland's 16%. Should these economies continue to grow at twice or more the rate of developed economies, one could make a case that the real price of commodities have bottomed. This could partially offset the deflationary pulses elsewhere. Equally, it has important implications for commodity producing companies and commodity producing nations like Australia.

Latin America is a different story. The main problem stems from weak institutions. Instead of using the period of strong investment flows from abroad to reform its fiscal recklessness, Argentina squandered the opportunity. The strong currency (then pegged to the dollar) was the final straw as foreign flows faltered and investors realised they would be seeing very little of their $150 billion back. Argentina's economic future looks very bleak.

Brazil has been far more disciplined and is running government surpluses before interest payments of over 3.5% of GDP. However, domestic government debt is very large at 269 billion Reals and interest payments are absorbing around 8.5 % of GNP. Worst still, these government obligations are some 90% inflation or exchange-linked and have a maturity of just 35 months on average. Given the uncertainty of the upcoming election (with the lead being held by Lula da Silva), a throw back to the radical left, a weakening currency and enormous government debt, leaves the country's future on a knife edge. This is exacerbated by a small trade component relative to this large economy. The government has little room to manoeuvre.

Japan is also vulnerable to unstable currencies. Just as it was starting to see the benefits of an export surge due to the weak yen, Japan is again facing obstacles. We have long held the view that the yen is the safety valve in that dysfunctional economy. On a recent trip we were dismayed at the seeming complacency among large employers. The giant electrical companies are a classic example. The cost of tenaciously standing by their worker obligations is putting their technological standing at risk. This year for example, the combined spend on IC chip facilities by the big five Japanese semi-conductor companies will be US$2.7 billion which is about the same as last year. This will be less than that of their nemeses in Korea, Samsung. Keep in mind their sales are more than three times as large as Samsung's. As pure manufacturers, the Japanese are still very competitive but the overmanning of support staff is a major problem. Even so, there are many facets to this enormous economy, which allows stock pickers to find inexpensive investments.

Conclusion

Investors can expect the media to give plenty of attention to whether Wall Street has reached a bottom. We think this will prove premature speculation and follows the normal pattern of false optimism that can be expected after an 18 year bull market (1982-2000).

Our medium term caution is based on the amount of consumption that has been brought forward from the excessive use of debt by companies and individuals, the still stifled criticism directed at key institutions and the willingness of investors to pay such high prices for true earnings (valuations are still too high). Where is investor revulsion caused by these swingeing losses? Money is still hiding in yesterday's winners, new issuance hovers in the wings but as money is withdrawn from equity mutual funds, even wonderful companies will be revalued downwards. **There is simply still too much faith in equities for this to be a fundamental bottom!**

Such a scenario is no fun for fund managers because of the likely volatility. Even with our short positions there are times when we will close positions on a trading view and in all likelihood forego opportunities. Alternatively our longs will periodically fail because of growth and competition proving worse than we anticipated or by our misjudging what is priced into expectations. Hopefully by scouring the world and being prepared to avoid the popular shares we may give investors some protection. In the short term there **could be a decent bounce** on account of the high level of investor pessimism.

Kerr Neilson
Managing Director

"Nasdaq Accounting Definitions"

Following last quarter's comment on accounting nonsense, we were taken by the following "Nasdaq Accounting Definitions" from the internet:

EBITDA – Earnings Before I Tricked the Dumb Auditor

EBIT – Earnings Before Irregularities and Tampering

CEO – Chief Embezzlement Officer

CFO – Corporate Fraud Officer

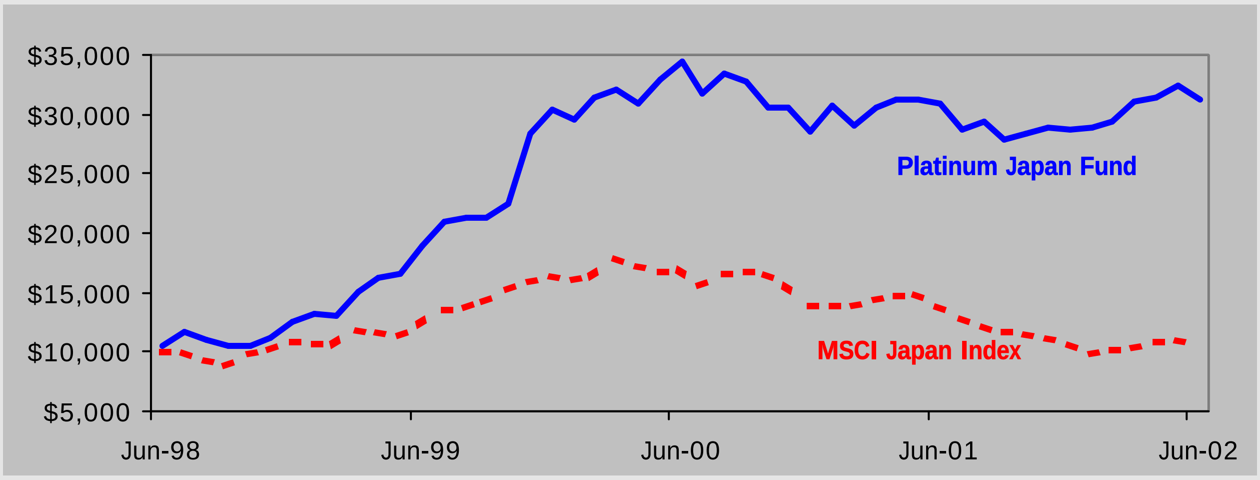
EPS – Eventual Prison Sentence

Platinum Japan Fund

Performance

REDEMPTION PRICE: CUM $1.9024 EX $1.7531

VALUE OF $10,000 INVESTED SINCE INCEPTION (1 JULY 1998 – 30 JUNE 2002)



The Japanese and Korean markets gave up their gains of the previous quarter following heavy falls in the US stockmarket. Japan experienced a fairly modest decline of 3% (in local terms) as global investors continued to favour it as a safe haven from the US turmoil. Within the market there was a major dichotomy as domestic stocks rose at the expense of the traditional foreign favourites such as exporters and telecoms. This was primarily driven by the sell off in the US$ against the yen which tends to favour domestic stocks. Korea was more heavily impacted with a 14% decline as the market took a breather from the large gains made since September of last year. The main impetus for the falls in Korea came from local investors who finally succumbed to poor global investor sentiment. It is worth noting that foreigners have been persistent sellers of the Korean market for all of 2002 as they take profits.

The significant move on global markets during the quarter was the rapid decline in the value of the US$ against all major currencies. In terms of those currencies held in the Fund, the US$ declined by 10.4%, 8.4% and 4.7% against the Yen, Korean Won and A$ respectively. We view these moves as a correction in the US$ from extremely overvalued levels which may well have further to run. In terms of the yen we have not picked up the full benefit of the move because we have been 50% hedged into A$. However we are reluctant to believe that the yen can be a strong currency given the imperative to provide easier monetary conditions for yen based manufacturers. Hence we would expect the yen to weaken relative to the A$ once this period of fear in global markets passes.

The Fund was essentially stable over the quarter, rising by just 0.7% in A$ terms whilst the MSCI Japan index rose by 1.3%. Gains made from shorting stocks such as Tokyo Electron, Advantest and Sharp in Japan were offset by losses on our Korea holdings - Samsung Corporation fell 36% and Seoul Broadcasting was down 24%. Good gains were registered in some of our small stocks in Japan such as Goodwill Group and Pasona, both temporary employment firms. For the year ended 30 June, the Fund rose 1.1% in A$ comfortably ahead of the MSCI Japan which declined by 24.6%.

Changes to the Portfolio

DISPOSITIONOF ASSETS

Region	Jun 2002	Mar 2002
Japan	68%	65%
Korea	20%	25%
Cash	12%	10%
Shorts	18%	16%

The biggest change in the portfolio was becoming more defensive in our Korean positions early in the quarter. We have not really changed our fundamental view on this market but rather we took the view that the rapid price moves since September 2001 and gathering global concern made it prudent to trim exposure. By quarter end we had reduced equity exposure from 25% to 20%, by selling our holding in LG Chemical which had been a star performer for the Fund rising from 15,000 won to 45,000 won in six months. We also raised our short position against the Kospi index from 5% to 8.5%. In the current environments we would look to add to our exposure again if the market pulled back to around the 650 level.

In Japan, we reduced our short positions against both individual stocks and the Nikkei Index toward the end of the quarter as the market adjusted to levels which represent good support. Shorts against Japanese stocks now represent **9%** of the Fund as against 16% in the prior quarter. The remaining short positions are against the likes of SMC and Keyence, highly valued machinery stocks with little prospect of immediate growth. Within the portfolio additions were made to Takeda, Denso, Credit Saison and Sky Perfect. We financed this by selling positions in Yamaha Motor, Towa Corp, Noritake and Air Liquide. The basic approach we are taking is to add good value, quality franchise, larger capitalisation stocks as the markets adjust downward. This will be at the expense of smaller names which whilst still fundamentally sound, don't represent as much relative value as they once did.

Commentary

During the quarter we visited 20 companies in Japan including many of our existing holdings. It was a very valuable experience as we were reminded of the immensely strong manufacturing base that the country still has despite 10 years of dithering at the national level. You can confirm this yourself by noting the number of Japanese brands still prominent in the household today (with a few Korean intrusions!). The point is that through this period of economic stagnation Japanese companies have continued to invest in modern facilities, processes and the R&D essential for new product development. It's not perfect however and there will be losses caused by duplication of effort and resistance to change. However it stands in stark contrast to the US model which in recent times has placed an emphasis on "high grading the franchise" by investing little and pulling forward demand. History shows that long term wealth creation is driven by those prepared to put in the "hard yards" and in this sense, maybe it is time for the Japanese model to shine once again.

The strength of Japanese manufacturing is best highlighted by the success of Toyota. This company has shown incredible devotion to its pursuit of global market leadership and has seen its share of the global auto market rise nearly every year since its establishment (currently 10%). In the beginning its success was based on the revolutionary lean production methods it pioneered and despite these processes being dutifully copied by competitors, it still holds cost leadership to this day. Lately the success has been built on things not often associated with Toyota. New technologies from its R&D spending are coming to fruition, the most high profile of which is the successful launch of the hybird electric vehicle. Against earlier scepticism, the company has achieved remarkable success with its Lexus range which has proved highly successful in competing against the luxury German brands. Today, Lexus accounts for 25% of its sales in the US market and much more of profits! We have chosen to play Toyota's strength through its listed auto components affiliate Denso.

Denso is a $18 billion sales organisation with great breadth of product range including air conditioners, fuel injectors, electrical controls and telematics. It is positioned as an integral part of the Toyota machine with 50% of sales to Toyota but more interestingly, with very high R&D spending it acts as the engine of growth for many of the newer technologies coming out of Toyota. Combining this with the fact that the other half of sales outside of Toyota gives it a special position in price negotiations with the parent. The stock appears very modestly priced for the high level of certainty attached to earnings growth. We see growth from gains in market share by Toyota on a global scale as well as secular growth from greater use of electronics in vehicles. The introduction of 42 volt platforms later this decade and greater consumer spending on car navigation and other electronic gadgets provides a solid underpinning. In addition, Denso was very upbeat about supplying to the US makers. It highlighted the chronic underspending by Delphi and Visteon once they were spun out of their parent companies (GM and Ford respectively) in order to meet Wall Street expectations. These latter companies are now calling on Denso to provide high specification products where their own technology has fallen behind.

TRENDS IN DEBT/EQUITY RATIOS – BIG FIVE JAPANESE ELECTRONIC COMPANIES

Company	3/98	3/99	3/00	3/01	3/02
Hitachi	0.8	0.9	0.9	1.2	1.3
Toshiba	1.8	2.0	2.0	1.7	2.6
NEC	2.0	2.7	2.0	1.8	4.0
Fujitsu	1.6	1.6	1.3	1.3	2.0
Mitsubishi	2.8	3.1	2.4	2.0	2.8

Of course Japanese manufacturing companies are not without their blemishes. The inaction of the past 10 years has resulted in much wasted investment and this is best highlighted by the problems currently afflicting the large technology companies such as NEC and Toshiba. These companies once epitomised Japanese economic progress and were held in high esteem for their technical and manufacturing excellence. They harnessed the energy of their employees to move from business to business and drive the Japanese economic miracle. However they have become top heavy and once others had mastered their tricks in manufacturing their relative competitiveness dwindled. The end result are corporate dinosaurs employing too many people and making too many products. We would estimate that the companies have to shrink their sales by 30-50% to make them viable. As the table above shows, both Toshiba and NEC have been pushed to the verge of bankruptcy (these numbers would be worse if we adjusted for intangibles, making NEC technically insolvent!).

This is not to say that there are no good qualities in these companies. They have great technical depth but this is suffocated by an overlay of debt and unprofitable businesses. It is also troubling that they do not seem to fully appreciate the extent to which they have lost choices. When we visited Toshiba it was apparent that after initially having some success in the late 90s with restructuring, they felt that they had done enough by laying off 10% of the workforce and exiting D-rams in the past year. The problem with this is highlighted in the table below. The semiconductor business is seen as one of the core businesses of the Japanese technology majors and for Toshiba, it is their main business. R&D and capital spending is the life blood of semi-conductors yet the Japanese companies have pushed themselves so close to the edge that they can't continue to invest to support the current level of sales. As the table illustrates, the big five are spending less than Samsung this year to support sales that are more than three times as large! What's more, they are doing it in businesses where their individual market shares are very low which makes it very difficult to ever make high returns.

COMPARISONS OF SEMI-CONDUCTOR BUSINESSES (US$BN)

	2001	2002 est
Sales		
Big 5 Japan	31.0	36.2
Samsung	7.4	11.2
Operating Profit		
Big 5 Japan	-5.8	-0.3
Samsung	0.6	2.7
Capex		
Big 5 Japan	5.1	2.7
Samsung	2.1	2.8

Our feeling is that a huge wakeup call will be delivered to corporate Japan through the inevitable failings of these companies and that this could reshape fundamental beliefs within the country. Whether it is through bankruptcy (unlikely as the government will underwrite the companies) or radical restructuring (more likely), these companies will be changed forever. In many ways Korea is a great leading indicator for what will happen. We can liken Toshiba and NEC to the failed chaebols Daewoo and Hyundai and highlight Samsung Electronics as the guiding light for what can be achieved if the hard measures are taken.

The general impression from our meetings was that the larger companies, which have huge employment burdens, are doing little to cut these costs aggressively. However NTT surprisingly seemed to be adopting a more aggressive approach. It is always hard to exactly pinpoint why some Japanese companies choose to change but it seems in NTT's case that operating losses in the fixed line business have finally spurred a reappraisal of employee salaries within the company. The source of NTT's problems is not so much the number of employees, which at 213,000 is in line with international comparables, but rather the amount they are paid; on average of 11 million yen or A$160,000 per annum. To reduce these costs the company has instituted the following measures:

1) All employees over the age of 50 (100,000) will have their salaries plus bonus cut by 26%. This saves the company ¥286 billion per annum although it will pay lump sum payments over three years totalling ¥567 billion as compensation. In addition retirement age will be extended to 65 from 60.

2) The company is tightening up on employee benefits such as low rent housing and special payments for telecom services. This will save ¥20 billion per annum.

3) 4,400 people will take early retirement in the March 2003 year at a one off cost of ¥48 billion.

4) The company is also continuing to cut capital expenditure and sell off real estate holdings.

The sum total of employment cost savings are ¥354 billion per annum which accounts for about 14% of total employee costs. Depreciation will also fall heavily as capital expenditures have been cut from 26% of sales to 20% in the last three years. This heavy cut to fixed costs is underwriting a thriving free cash flow position and improvements in operating earnings. Given the beating the stock has taken over the past two years these are encouraging trends. Longer term the company is well positioned in fibre to the home internet solutions although for the present ADSL seems to have the running and there is strong price competition. However this seems to be abating as the main culprit, Softbank, is in financial difficulty. To become more positive we would need to see the company enunciate a strategy which targets a return on capital in the fixed line business above its cost of capital.

A common myth about Japan is that one shouldn't invest there because of the ageing population and consequent lack of economic growth. Of course, this argument could be applied to most western countries and hence really serves as a convenient excuse to attack the failings of the Japanese economic system. Rather than address the complex argument about ageing and growth, it is clear that the argument masks the underlying dichotomy within the economy and hence the opportunities created for stock pickers.

There is a large pool of young people in Japan and their spending habits are as progressive and novel as anywhere else. They pioneered SMS, love blonde colourants, are glued to MTV and are developing a passion for credit. We believe that any portfolio in Japan should take account of this younger generation and try to identify the types of industries that benefit from their spending patterns. By contrast the older generation will struggle with the broken social contract and will suffer from inadequate pension funding. The government is also talking about changes to gift taxes, which if enacted could lead to a diversion of wealth to the young.

Along a similar theme we are interested in those companies in the newer industries that don't play by the old rules of corporate Japan. They tend to be run by younger executives who speak English and are open to foreign ideas. A good example of this is the temporary employment firms.

Outlook

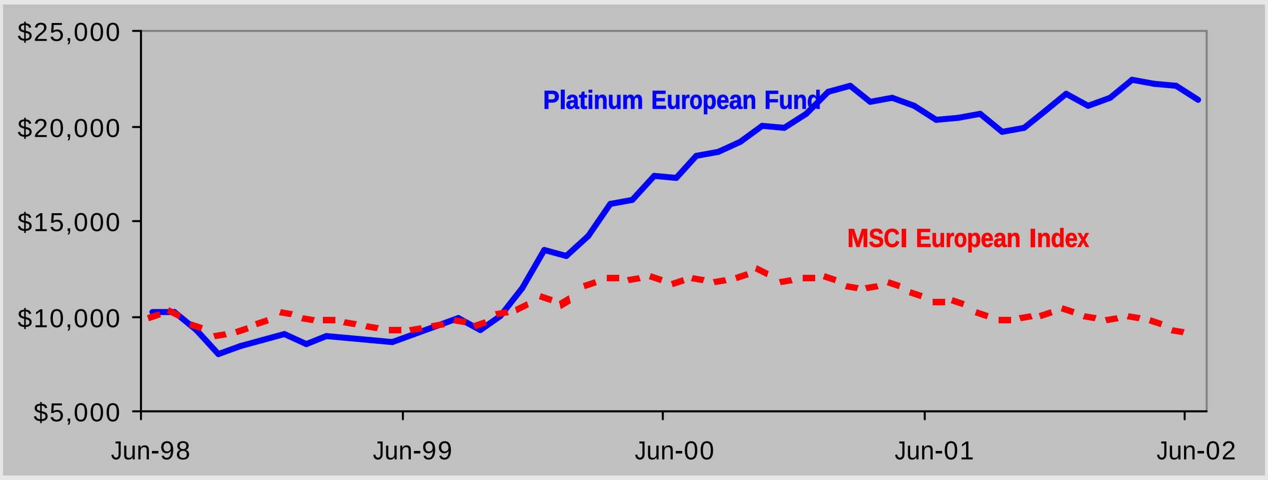
We are relatively optimistic about Japan and Korea because we see a structural change toward higher corporate profits in their economies. The biggest problem is clearly the impact on exports of the fallout from the adjustment of US economic imbalances. If the US consumer retrenches, these markets will take a further downward adjustment. However, we are positioning the portfolio on the basis of modest growth in the US and Europe. There is a bias towards domestic growth stocks in both Japan and Korea, although select high quality export names will be bought on weakness. We would become fully invested if the markets decline further from current levels.

Platinum European Fund

Performance

REDEMPTION PRICE: CUM $1.7262 EX $1.6138

VALUE OF $10,000 INVESTED SINCE INCEPTION (1 JULY 1998 – 30 JUNE 2002)



Bear market gathering breadth, telecom and technology stocks capitulating

European share prices were down heavily in the three months to 30 June 2002, led by capitulation in the "bubble" parts of the stock market: telecom equipment -47%, computer services -40%, computer hardware/software -38%, telecom services -32% and media -27%. Insurance companies (-20%) suffered in sympathy with stock markets, despite the strong bond market (German ten year yields rallied from 5.25% to 4.95% over the quarter). It is noteworthy that several growth-sensitive parts of the market fell, as doubts crept in over the strength (and timing) of the much-heralded global economic recovery: auto parts -17%, manufacturing -17%, and industrial products -20%. Perhaps most tellingly, only one sector (tobacco, +2%) was up for the quarter, and that is hardly an inspiring area of the stockmarket.

As the sector movements suggest, the bear market in stocks broadened these last three months. Of the 500 largest European listed companies, just 13 saw their share prices increase by over 10%, while 180 had declines of over 15% and 50 lost a third or more of their market capitalisation.

The MSCI Europe index was down 15% measured in local currencies, while a steadily strengthening euro (particularly against the US$, but also versus the yen and Australian dollar) reduced the index loss to 9% measured in A$.

The Platinum European Fund was down 5% in the quarter. The Fund had solid performances from most of its large holdings (especially Stinnes, Hornbach, Novozymes, Givaudan, SGS Surveillance) and some protection from the short positions (especially Nokia, Adecco, AstraZeneca). However these were offset by the weakening of the previously steady "mid-cap" (market capitalisations of Euro 1 billion – Euro 10 billion) part of the stock market where most of the Fund is invested, and also by three holdings – Ericsson, Hagemeyer and Serono – which performed very poorly. In addition, our decision to expose two thirds of the Fund to the A$ (and only a third to European currencies) was costly given the 7% appreciation of the Euro against the A$ over the period.

Commentary

European stocks fell more than US markets despite many US-domestic problems

The performance of European equity markets in the light of the US problems of crooked executives etc illustrates the point that in fact the front page headlines are merely coincident, perhaps catalytic, but not the core of the problem. Simply put, western world sharemarkets are expensive after the two-decade bull market, and just as European stocks climbed higher than their US counterparts in the 1990s, they are falling faster today. This is partly due to the constituents of the index (telecoms etc are (were!) a larger part of the European than the US indices), but also due to the depth of the markets – in Europe the public enthusiasm for shares was a wildfire which was quickly extinguished. Hence the price adjustment.

By 1999/2000 valuations of the "new economy" stocks were, as we have written about for ten quarters, wildly optimistic. The issue today is what to make of valuations in the broader market. Clearly investors are now starting to discount a recession of some sort, after last year's patchy slowdown was reversed through very low central bank interest rates (falsely?) propping up housing and consumption. The first thing to say is that in general we feel positive about markets when we find a lot of modestly valued stocks. During the sell-off of August/September 2001, this was clearly the case, and at the extreme of the selling in the nine days following the World Trade Centre attacks, we put all of the cash in the Fund into the market.

Unfortunately things are not so tempting today – either we are failing to find the interesting investments, or they are not yet available. Indices have returned to the September 2001 lows, but this is disproportionately due to the collapse of technology/telecoms (ie. the decline of the erstwhile high capitalisation technology and telecom stocks harmed the indices but the rest of the market has fallen somewhat less). The great companies are still expensive, the weak and/or indebted companies' prices are low but these shares are dangerous rather than cheap. We are working in the middle ground, and trying to address the question of relative valuations and risks. For example the shares such as Adidas, Siemens and Linde to which we added aggressively in September are 70%, 50% and 35% higher respectively. Where and when should we be selling out of those in preference for other stocks which have fallen more than the fundamentals justify? We have been running 20% cash and 10-15% shorts for most of the quarter for a net exposure of under 70%. Not until we see many interesting valuations will we be likely to take this net exposure back over 90%.

Ericsson, Hagemeyer, Serono – all very weak, Fund adding to all three (gently)

As mentioned above, three of the Fund's holdings have performed very poorly. Ericsson is a stock which we bought at around SEK40 in mid 1999 and sold over the subsequent eight months for SEK150-205. The stock peaked at SEK229 in March 2000 and was back at SEK44 by early 2002. Somewhat unimaginatively we again bought a modest position at this level, and have regretted it ever since. We reduced the position at SEK28 and have since added to the position at prices down to SEK14. Today it is SEK15 and some commentators have questioned the likelihood of Ericsson's survival. The company has little debt today but faces a difficult couple of years and heavy cash expenses as it cuts staff to focus on its core area of mobile telephony infrastructure. In this field it remains the clear world leader, however doubts over the timing of mobile telecom operators upgrading to "third generation" kit means that this leadership position is not yet yielding profits. Our view is that the product strengths (both its existing customer base and its powerful "3G" offering) of this company means its place is not easily usurped, although clearly the lax attention to cost management of the past needs to change quickly (which it is). More to the point, the absurd financial position of many of Ericsson's customers is being confused with the prospects for broadband mobile telephony (which we believe are sound). Thus at this very low price, but with the recovery in Ericsson's profitability still some quarters away, we have been adding gently and have around 2.5% of the Platinum European Fund in the stock as at 30 June.

We wrote about Hagemeyer last quarter and suggested we would get another chance to buy the stock. With the continuing weakness in the US and German industrial economies, and the evidence that the restructuring story of Hagemeyer is a "work-in-progress", the stock has come back under Euro15 versus our E19 entry price (December 2001) and the peak of E26 it achieved a few months later. We have spoken to the management twice in recent weeks (once face-to-face, once by phone) and are adding gently to the position as the continuing low volumes at their customer facilities offsets the attractive valuation. 3% of the Fund is invested in Hagemeyer, but we are not yet making it a very big position, as the risks associated with the transformation of the company could result in further panic sell-offs in the stock.

Serono is a “biotech” stock based in Switzerland, which performed strongly after our February investment, when in March they received US FDA approval to sell their most important product (Rebif, for multiple sclerosis) in the world's biggest market for drugs. This approval, along with some important technical backing from the FDA allowing Serono to claim superiority over the existing treatment, is a transforming event for the company's profits over the next five years. This happy scenario, however, has become secondary to the US-led capitulation in biotech stocks. With even the heavyweight champion Amgen succumbing (it has fallen from $60 to $37 in three months), Serono was bound to follow its sector down and is now 25% below our CHF1,240 entry price. We have been adding to the stock because although other (much smaller, very narrowly focused) biotech companies are available at valuations near or below their cash balances, they have no prospect of earnings soon, while Serono's earnings are growing strongly due to the Rebif approval. Clearly in this economic environment, growing earnings streams are not so common. The Fund has 2% in Serono and is adding carefully to the position.

Portfolio Activity and Outlook

BREAKDOWN BY INDUSTRY

Categories	Examples of Stocks	Jun 2002	Mar 2002
Chemicals/Materials	Linde, Givaudan, Merck KGaA, Novozymes	18%	18%
Miscellaneous Services	Hagemeyer, Fraport, Stinnes	17%	21%
Retail	Kingfisher, Rinascente, Hornbach	12%	8%
Capital Goods	Océ, Schindler, Siemens	11%	13%
Consumer	Adidas, Michelin, Henkel	10%	11%
Health Care	Novartis, Serono	5%	7%
Financials	Deutsche Boerse, Alleanza, Assicurazioni Generali	4%	8%
Tech/Media	Ericsson, Intentia	4%	4%

Outlook – dare we say it again? – difficult!

As this report is being written various events are occurring in Europe which may point to a short term crescendo in the selling, with many of the bull market leaders having capitulated. In Paris there is talk of the government “renationalising” France Telecom. The state owns 56% of the company, and with the shares down 96% (ninety-six percent) since their peak, the 44% minority owned by investors is worth only E5bn (A$9bn). France Telecom has over E60bn of debt and needs to be recapitalised (anyway, but short term to avoid its credit rating being lowered to “junk” status with the attendant increase in interest rates it would then have to pay, leading to more debt etc). Clearly since the French government would have to put up over half the money in a rights issue, it makes economic sense to reabsorb the company so that it pays French government interest rates instead. Economic sense, maybe, but politically? The company was bought by (over one million, voting) French individuals for E28 in 1997 so they may not like being relieved of their stock for E10-15 per share. More interestingly, the French government is pondering the “capitalist failure” tag that may apply if they take the company off the stock exchange. It will be an interesting debate, but the point is that resolutions are starting to be considered for the stocks which have led the bear market thus far.

Another event (also in Paris) which suggests change is the sacking, by the French business establishment, of the once-lauded Jean-Marie Messier who has presided over the transformation of the profitable water utility Generale des Eaux into the debt laden, loss-making Vivendi Universal. His rise and fall marks the western world cycle of greed and misjudgment that perhaps best explains why European stock markets have been unable to resist the lead of Wall Street in both the bull and bear markets.

As implied in the discussion above, we see a good chance of a broadening sell-off in markets, to which the Platinum European Fund obviously will not be immune, but from which the Fund may find some good investment opportunities in the months ahead. To reiterate, the broad market is now dependent upon the progress of the world economy, but there are surprisingly few bargains available at the moment.

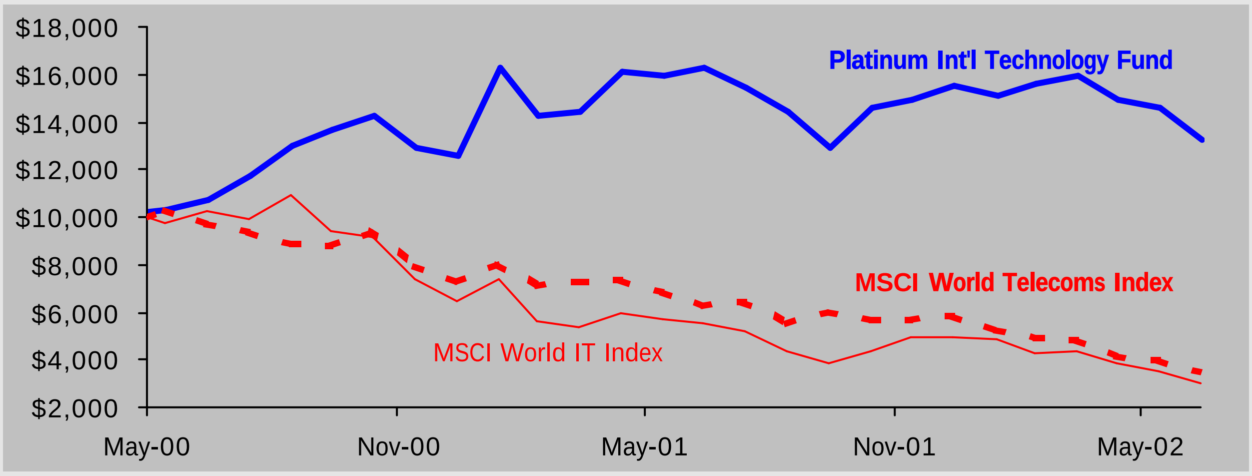
Toby Harrop
Portfolio Manager

Platinum International Technology Fund

Performance

REDEMPTION PRICE: CUM $1.0336 EX $0.8498

VALUE OF $10,000 INVESTED SINCE INCEPTION (18 MAY 2000 – 30 JUNE 2002)



The Fund fell 17% in the last quarter as the onslaught of pessimism regarding technology and telecom stocks continued. During the quarter the MSCI Information Technology (A$) index and the MSCI Telecom Services Index (A$) fell 31% and 28% respectively. For the last 12 months, the Fund fell 19% versus the falls of 44% for both the technology and telecom benchmarks.

Although a reasonable outcome for the quarter, it is somewhat disappointing given the Fund's net invested position of less than 50% for most of the period. As we move into what is likely to be the final stages of the bear market in technology stocks, a number of the Fund's holdings saw markdowns of 50% or more. Although the Fund did receive good returns from its short positions, these only provided a partial offset to the poor performance of the Fund's long positions.

Changes to the Portfolio

DISPOSITION OF ASSETS

Region	Jun 2002	Mar 2002
US	45%	35%
Other Asia (incl. Korea)	12%	13%
Japan	13%	13%
Europe	3%	7%
Cash and Other	26%	32%
Shorts	25%	19%
Net Invested	49%	49%

BREAKDOWN BY INDUSTRY

Region	Jun 2002	Mar 2002
Semiconductor	23%	18%
Electronic Components	11%	10%
Software	8%	12%
Telecom Equipment and Suppliers	18%	11%
Other	14%	17%

During the quarter, the Fund topped up a number of its holdings across the portfolio as prices fell. New additions include Verizon and EDS. Verizon is one of the US incumbent telecom operators. Not only does Verizon own the only profitable wireless phone business in the US, it has the benefit of diminishing competition in its local telephone operation as the threat of new competitors recedes as well as having negligible revenues from the very competitive long distance market. EDS is one of the leading providers of outsourced information technology infrastructure for large companies. The stock was hit heavily late in the quarter as a result of the collapse of Worldcom (which is both a customer and a provider of telecom services to EDS) which gave the Fund the opportunity to add to its holdings at attractive levels.

Outlook and Commentary

The quarter ended with the furore over Worldcom's US$3.9 billion accounting fraud and subsequent default on US$4.3 billion of bank debt. Although we would not dismiss lightly the fraudulent behaviour of senior management and the incompetence and/or conflicted position of the auditors, a rather more important point is generally being overlooked. How could a company that generated over US$20 billion in annual revenue from selling basic telecommunication services to a wide range of business and residential customers be unable to generate returns that would allow it to service its debt?

The central problem (amongst many) at Worldcom is that it is in an inherently bad business. The provision of long distance telecommunications services is a pure commodity with the price being the only differentiating factor, and it now faces a market with massive excess capacity. Over the last eight quarters we have written often about the bull market myths of endless growth and the errors that were made as a result by both corporate managements and investors. What is being revealed today is another set of myths about the quality of many of the technology and telecom businesses that the market once loved.

During our visits to Silicon Valley in 1999 we were often met with compelling stories about a given company's lock on their market. For many of the small semiconductor companies the story was often the same. The company had designed a chip for a particular function inside a router or a switch or some other piece of telecom equipment and was the only company or maybe one of two companies that had such a product. The chip had been designed into a number of products of the big equipment companies such as Cisco or Nortel and the company was having good success with additional "design wins". Even if a competitor came along with a new chip the company had "the slot" on the circuit board and the customer would have to completely redesign the board should a replacement chip be chosen. Something they wouldn't do when "time to market" was of utmost importance in a fast changing world. Besides there was a shortage of components. There was little point of competitors trying to break in so they were limited to targeting the next generation of higher speed components. Of course, to do this would require significant capital and intellectual property outsiders lacked. Meanwhile, the company already had products that were being sampled by customers. This type of story was repeated many times and when put together with annual revenues of US$250 million to US$700 million and growth rates as high as 100%, one's critical faculties were deadened. Companies with these type of stories achieved market valuations as high as 50 times their prevailing annual revenues.

Unfortunately for investors, in most cases the lock on the customer was an apparition. One of the best examples of this is Broadcom which had a dominant position in selling chips to the makers of cable modems and was regularly quoted as having a market share of over 90%. In the last 12 months, Texas Instruments has made major inroads into Broadcom's share with new products which has seen them win business from Motorola, the largest of the cable modem makers. In our recent trip to Silicon Valley we visited Cypress Semiconductor who are now taking share in the market for "physical layer" chips used in telecom equipment. It turns out that in tough and slower times it makes good sense for the equipment company to redesign a circuit board in an attempt to lower costs. Although Cypress is a strong company, it is a new entrant in the telecommunications area, having operated primarily in the unrelated area of specialty memory chips.

Another of the great stories of the tech boom was that of EMC. EMC makes computer storage systems. These systems, are at the simplest level, a huge array of hard disk drives that are connected to computers for the purpose of storing data. EMC's leading position in storage was a result of their ability to address the entire storage market. Their systems could be connected to an endless number of different computing platforms whether they be mainframes, different varieties of the Unix operating system, or the Windows NT platform. By comparison, their competitors were the computer companies who made storage systems that only operated with their own machines. As most large companies run heterogenous computing environments, EMC was the only offer that would allow them to standardise the management of their data storage. For a competitor wanting to emulate EMC's position, they faced the daunting task of a product that worked with a full choice of alternative systems.

The barrier to entry may have been high but if there is enough incentive (and the profitability of EMC certainly was) then someone will try and jump it. Hitachi Data Systems developed a platform that while perhaps not EMC's equivalent, was good enough to provide serious competition and impact EMC's pricing power. Other changes were also taking place. Storage area networks (or SANs) are a relatively new configuration where the storage is attached to a network rather than attached to a specific computer. This was meant to be a boon to EMC as companies consolidated their storage to SANs, but SAN switches developed by the likes of Brocade, have allowed companies to achieve interconnectivity between different computing and storage systems, removing one of EMC's key advantages. Another development was "network attached storage" systems from Network Appliances that compete with EMC at the low end. None of these developments will particularly result in EMC losing its leadership position but they do imply a more competitive and thus less profitable position for the company.

Elsewhere we note the successful launch by National Semiconductor of its GSM cellular phone chip set and the implications for Nokia and the other handset companies. National has long held a strong position in the chip market for cellular phones. Typically it has sold around US$2 of chips per phone made by the major handset companies. The company's new 4-chip set for a GSM phone integrates most of the functions provided by semiconductors in the phone and is being sold for US$18 versus the typical cost of US$25 per phone. Although the cost differential is a nice saving, the original goal was to provide low end phone makers with a solution that would allow them to sell US$50 phones in markets such as China. The first phone launched using the chipset is the Ericsson T66 which has been positioned as a high-end phone and sold for around A$500 in the UK. The fact that a chip set designed for a low end $50 phone provides the same functionality as a high-end phone we would view as a devastating outcome for mobile phone manufacturers.

In the early stages of the technology bear market the unsustainable "cash flow negative" business models of the "dot coms" and the start up telecom operators were abandoned. Then we had the realisation that the market would not grow in a straight line forever and that in fact the recent good times were simply a function of easy money created by the central banks. The final revelation is that technology businesses are just like any other but with additional risk of the rapid pace of technological development. What makes a good technology business is no different from what makes any business a good one. It may be a special position in the market, such as the likes of Microsoft and Intel hold in PCs, or that a Telstra or Verizon has with its strong grip on the residential telephone customer. It may be a corporate culture that inspires excellence in its employees. Rarely though will "intellectual property" alone provide a ***sustainable*** competitive advantage.

In the last quarter we have seen many of the Fund's holdings hit hard with some falling over 50% from levels we thought to represent good value. Companies such as Agere, AMD, and Parametric we believe have strong positions in their respective markets but face the common problem of low demand for their products today. As they struggle to deal with cutting overheads to levels appropriate for current output, the losses being incurred are not insignificant. Nevertheless, the very low valuations on these stocks should start to provide some support for the share prices from here on. Current levels for many stocks represent attractive levels for potential acquirers and we would expect to see a pick up in takeover activity in coming months. This is not to predict the beginning of a new bull market in technology stocks as a full recovery in demand is still some way out. Further, many leading technology companies are priced as if their businesses are in some way "special". Until investors treat technology as just another sector of the stock market, these companies continue to make good short positions for the Fund.

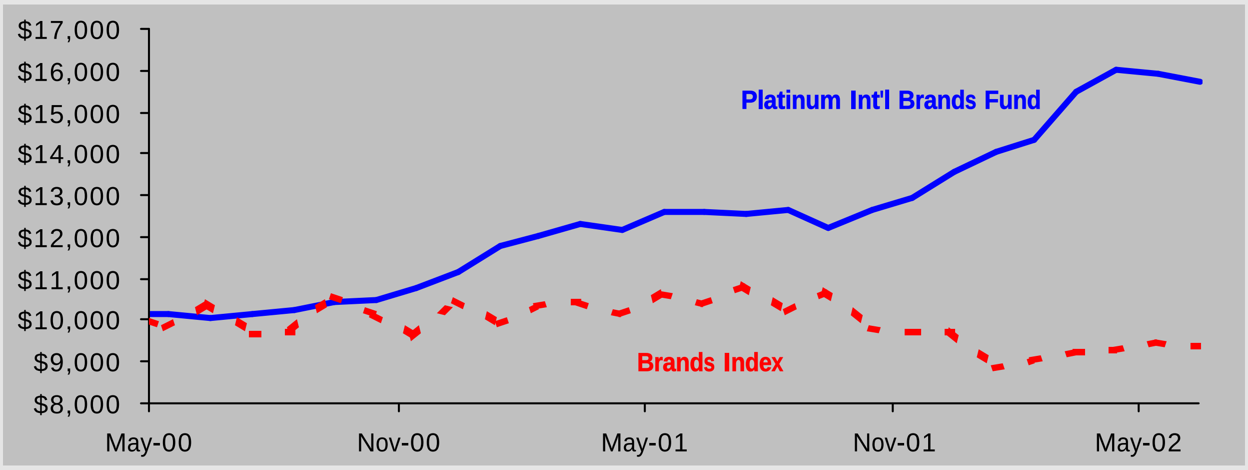
Andrew Clifford
Portfolio Manager

Platinum International Brands Fund

Performance

REDEMPTION PRICE: CUM $1.5130 EX $1.4247

VALUE OF $10,000 INVESTED SINCE INCEPTION (18 MAY 2000 – 30 JUNE 2002)



The International Brands Fund rose by 25.2% over the past 12 months. Our proprietary index of branded goods and services companies fell by 9.7%, whilst the MSCI World Index fell 23.2% over the same period. Clearly the defensive nature of consumer goods and retailers attracted investors in these uncertain times. The top performing stocks in the brands index were, Tyson Foods up 49%, Wendy's (restaurants) up 40% and Electrolux up 30%, with many of the other positive contributors being brewers, beverage and household products companies. At the other end of the scale there was a preponderance of retailers, Kmart losing 92% of its equity value, Gap 57%, and luxury goods companies such as Bulgari losing 46% and Estee Lauder 25%.

In the quarter, the International Brands Fund rose 1.7%, matching our brands index, whilst the MSCI World Index fell 13.6%. Nearly two thirds of the companies in our brands Index declined in price over the quarter with many of the worst performing companies being the retailers and luxury goods companies;

- Shares in Carlsburg, the Danish brewer were a stand out rising 22%, UK brewer Scottish and Newcastle rose 10% as both these companies re-organised themselves and expanded their reach into the fast growing Russian and Baltic markets. In the US, the brewers fared less well with the dominant Anheuser Busch falling 8% whilst Adolph Coors, the number three brewer fell 14.5%. South African Breweries (up 7%), one of the five largest brewers in the world, announced a US$5 billion takeover of Miller, the number two brewer in the US. This continues the trend of consolidation within the sector and encouraged further speculation that other large mergers or takeovers would occur.

- Retailer stocks lost significant value in the quarter, Kmart losing nearly 40% whilst Home Depot, Safeway and Best Buy were significant with 30%+ losses.

- Clothing and Footwear stocks were mixed, with support from the Soccer World Cup assisting Adidas-Salomon to rise 7%, whilst clothing stocks such as Hugo Boss lost 25% on issues of accounting and inventory management in their US subsidiary.

- US food companies generally suffered share price declines, Heinz lost 5%, as did Sara Lee whilst Campbell Soup fared marginally better. In Europe the picture was more positive, Associated British Foods gained 18% and Unilever showed progress on their restructuring and gained 10%. Associated British Foods is considered a particularly defensive stock especially since it holds 20% of its market value or £1 billion in cash.

- Other notable share price movements include strong performance from some of the Japanese companies including Shiseido appreciating 21%, Kao 17% and Japan Tobacco up 9%, consistent with a defensive theme.

The noteworthy performances within our Brands Fund include once again Lotte Confectionery and

Puma, as well as Adidas-Solomon and Campari. We sold our positions in Coke and Kimberly-Clark at attractive prices before they sank back later in the quarter.

We increased our holdings in Japanese companies and added two new names, Nintendo (games) and Sky Perfect Communication (multi-channel broadcaster), to the portfolio. In Europe we increased our holdings in Adidas-Solomon, Michelin, Hunter Douglas (window blinds) and the retailers Douglas Holdings (perfumeries), Kingfisher (home improvement retailer) and Rinascente (department stores) and introduced some new names including the cosmetic and skin care company Clarins, and the retailers Casino Guichard and Hornbach Holdings.

Clarins, the French family owned company, produces and markets, skin care products, beauty products and makeup. The group also produces perfumes such as Chrome by Azzaro and Angel by Thierry Mugler, the best-selling perfume in France. Clarins has strong research in developing plant-based skincare products and is now a market leader in Europe with its leading brand Clarins. Last year the company dealt with both the external influences of weak markets as well as struggling with relocating to a new logistics centre. As a consequence profits fell over 40% along with the share price. Looking forward, the worst of the logistic centre problems appear to be over and we would expect to see profitability recover this year. Sales for the first quarter to March 2002 were up an encouraging 8.8% with the key Clarins brand growing 13.6%, providing some comfort that a rebound in profits might be underway.

Casino Guichard, a French company with supermarkets, hypermarkets, convenience and discount food stores, has a very strong market position in Paris and South Eastern France. Casino has the advantage that a relatively large part of its portfolio is small inner city stores (Monoprix, Petit Casino), which are experiencing better growth than large out of town hypermarkets (Geant), as French shopping habits change. The company is enjoying good profit growth from the success of its growing network of hard discount food stores (Leader Price), and operational improvements in its traditional supermarkets (Casino).

Commentary

We are witnessing a number of the leading branded goods companies redefine their businesses, many are divesting assets once described as core and practically all have some form of cost restructuring. So is this natural evolution or are other factors at work? Unfortunately we believe that many of these companies did not respond either appropriately or with sufficient foresight to the changing circumstances of the past decade.

Examples in just this quarter, Heinz has sold its 9-lives pet foods, Starkist Tuna and Natures Goodness baby food businesses. Danone, known for its dairy products has sold the majority of its US bottled water business to a joint venture company with Coke, having previously divested its Kronenbourg beer business. Unilever has a program to significantly reduce its brand portfolio to 400 brands from 1,600 brands, whilst Gillette announced last year that it would cut its product lists by 75%.

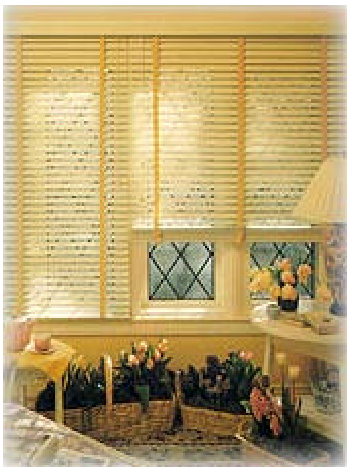
So how did this come about? Many branded goods companies were faced with similar problems. They were struggling to grow their revenue as geographic expansion proved more difficult than expected. In the early days companies like Kellogg led the way with expansion to overseas markets, with Australia one of their first international expansions. As the “easier” markets were exploited so these companies turned to the developing markets of Asia, Latin America and more recently Eastern Europe and

China. Profitably developing these markets proved to be more difficult and painfully slower than many (American) management teams had expected. Western breakfast cereals are crunchy, sweet and cold, breakfasts across Asia are soft, savoury and warm. Global scale is not the answer.

Meanwhile the retailers were changing. The smaller independent stores were disappearing and larger more demanding supermarket chains emerged. Over 80% of US households (88 million US households) now shopped at WalMart. That makes for significant bargaining power and margins at the branded goods companies are under pressure.

The branded goods companies reacted, introducing what they termed “range or brand extensions”. Variations of the original brand, invariably with the tag “new” or “improved”, often with very little real difference but at a higher price. They believed that levering off the equity of the core brand was a less risky and cheaper option than trying to research and build a genuinely innovative new brand or product.

In Europe, over 500,000 new items are introduced annually with a 90% failure rate in the first year. According to AC Nielsen over 90,000 new consumer items are introduced to the UK each year with a similar 90% failure rate. It all became a treadmill, as most new launches had short lives, more were required to compensate for the loss of momentum of earlier launches. To try and break the circuit they started buying other brands and companies, hoping that if they could become large enough they would gain some bargaining power against the ever more powerful retailers.



In the US, visits to the supermarket have declined nearly 20% over the past five years with the average shopper spending 21 minutes in the store and selecting only 18 items from the 22,000+ available. These shoppers are also faced with 360 new products (and variations) each week! To make things harder for the branded goods companies, the advertising industry became very fragmented. P&G’s CEO recently commented, that in 1960 it took only four network TV stations and 18-20 radio stations to contact 70-80% of consumers, now it takes up to 100 different commercials to reach the same audience.

Further research suggests that 80% of brands have less than a 1% market share and that 80-85% of consumer needs can be met with a mere 150-200 products. Retailer's shelves have become cluttered and confused and quite often the most profitable major selling product runs out of stock with the resultant lost sales. Studies show that 48% of all items are out of stock at least once a month. In an attempt to address the problem of inadequate stock of leading brands, retailers are reducing the ranges. An example in Asia resulted in P&G’s haircare range being reduced by 38%, volumes rose 7% and out of stocks fell 50%.

Consumers became more demanding, seeking better performance from the products, newer versions, added ingredients (eg. vitamins), lower fat levels, and unbelievably, washing powders that actually worked. Groceries, packaged goods, household products and many personal care products are functional items and consumers are adept at the value equation. These may be branded goods but they are a far cry from the romance and imagery of beauty, fashion and perfumes. Pushing prices up to maintain margins is not sustainable.

Retailer’s own brands, generics and “discount retailers” appeared, promising to keep prices lower every day and not participate in the “high one week - low the next” strategies. Consumer surveys suggest that 78% of shoppers would rather have continuously lower prices than the constantly changing promotions and discounts around special offers. Perhaps this explains why the average WalMart shopper visited WalMart more than twice as often as a Kmart shopper visited Kmart, and importantly spent nearly 20% more each visit. Eliminating the illusion of choice and building trust in the prices goes a long way.

The costs of ever more complex businesses was comprehensively underestimated by the branded goods companies. They are starting to return to their core products (hence Unilever, P&G and Gillette's massive product range streamlining) and to understand that there are good returns to be made from a well run focussed business. They are also starting to understand that despite the rising cost, genuine innovation can be a key to long term success. Even so, we continue to see many other companies struggle to justify, with often quite obscure logic, the benefits of combining diverse product portfolios of pet food, toothpastes alongside underwear, and hot dogs.

Where there are changes of this magnitude there may be opportunities, likewise there are also companies that have been much more disciplined in their approach and are currently performing well. We remain cautiously vigilant for such opportunities.

Outlook

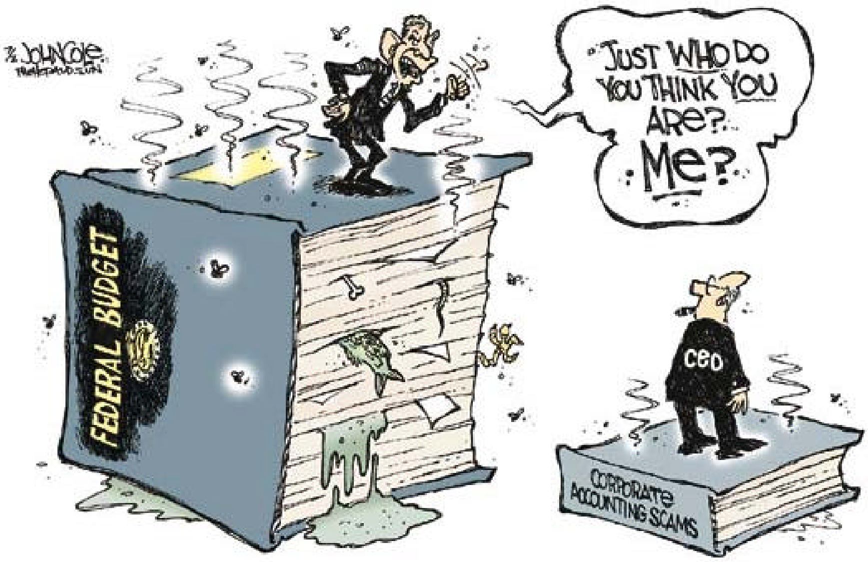
We are wary of the current valuations and of the near term prospects for many of the major branded goods companies. The data from surveys of consumers and their spending intentions suggest that there is limited potential growth. The year on year, quarterly sales comparatives for the next quarter may suggest otherwise as we compare against the September 11th 2001 quarter and it will be especially important to look beyond the headlines to understand the underlying business trends. We will continue to invest only when the fundamentals of the business are not fully reflected in the share price.

Simon Trevett/Kerr Neilson
Portfolio Managers


ZZZZZZ
SNORT MMPH
CORPORATE GREED
INVESTORS
WHAT HAPPENED LAST NIGHT?!
6:00 AM
THE 90's
DEERING


THIS IS YOUR CAPTAIN... WE'RE AT 30,000 FEET... TRUST US.
WORLDCOM
BERNIE WAS HERE


Mike Luckovich
YOUR INCOMPETENCE AND LAWLESSNESS BANKRUPTED THE COMPANY, COST THE WORKERS THEIR JOBS, DEPLETED THEIR RETIREMENT FUNDS.....
HURRY, GET TO THE PART ABOUT MY $ 125 MILLION SEVERANCE PACKAGE....
CEO


JUST WHO DO YOU THINK YOU ARE?.. ME?
FEDERAL BUDGET
CEO
CORPORATE ACCOUNTING SCAMS


DESERET NEWS
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It all starts with stealing your brother's chewing gum Jeffrey... and before you know it you're an ACCOUNTANT!
ENRON, ADELPH
WORLDCOM
ACCOUNTING SCANDAL


HIBERNATION'S OVER AND I AM HUNGRY!!
WALL STREET BEAR
SMALL INVESTOR