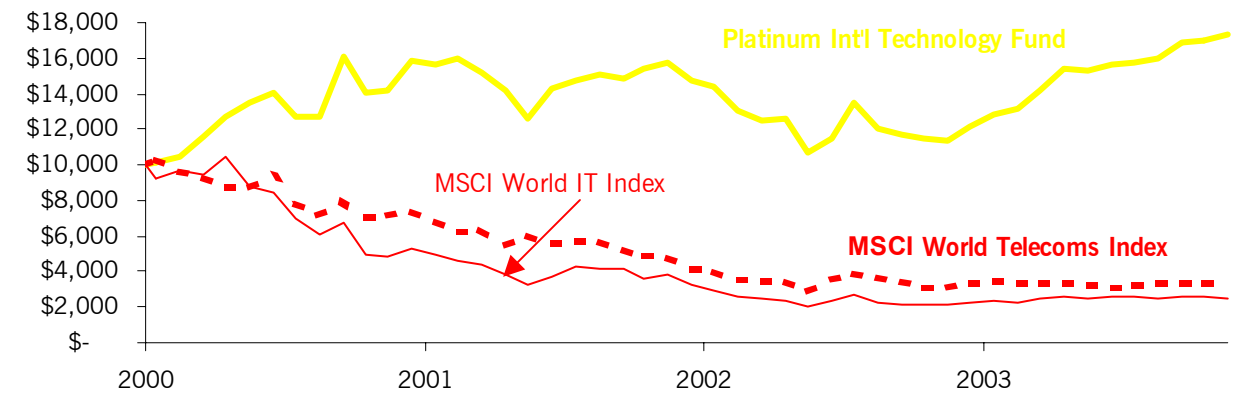
Platinum International Technology Fund

Performance

REDEMPTION PRICE: $1.0176

VALUE OF $10,000 INVESTED SINCE INCEPTION (18 MAY 2000 – 31 MARCH 2004)



Source: Platinum and FactSet Refer to Note 2

The Fund performance during the quarter was satisfactory returning 8.5%, while both the MSCI World Information Technology Index (A$) and the MSCI Telecommunications (A$) Index fell 1%. The US Technology Index, Nasdaq, was down 0.5% for the March quarter, breaking a series of five consecutive quarterly gains.

Major contributors to the Fund's performance were our European, Japanese and Asian holdings. Stand out performance from Ericsson (Communication Equipment +62%), ZTE (Communication Equipment +53%) and Checkpoint Software (Security Software +35%) added nicely to returns. Our short positions in selected stocks and Nasdaq had a neutral impact.

Changes to the Portfolio

DISPOSITION OF ASSETS

Region	Mar 2004	Dec 2003
Japan	19%	16%
Other Asia (incl. Korea)	19%	17%
North America	18%	26%
Europe	11%	17%
Cash and Other	33%	24%
Shorts	15%	15%
Net Invested	52%	61%

Source: Platinum

BREAKDOWN BY INDUSTRY

Region	Mar 2004	Dec 2003
Telecom Equipment and Suppliers	18%	21%
Semiconductors	15%	18%
Electronic Components	14%	11%
Software	7%	17%
Other	13%	9%

Source: Platinum

During the quarter we have reduced the Fund's equity exposure to US and European technology stocks after many of our holdings reached their valuation targets. We increased exposure to Japan and other Asian countries (they now represent 38% of the Fund's total assets): we believe the combined effects of continuing strong demand from China and a general improvement in the Japanese domestic economy will have a positive impact on equities in these regions.

In Europe we partly reduced the Fund's holdings in Marconi and Ericsson and we exited our investments in Epcos and Spirent, while in the US we reduced our positions in Checkpoint Software and Nvidia following strong price appreciation.

We introduced our first investment in China with ZTE Corp (the second largest telecom equipment vendor in the country) and in Japan we added NEC Corp. Three of our top five holdings in the Fund are now Asian stocks.

Commentary

On 26 January Nasdaq reached its highest level since June 2001. The rebound from its recent lows of March 2003 has been a strong 70% (the index is still 60% below its all time high in March 2000). Valuations in US technology stocks have in many instances reapproached bubble-type levels which we find difficult to justify, but the progressive improvement in final demand could push the market higher yet.

Last year's positive trends in technology spending continued this quarter, with signs of improvement in demand and capacity utilisation in many of the industries we monitor.

In 2003 global mobile phone shipments reached nearly 490 million units, up a strong 20% from the previous year, mostly driven by demand for phones with new features such as screens and digital cameras. Selected mobile operators in Europe and Japan have started investing more aggressively in new services (video-calls, multimedia messaging services etc) and expectations for demand are increasingly positive.

Semiconductor Industry Association's data also showed that in February global semiconductor shipments were still growing strongly (+31% year on year) with demand for PCs and mobile phones lifting sales, from the industry's worst ever recession in 2001 and 2002. Production capacity is getting tighter allowing producers to raise their prices. The average selling price rose almost 7% versus a year ago (in contrast with the normal experience of falling prices due to miniaturisation and process improvements).

Volume growth in worldwide PC shipments during the first quarter is estimated at +14% year on year, with a strong contribution in the Notebook category (+27%).

A key factor to monitor over the next few months will be the behaviour of the US consumer after such a strong performance. We believe that easy monetary policy and tax incentives in the US have greatly bolstered consumer discretionary spending. Any decline in appetite for consumer electronics will have to be offset by increased corporate IT spending, if the various components markets are to keep growing at current rates.

We are less worried about Asia, where the incipient recovery of domestic consumption in Japan and the secular growth of China's middle-class will stimulate demand for many technology industries.

Chinese Technology Standards

China has recently required local and foreign technology companies to comply with a new encryption standard for wireless communications, with the aim to increase security of these technologies. In an unprecedented letter addressed to the Chinese Government, US Secretary of State, Colin Powell and other senior officials of the US Administration urged Beijing to repeal the standard.

The US argued that the new encryption standard violates World Trade Organisation rules because it would favour local companies versus foreign firms and it would force US technology giants to share designs with their Chinese competitors.

Similarly, China has moved to define domestic standards for other important technologies such as office software, mobile phones, DVD players, video compression etc.

Another equally contentious issue has been a law giving Chinese chip makers unfair tax advantages: China currently levies a 17% value-added tax on imported semiconductors, while domestic producers

qualify for tax rebates of as much as 14%. China still imports about 80% of the chips it needs for its factories and it's understandable that Chinese officials want to develop a local industry to alleviate their dependency on expensive foreign technology.

These events suggest an American corporate sector increasingly worried about China's enormous bargaining power. US technology leaders fear their engineering and design know-how could be copied or replicated in China, but ultimately no large American company wants to be left out of this potentially huge market (China is second only to the US in number of Internet subscribers - 80 million - and it already has the largest number of mobile phone subscribers in the world – 280 million).

China's policy is not really different from Japan's strategy in the 60s and 70s when they demanded technology transfers to rebuild industries after World War II. Similarly Taiwan has recently become a leading centre of chip manufacturing and its major foundries (semiconductor factories) are now acknowledged to be the most cost-efficient.

Since 2000 the Chinese leadership has pushed aggressively towards the development of the local IT industry, by attracting foreign capital with all sorts of incentives (tax breaks, cheap land, fast-track Government approvals etc). Motorola has 19 research centres in China, Microsoft employs 200 researchers, Siemens has even joined a local company to design and develop a new mobile phone standard which will be adopted by one or more of the local operators. It's not only Western companies investing in China: three of the six largest projects in the semiconductor industry have been funded by Taiwanese companies. Korea's second largest technology group LG Electronics has already invested $2.5 billion in China in mobile phone and plasma screen manufacturing (incidentally Korea now exports more goods to China than to the US).

In the context of indigenous technology development we are able to participate via the likes of ZTE Corp. This is the second largest telecom infrastructure vendor in China (after privately owned Huawei). ZTE was formed by the Government in the early nineties as a merger between various local semiconductors and telecom equipment manufacturers. It was set up at a time when China's telecom operators were heavily dependent on foreign telecom equipment suppliers and it is now a leading player in CDMA wireless infrastructure, handsets and fixed-line switching, with 10% of its revenues currently spent in R&D. ZTE will be a major beneficiary of telecom infrastructure spending in China and emerging markets, where it is gaining market share against more established competitors.

Software Wars

In March the European Union Commission imposed a fine of euro 500 million on Microsoft after finding that "it has abused its virtual monopoly power over the PC desktop market in Europe …". The Commission argued that Microsoft deliberately restricted inter-operability between Windows PCs and non-Microsoft work group servers by failing to provide the information needed by rivals (like Sun Microsystems and Novell) to sell their products in a Microsoft dominated environment. Similarly it claimed that Microsoft has tied its Media Player to the main Windows operating system and hence it significantly weakened competition in the media player market (to the detriment of rival programs such as Real Networks' Real Player and Apple's QuickTime).

The Commission rejected a last-minute settlement proposed by Microsoft, breaking with a 20 year tradition in which the EU regulator would review complaints and invariably reach a mutual settlement. (In 1984 IBM had reached a similar settlement in relation to its dominance of the mainframe market and inter-operability with other hardware). This time the EU decided against settling and preferred to establish a precedent by issuing a ruling. Why?

While this case started a few years ago instigated by Microsoft rivals and disgruntled users, other complaints remain outstanding in the EU. The most important one is promoted by the Computer & Communications Industry Association against Microsoft bundling of Windows XP with Instant Messenger, Outlook Express and Movie Player. The next generation of Windows (named Longhorn, due in 2006) is promising even more bundling and functions, and it is likely to stir additional complaints. By rejecting a settlement and opening the way for Microsoft to appeal to the European Court, the EU clearly signalled a longer term battle regarding monopolistic behaviour.

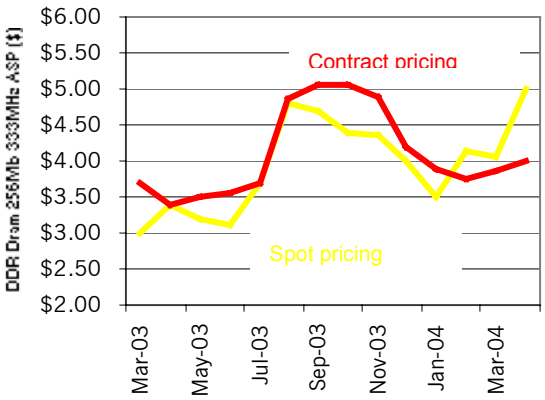
Microsoft's reluctance to unbundle the elements of its software suites is dictated by its desire to leverage its huge existing customer base to sell new applications and to prevent competitors from gaining market share. Moreover, the emergence of new open-source software (software written without restraining external software developers from accessing the original code such as the Linux operating system) is anathema to a company which has made its fortune out of a dominant proprietary code.

In this context (at the time of writing this report), the joint announcement made by Microsoft and Sun Microsystems that they would settle their long-standing disputes came as a surprise. Microsoft has agreed to pay US$2 billion to Sun to settle antitrust and patent issues, partly addressing the complaints lodged with the European Commission, and more importantly opening the way for a broader collaboration between them. Sun officials note that this settlement will provide even more information than they had sought in the European case: soon Microsoft will share information about PC and server versions of Windows, but also about database software and email.

We are pleased with the $2 billion cash infusion for Sun Microsystems (a Fund's holding) but we don't believe the war is over. We rather think that an armistice has been signed. Expediency is not foreign to Microsoft's behaviour. In 1997 it paid a relatively small $150 million to Apple Computers to settle various patents infringement and inter-operability issues: helping to keep alive one of the few remaining competitors in the PC operating systems and giving Microsoft a counter-argument to monopoly charges in its antitrust cases. In 2003 Microsoft paid $750 million to AOL Time Warner to settle a dispute over the alleged attempt to weaken Netscape's position against the dominant Internet Explorer. The money spent for these settlements is still a fraction of the huge US$53 billion of cash sitting on Microsoft's balance sheet. The settlement with Sun may even help Microsoft to resolve its case with the EU if it can demonstrate a willingness to share information with its rivals.

In the long term though we believe the emergence of open source software and clients' requirements about inter-operability will sustain competition to the benefit of underdogs such as Sun Microsystems.

DRAM SPOT AND CONTRACT PRICE CURVES



Source: Smith Barney

Alex Barbi
Portfolio Manager

Notes

1. The returns represent the combined income and capital return for the specified period. They have been calculated using withdrawal prices, after taking into account management fees (excluding any performance fees), pre-tax, and assuming reinvestment of distributions. The returns shown represent past returns of the Fund only. Past performance is not a reliable indicator of future performance. Due to the volatility of underlying assets of the Funds and other risk factors associated with investing, returns can be negative (particularly in the short-term).

2. The investment returns depicted in the graphs are cumulative on A$10,000 invested in the Funds since inception and relative to their Index (in A$) as per below:

   Platinum International Technology Fund:
   Inception 18 May 2000, MSCI Global Technology index in A$

   The investment return in the Funds is calculated using withdrawal prices, after taking into account management fees (excluding performance fees), pre-tax and assuming reinvestment of distributions. It should be noted that Platinum does not invest by reference to the weightings of the Index. Underlying assets are chosen through Platinum's individual stock selection process and as a result holdings will vary considerably to the make-up of the Index. The Index is provided as a reference only.