Platinum European Fund

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Disposition of Assets

REGION	MAR 2016	DEC 2015
Germany	21%	16%
UK	18%	21%
Italy	6%	4%
Austria	6%	5%
Spain	5%	5%
France	5%	4%
US *	4%	4%
Russia	4%	4%
Hungary	3%	2%
Switzerland	2%	3%
Norway	2%	1%
Netherlands	2%	1%
Sweden	1%	1%
Turkey	0%	<1%
Cash	21%	29%

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

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

Performance and Commentary

(compound pa, to 31 March 2016)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum European Fund	-6%	-2%	14%	11%	11%
MSCI AC Europe Index	-7%	-9%	13%	8%	2%

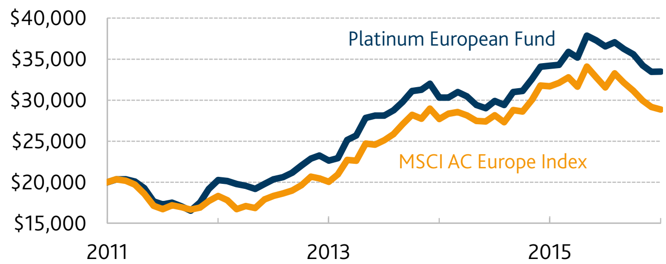
Source: Platinum and MSCI. Refer to note 1, page 4.

European shares peaked last April. Since then, the market has fallen by 17%, having been down 27% at February's trough. The MSCI AC Europe Index is now back where it was at the start of 2015, before the European Central Bank (ECB) announced its Quantitative Easing program.

The European economy grew throughout 2015, but not fast enough to meet the expectations baked into stock prices. With growth slowing globally, doubts about the durability of the European recovery have set in. Initially the sell-off was concentrated in cyclical companies, especially those exposed to Emerging Market economies. Hardest hit were Materials, Energy and Industrials.

Value of $20,000 Invested Over Five Years

31 March 2011 to 31 March 2016



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

This dynamic changed in 2016. The hitherto hardest hit sectors enjoyed strong rebounds, while Financials now bore the brunt of the selling. Financials had been spared initially because of their domestic focus and because valuations were not stretched. This changed as investors cooled on Europe's economic prospects and interest rates looked likely to fall further into negative territory, especially after the Bank of Japan adopted negative interest rates in late January. Investors' fears were further amplified when the market for contingent convertible securities seized up on speculation that Deutsche Bank would be unable to pay its coupons on these instruments.

In March, the ECB delivered another round of monetary stimulus. It is now buying high-grade corporate bonds as well as government bonds, and the quantum of purchases will increase to EUR80 billion per month. The deposit rate was cut to -0.40% and banks will now be allowed to borrow from the ECB at negative interest rates to temper the effect of interest cost on their margins. The impact of all this was somewhat blunted by subsequent comments which downplayed the prospect of further rate cuts. Thus, while credit spreads narrowed, the response from equities was somewhat muted and the Euro actually ended the quarter 5% stronger against the US dollar.

European equities fell 5% in local currency over the quarter. The strongest sectors were Materials (+3%), Energy (+2%) and Industrials (+2%). The weakest sectors were Banks (-16%), Autos (-12%), Insurers (-12%) and Healthcare (-9%).

The Fund returned -5.9% for the quarter and -2.1% for the 12 months to 31 March in Australian dollar terms. This compares to -7.3% and -8.9%, respectively, for our benchmark. Our cash balance fell from 29% to 21% as lower stock prices opened opportunities to invest our capital.

In our December 2015 Quarterly Report we warned that the Fund would likely underperform its benchmark should Materials, Energy and Industrials rebound. While this rebound did occur, the Fund in fact outperformed the Index. This is doubly surprising when one considers that the Fund is now overweight Banks, which were the worst performing sector.

It helped that the banks owned by the Fund performed significantly better than their peers. While two of our banks performed marginally worse than their sector, the other six handily outperformed, some by a wide margin. The Fund also benefited from strong performances by two of our larger holdings, **Markit** and **GfK**, underscoring the central role individual stock selection plays in our investment process.

Changes to the Portfolio

Given the intensity of the sell-off, it should come as no surprise that we did a lot more buying than selling this quarter.

We re-established an investment in Franco-Italian luxury goods conglomerate **Kering**, owner of well-known brands including Gucci, Bottega Veneta and Saint Laurent. Following a decade of impressive demand growth and price escalation, the luxury sector is now experiencing a period of indigestion as rapid footprint expansion leaves it vulnerable to weaker economic growth in Emerging Markets and a corruption crackdown in China.

The attraction of Kering as an investment idea is that it is multifaceted. Most obviously it will benefit from a rebound in global economic growth. But there are company-specific angles too, with hints that the company may sell its long-struggling sports brand, Puma. This would significantly reduce its debt at no cost to earnings and turn the company into the luxury goods pure-play that investors want.

Of even greater interest is the potential turnaround at Gucci, where the offering had become somewhat stale and increasingly undeserving of its high price point. Appointing an unknown entity in the form of Alessandro Michele as Creative Director and granting him a high degree of artistic freedom was risky, but it has proven to be an inspired choice. His new aesthetics can be experienced at Gucci's store in Sydney's Pitt Street Mall. While it may not be to everyone's taste, leading opinion makers and fashionistas are sold on it and the brand's credibility has not only been salvaged, but enhanced.

Whether this 'buzz' can be translated into increased sales in the all-important leather goods category remains to be seen, but with Gucci accounting for 60% of Kering's earnings, a turnaround would be especially meaningful. Naturally, there are risks. Bottega Veneta looks likely to struggle going forward and recent terrorist attacks in Europe may disrupt tourist demand. Nevertheless, on 15x earnings we think this is a good money making opportunity.

In January, as the oil price retreated below US$30 per barrel, we took a position in Norwegian seismic data company, **TGS-NOPEC**. The thesis here is straightforward. For modern societies to function, we need to move people and things around. To do this, we need to burn oil. But to burn it, we first need to find it. And to find it, we need seismic. Seismic surveys are an important tool used in oil and gas exploration. Like medical ultrasound tests, seismic surveys produce images of rock formations beneath the Earth's surface by 'shooting' shock waves into the Earth using an energy source and recording the waves refracted back to the surface.

Oil companies outsource seismic shoots to specialist service providers. This gives them the flexibility to cut spending easily in a downturn. By contrast, the service providers have to carry the fixed cost of owning ships and employing crews. They also carry a fair bit of debt to finance that kit. With seismic spending having been cut in half from its recent peak, seismic operators are on their knees. The cost of shooting seismic has collapsed as fleet owners slash pricing in a desperate attempt to cover some of their fixed costs. In many cases this simply delays the inevitable; some have already gone bust and others are likely to follow.

This brings us to TGS, which is different in that it doesn't own any ships or employ any crews. Instead, it hires those of its competitors as and when it needs them. And these are now a lot cheaper. In essence, TGS is more an information broker than a seismic operator. The main asset on its balance sheet is its data library, not ships and seismic equipment. By not owning ships and not employing crews, they have to pay up for these when demand is strong, sacrificing some upside. But they benefit during tough times, because their costs are extremely flexible and those of competitors aren't.

TGS has no debt and has 10-15% of its capitalisation in cash. It remains comfortably profitable. Seismic spending would have to fall more than 80% from the peak to push them below break-even. This is still a long way off and assumes they don't cut costs.

Eventually, oil companies will have to find new sources of oil to replace today's production. Spending on seismic can be deferred but not avoided. If less is done today, more will be done tomorrow. With competitors failing, TGS will capture a larger share of this future spending. While we sit and wait for this to happen, we are collecting a 5% dividend, having bought TGS at just over book value, a significant discount to historical valuations.

Outlook

The economic recovery in Europe continues. Employment is growing with recruitment firm, Hays, reporting 13% revenue growth in its European segment. New car registrations are growing 14%, indicating the strength of consumer sentiment. And, while business investment is often cited as an area of weakness, commercial vehicle sales are up 18% from a year ago. We therefore find it difficult to be too pessimistic.

That being said, risks remain plentiful. On the political front we have the 'Brexit' referendum, separatist rumblings in Catalonia, an inability to form a government in Spain, Russian revanchism, internal divisions on asylum seeker policy, terrorism and disillusionment with elected representatives fuelling support for parties on the political fringe.

On the economic front, there is little appetite for badly needed reform. The current faltering attempt at reforming the French labour market demonstrates the ability of entrenched interests – in this case, labour unions which, incidentally, represent just 8% of French workers – to derail any attempt to curb their influence. European economies remain vulnerable to external shocks while ultra-loose monetary policy risks amplifying the pervasive distortions.

The main change is that share prices have fallen significantly in the last few months. This has reduced the greatest risk we face as investors, namely, the risk of overpaying for assets. Attractive investments are becoming easier, though not easy, to find. Our cash balance remains high, leaving us well placed to capitalise on any new opportunities while protecting our capital should the sell-off persist.

Notes

1. The investment returns are calculated using the relevant Fund's unit price and represent the combined income and capital return for the specific period. They are net of fees and costs (excluding the buy-sell spread and any investment performance fee payable), are pre-tax, and assume the reinvestment of distributions. The investment returns shown are historical and no warranty can be given for future performance. You should be aware that historical performance is not a reliable indicator of future performance. Due to the volatility of underlying assets of the Funds and other risk factors associated with investing, investment returns can be negative (particularly in the short-term).

   The inception dates for each Fund are as follows:
   Platinum International Fund: 30 April 1995
   Platinum Unhedged Fund: 28 January 2005
   Platinum Asia Fund: 4 March 2003
   Platinum European Fund: 30 June 1998
   Platinum Japan Fund: 30 June 1998
   Platinum International Brands Fund: 18 May 2000
   Platinum International Health Care Fund: 10 November 2003
   Platinum International Technology Fund: 18 May 2000

   (NB: The gross MSCI Index was used prior to 31 December 1998 as the net MSCI Index did not exist.)

2. The investment returns depicted in this graph are cumulative on A$20,000 invested in the relevant Fund over five years from 31 March 2011 to 31 March 2016 relative to its benchmark index (in A$) as per below:

   Platinum International Fund - MSCI All Country World Net Index
   Platinum Unhedged Fund - MSCI All Country World Net Index
   Platinum Asia Fund - MSCI All Country Asia ex Japan Net Index
   Platinum European Fund - MSCI All Country Europe Net Index
   Platinum Japan Fund - MSCI Japan Net Index
   Platinum International Brands Fund - MSCI All Country World Net Index
   Platinum International Health Care Fund - MSCI All Country World Health Care Net Index
   Platinum International Technology Fund - MSCI All Country World Information Technology Net Index

   The investment returns are calculated using the relevant Fund's unit price. They are net of fees and costs (excluding the buy-sell spread and any investment performance fee payable), pre-tax and assume the reinvestment of distributions. It should be noted that Platinum does not invest by reference to the weightings of the benchmark index. Underlying assets are chosen through Platinum's individual stock selection process and as a result holdings will vary considerably to the make-up of the Index. The Index is provided as a reference only.

3. Invested position represents the exposure of physical holdings and long stock derivatives.

Disclaimer

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