Platinum European Fund

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Disposition of Assets

REGION	DEC 2010	SEP 2010
Australia	1%	0%
Belgium	3%	3%
Finland	3%	4%
France	25%	25%
Germany	42%	41%
Italy	2%	2%
Netherlands	1%	2%
Sweden	2%	3%
Switzerland	1%	4%
UK	11%	11%
US	2%	1%
Cash	7%	4%
Shorts	4%	6%

Source: Platinum

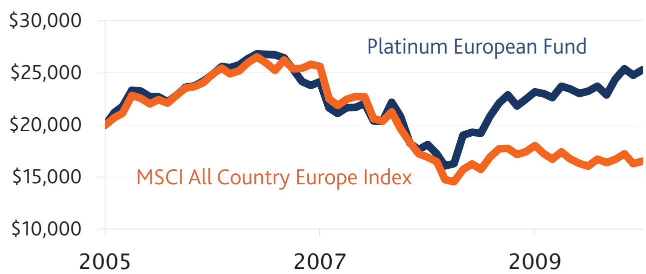
Performance

Outside of the periphery (Spanish IBEX -5%, Italian MIB -2%) European markets in general continued their upward march since September; the UK and French markets appreciating 6% and 3% respectively, with Germany being the clear standout, up 11% for the quarter.

The outperformance of the German market continues when measured over the year, the DAX returning +15% well-ahead of the FTSE (UK +9%), CAC (France -3%), MIB (Italy -13%) and IBEX (Spain -17%). The fruits of a decade of work to restore German corporate competitiveness (which are getting a steroid shot in the form of a weak Euro and low interest rates) are now flowing down to the broader consumer. The unemployment rate (even when accounting for short time workers which allows companies to put workers on reduced schedules rather than lay them off) is fast approaching pre-crisis levels and we are seeing real growth in German wages for the first time in 10 years. This dynamic is breathing life into the long stagnant German retail and construction sectors, and investors have been keen to play the theme with the domestic consumption plays (DIY retailer Hornbach (+25%), food and electronics retailer Metro (+17%) and TV broadcaster Prosieben (+25%)) doing well over the quarter.

Value of $20,000 Invested Over Five Years

31 December 2005 to 31 December 2010



Source: Platinum and MSCI. Refer to Note 2, page 5.

Elsewhere strong performance for the quarter was all about the cyclicals. Auto stocks were up across the board as their profitability continued to surprise analysts (Volkswagon +31%, Fiat +36%), the share prices of European specialty and commodity chemical producers continued to reach record highs (Lanxess +47%, BASF +30%) and the capital good stocks were again strong, especially those directly linked with spending in the mining sector (Atlas Copco +30%, Metso +25%).

Conversely the weak areas of the market were a replay of the trends seen throughout the year, utilities (electricity prices remain low, a product of low gas prices and generation overcapacity), banks (fears over regulation/sovereign risk on top of broadly dull credit demand), pharma (patent cliffs mixed with investor boredom) and telcos (shrinking fixed line revenues) all doing very little.

In local currency, the MSCI Europe Index was up 5% for the quarter, however, with the $A appreciating 4-8% against the European currencies over the period, the Index return when measured in $A was a more modest -1.1%. The Platinum European Fund returned 3.6% over the quarter.

Over the calendar year the European Fund was up 9.1% outperforming the MSCI Europe Net Index which returned -8.3% over the same period.

Changes to the Portfolio

Outside of two promising real estate/infrastructure investments which we detail later in the report, new additions over the quarter included German diagnostics leader **Qiagen** which we entered at an excellent price after the stock sold off on concerns over slower growth in the US; oil giant **Royal Dutch Shell** who is set to harvest the cash flow from the past five years of heavy investment and French distiller **Pernod Ricard**. The funding for these new purchases came from the full exit of Dutch vaccine producer **Crucell** and Swiss pharmaceutical player **Novartis**. We also trimmed a number of our more cyclical holdings after strong performance.

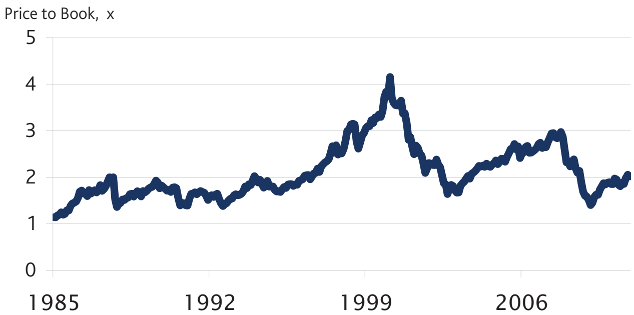
On the currency front, with an eye on the prospect of further tightening in China and the speculative froth around commodities prices, we further reduced our modest hedge into the Australian dollar by 10%. The majority currency position of the Fund now stands at 50% Euro, 14% Australian dollar, 12% British pound, 11% US dollar and 8% Norwegian kroner.

Commentary

December marks the period where the crystal ball gazing of the brokerage community goes into overdrive as each house produces their forecast on the outlook for 2011. As investors, we are primarily interested in what is the likely return we can make from markets in 2011 and what companies/industries hold the most promise. We can make a good start to these predictions by answering two simple questions: Firstly, are European markets still attractively priced and secondly, how are investors positioned?

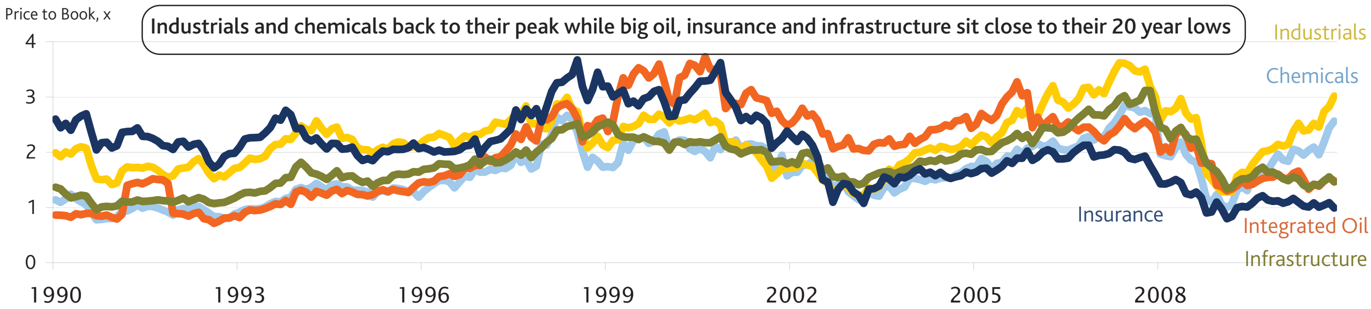
On valuation, the MSCI Europe Index is trading on a current PE of 12 times which is expected to fall to below 11 times in 2011, a reasonably modest starting point given the long-term average PE of markets is 14-15 times. On a price to book valuation, Europe is now trading at roughly two times book, a similar valuation to when Europe was last exiting a recession in 2003 and below its 20 year average of 2.3 times and the 2007 peak of three times. Overall valuations in aggregate are not pointing to markets being over-extended.

Europe - Price to Book



Source: Factset

European Sector - Price to Book



Source: Factset

Looking beneath the index, the picture is less sanguine. Valuations in Europe are increasingly clustering at opposite poles and investors are still heavily positioned in the stocks perceived to offer growth or cyclical recovery. The poster child of this enthusiasm for growth are the European industrials and chemicals who have rebounded to their 2007 valuation peaks while sectors like insurance and infrastructure sit at 20 year lows. Overall our market PE of 12 times is a combination of the higher quality or growth businesses priced at 17-20 times whilst the comparatively dull media/retail/insurance/utilities/bank/pharma stocks all sit at valuations of 10 times or lower… a far less comfortable starting point!

As alluded to in the opening salvo, many of these unloved industries are cheap for good reason; a structurally declining fixed line telco or postal service is an unattractive investment unless extremely cheap and even then, only as a short-term trade. However, for others the headwinds are far more transient and one area we have been finding opportunities are the traditional 'hard asset' stocks (utilities, infrastructure and real estate etc).

A change in expectations around inflation would be a trigger for investors to revisit these companies as whether it be via high leverage with fixed cost debt or revenues with some linkage to inflation, the common thread to these businesses is that they are given a helping hand in inflationary environments. Whilst the level of commentary is building, the spectre of rising inflation is not really being priced into these stocks. This is interesting given we have ongoing money printing in the US, roaring commodity prices, building wage inflation in China and a one size fits all monetary policy in Europe which for the benefit of the periphery will remain too lax for Germany. Of course the nature and the immanency of the inflationary pulses in each economy will differ (i.e. China is currently experiencing strong wage and food inflation, where Germany is at risk of higher inflation especially if there is a pick-up in domestic credit growth) and we would highlight our recent investments are ones where rising inflation would provide a welcome free kick rather than being the crux of the investment case.

One such addition is UK pub owner **Enterprise Inns**, a company readers of the Brands Fund quarterly reports will already be familiar with. The owner of 7,100 tenanted pubs, the business is one of a real estate owner who collects a rent but also participates in the trading profit of the tenant (through tied alcohol sales) and hence there is a large day to day operational element in selecting and supporting your publicans. The business has struggled under a huge debt load, product of a land grab which left it with too many weak pubs (and publicans) just as the headwinds of smoking bans and recession hit. The last 18 months have seen underperforming pubs sold, weaker tenants replaced and debt terms and costs restructured. Profits have stabilised and with the bulk of the fires now extinguished, management can now get back to the real business of improving the trading at their pubs. Annual rent increases are indexed to UK retail price inflation which is currently running at 5% and this together with some modest growth in beer revenue will put us on track for solid profit growth. The level of gearing ensures this is an investment not without risk, however, given we are paying a low single digit multiple of earnings and a mere 0.3 times book value the risks are largely priced and the upside, should events progress to plan, will be quite dramatic.

Elsewhere we have been building a position in a fine transport infrastructure asset that is operating well below its intended capacity. Revenue and traffic levels have historically disappointed, regulated charges were set at uncompetitive levels and the company was forced to rely on a single poor performing third party operator to complete its freight service. The catalyst for an improvement is the recent deregulation of both the companies operating parameters and its industry participants. Fixed tariffs have been lowered and new operators can now enter the industry to challenge the old guard. This will not only open up new freight and traffic catchment areas, but more importantly will allow management to setup their own freight logistics service, side stepping some third party operators and giving them control over delivery times and reliability.

Establishing new routes and attracting new customers will take time so the improvements in operations will be felt over years rather than months. However, the fixed cost nature of the business will ensure incremental revenues largely fall to the bottom line as profit, whilst the long concession life allows profits to be reliably forecasted (and valued) many years into the future. The combination of the above means that even modest improvements in traffic and revenue will have a disproportionately large effect on the share price.

Outlook

The need for Ireland to call on the European Central Bank (ECB) for help has intensified the scrutiny on the plight of the Spanish. The past success and current problems of the two countries stem from similar issues. With the benefit of low interest rates after entry into the Euro, both experienced a credit boom that made them the tigers of Europe, with fast economic growth and rising employment attracting flocks of migrant workers to their shores. The credit boom eventually led to a construction and real estate bubble, and it is the subsequent housing bust and the desire to support their banks that is putting government finances in jeopardy, rather than wild overspending in the past[1].

[1] Both the Spanish and Irish governments had been de-gearing since the mid-nineties. From 1996 to 2007, both governments kept their total debt load fairly stable, while their economies grew massively. Spanish government debt as a percentage of GDP dropped from 67% in 1996 to 36% in 2007. Ireland's debt dropping from 73% of GDP in 1996 to 25% in 2007.

Given the similarities, is it inevitable that the Spanish follow the Irish in calling on the ECB for support? Not quite, the banking sectors have their differences. Firstly, 50% of the Spanish banking sector is controlled by Santander and BBVA, whom unlike the Irish banks have diversified businesses with highly prized and profitable operations outside of Spain (Santander – Brazil/UK, BBVA – Mexico/Turkey). These overseas assets not only provide profit to recapitalise losses in Spain, but the appeal of these divisions to investors have allowed Santander and BBVA to continue to raise equity from the market. In the event of further big write downs of Spanish loans, it is not obvious the government would need to bail these two out. Secondly, even if we simulate Irish style loan losses on the total Spanish loan book, the cost of full recapitalisation would be approximately €300 billion. Netting off the value of the equity portfolios held by the regional savings banks (conservatively valued at €150 billion) would see government debt rise to roughly €800 billion (80% of GDP) post recapitalisation. Not a comfortable number but below Italy and on par with France who have debt to GDP ratios of 115% and 80% respectively.

While a banking-led sovereign crisis is not inevitable in Spain, realistically in the short-term this may not matter. The bond market is looking for a stable recovery to GDP growth but the country still has high unemployment and a government trying to cut spending, none of which will promote economic stability in the short-term. In this context, near term setbacks are more likely than not and with the markets skittish, we are mindful borrowing costs could blow out at the first sign of weaker than expected GDP numbers. All up, common sense dictates that any Spanish investments need a decent margin of safety and with the Spanish market now 40% below its 2007 peak we are further researching some opportunities were the risks look to be more than adequately reflected in the price.

On a broader scope, for the moment the prospect of a continued recovery in the US is outweighing concerns over inflation pressures in Asia. The growth divergence between Europe's north and south is set to continue and while this idea is not lost on the market, large macro shifts in profit leadership tend to run for some time. The key, as ever, is paying the right price and we are comforted in the outlook for the portfolio by the fact that we are still finding a steady flow of new ideas for the Fund.

Notes

1. The investment returns are calculated using the 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: 31 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

2. The investment returns depicted in this graph are cumulative on A$20,000 invested in the relevant Fund over five years from 31 December 2005 to 31 December 2010 relative to their Index (in A$) 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
   (nb. the gross MSCI Index was used prior to 31 December 1998 as the net MSCI Index did not exist).

   The investment returns are calculated using the 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 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.

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