Platinum European Fund

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Disposition of Assets

REGION	DEC 2011	SEP 2011
Germany	48%	46%
France	16%	17%
UK	12%	12%
Netherlands	5%	2%
Italy	4%	4%
Spain	2%	2%
US	2%	2%
Sweden	1%	2%
Finland	1%	1%
Belgium	1%	1%
Switzerland	1%	1%
Cash	7%	10%
Shorts	9%	6%

Source: Platinum

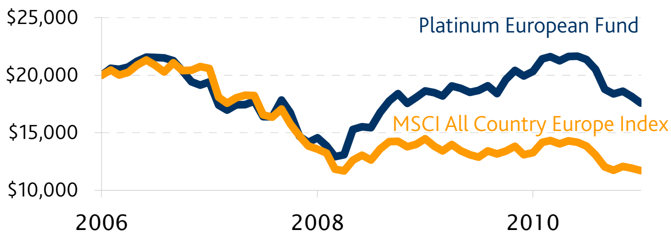
Performance

European stock markets made a tempered recovery from their October lows, with the various indices, German DAX (+10%), UK FTSE (+8%) and French CAC (+7%) all rising over the quarter (in local currency). Investors continued to shun the periphery with the Italian MIB and Spanish IBEX indices failing to participate in the rebound. The Australian dollar appreciated 10% and 6% against the Euro and British pound over the period, so when expressed in A$, the MSCI All Country Europe Index returned -0.3% versus -4.3% for the European Fund.

For the 2011 year as a whole, European markets were down across the board. Unsurprisingly given the sovereign crisis, the Italian market suffered the largest fall -27%, followed by the French -20%, German -15%, Spanish -14% and UK -8%. The broad nature of the sell-off meant few industries were spared, however, the 'defensives' faired best with the clear standout being the ironic pairing of Healthcare (Merck KGaA +26%, Fresenius +20%, GlaxoSmithKline +17%) and Tobacco (Swedish Match +26%, British American +22%). The worst hit sectors were the financials (Commerzbank -70%, Unicredit -54%) and non-energy commodities (Xstrata -35%, Rio Tinto -30%).

Value of $20,000 Invested Over Five Years

31 December 2006 to 31 December 2011



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

In what is a disappointing outcome, despite the Fund's minimal direct exposure to the key areas of weakness (financials, commodities and the periphery), the performance for the year was little different from the Index, with the European Fund returning -13.6% versus the MSCI Europe Index down -11.8%.

Commentary

The 50% share price fall of express parcel logistics player **TNT Express** after its separation from the Dutch national post operator was the trigger for us to revisit the company, and we have subsequently taken close to a 3% position in the stock over the quarter.

Express logistics has been an interesting growth industry as globalisation and technology improvements drove changes to traditional supply chains. The geographical shift of higher value manufacturing to low cost countries and the continued adoption of 'just in time' supply chain practices (i.e. keeping less finished product in stock and instead relying on rapid delivery direct from the manufacturer), played into the hands of the express parcel players who could provide a cross-border express delivery product.

While TNT is the smallest of the four global express players (behind UPS, FedEx and DHL), its strength resides in its pan-European express network where TNT holds the leading market share (18%) and can deliver to more locations, more profitably, than any other player. The other defining aspect of TNT's business is that its delivery network is more heavily weighted to ground (truck based) delivery rather than air. Long-term, this is a benefit as the quintupling of the oil price over the last ten years has inflated the cost of air express and at the margin shipment volumes continue to move to slightly slower, but considerably cheaper ground alternatives.

So why has the market halved the price of TNT? The worry of cyclicality is certainly one reason; shipping demand is always broadly linked to economic activity and investors fear the worst for Europe. The other issue stems from TNT's strategy to further expand internationally. In the early 2000s, the larger players like FedEx and DHL were building out air express networks in Asia, largely serving the import/export market (i.e. packages going from China into the US or Europe). TNT wanting to participate in this growth, but without the financial muscle to spend billions taking on the big boys in the air, concentrated on serving the local market of these emerging economies (i.e. delivering packages within China). TNT's two countries of focus have been China and Brazil, and while the company has had reasonable success in cultivating their ground network in China, the same cannot be said of the Brazilian operations. The recent failed integration of Aracatuba (a second Brazilian network the company acquired in 2009) saw on-time delivery levels collapse, customers flee and TNT Brazil fall into heavily losses (€120 million pa).

Given these issues, why do we think TNT is an interesting investment? Starting with valuation, from whatever angle we view it, TNT is trading very cheaply. The Fund was able to acquire the bulk of its position at a price that valued the entire business at €2.6 billion, a price to book of 0.8 times (TNT has almost no financial debt). TNT's European network alone made a €600 million pre-tax profit in 2006 and 2007 and is currently making €400 million, hence we are paying four times peak or seven times current profit for the European network, attributing no value to the positions in Australia and China.

Another way to think about the value of the business is from the perspective of an industrial buyer. Express logistics is a 'network density business', namely profitability is reliant on whether your trucks/planes are full on their pickup, line-haul, and final delivery routes. This creates a high hurdle for new competitors to enter the market, you need to offer a comparable service to the established player (speed, destinations served, price) to win business, but without volume on your network you will be at a massive cost disadvantage. The case example of this was DHL's ill fated attempt to build an express network in the US competing against UPS and FedEx. From entry in 2003 till exit in 2009, DHL cumulatively lost close to $9 billion before giving up. It would be *very difficult* to replicate TNT's European network for €2.6 billion and it's not unlikely that a large competitor, with borrowing costs at record lows, may see TNT as an opportunity to buy rather than build.

On the aspect of timing, there are a couple of catalysts that could see a higher price over the next twelve months. Firstly, the newly independent management has made it clear that a resolution to the losses in Brazil will be visible by year end, either the business will be well on its way to break even or solutions like a partnership or sale will be set in motion.

Progress will be closely watched by the Dutch Post (PostNL) who holds a 30% stake in TNT which they need to monetise over the next 18 months to pay down debt. No doubt they will remain in discussions with potential suitors with an eye to maximising the value of their stake.

Finally, how to think about cyclicality? All businesses carry some cyclicality and accurately predicting the effects of an economic downturn on profits is as much art as it is science. The best defence an investor has is when the fears of a cyclical downturn are more than compensated by a low valuation. The trick is to ensure that what you think is a cyclical downturn is not a lasting fundamental change to the economics of the business (think newspapers in the internet age), where the past history of profits will actually mislead you. We feel the cyclical risk in TNT's business is more than reflected in the price, while the ultimate business risk is low. Express logistics is still a growth industry aided by the tailwind of globalisation and TNT's lack of debt will allow it to weather any short-term fall in profits.

Please refer to the article titled 'Why Valuation Matters'.

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Outlook

Readers will know that a quick perusal of any weekend financial press will leave one still confronted with a number of negative headlines surrounding Europe. This position is echoed by the investment community; investors are very pessimistic about the economic outlook – all analysis of the future is being coloured by a focus on 'how things can get worse'. At times like these it is worth remembering that the real economy is always less volatile than the stock market implies, and there are always areas of growth and activity underneath the surface.

A good example is housing, while headlines across the continent opine of lower mortgage growth and falling prices, activity is quietly building in Germany. The German operations of Hornbach (the Bunnings of Germany in the DIY sector) are reporting the strongest sales growth they have seen for 17 years, as access to record low interest rates is fuelling German interest in upgrading their homes. Similarly, the press around the weak sales of the UK traditional high street retailers (echoed by the likes of David Jones and Myer on our shores) would leave most with the feeling that the consumer is in very bad shape. However, as evidence that activity may be stronger than it seems, we would point to the fact that Yodel (the UK's second largest home parcel delivery network), on the back of a boom in online shopping, has seen parcel volumes running 20% higher than their most optimistic projections.

The breadth of the market sell-off has recalibrated relative valuations across industry sectors and we are taking this opportunity to concentrate our holdings into companies that have better growth prospects over the next couple of years. The widespread pessimism has led to attractive valuations across the board, with large swathes of the portfolio now looking very cheap. In light of this, the Fund remains fairly fully invested, with an 84% net position (93% gross, with 9% short).

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$20,000 invested in the relevant Fund over five years from 31 December 2006 to 31 December 2011 relative to their Index (in A$) 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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