PLATINUM INTERNATIONAL FUND

Kerr Neilson Managing Director

Share markets lost momentum in the June quarter as doubts crept into investors' minds. The emerging markets of Asia and Latin America mostly declined, by between 1% and 14%, while markets in Europe and America ranged between zero and +8%. The Yukos affair hurt sentiment towards Russia badly with that market selling off by 20%. The wash-up from all this was an advance by the Morgan Stanley World Index of 1.6% when measured in local currency. For the year, this index is up 21%. However, the rebound of the US$ in the quarter saw the A$ fall from $0.76 to $0.70 and this translated into a gain by the World index of 10.6% in A$ terms. The annual figure was 19.4%. Our emphasis on Asia, which has tended to be weak recently, worked against us. Hence we underperformed during the quarter, returning 3.5%, though the short term dip is not apparent in the year's return of 27.9%.

As one would expect in a year of recovery, the cyclical industries way out-performed the defensives. Health care and telecommunications, the two laggards, have additional problems of their own. The pharmaceutical giants are suffering from patent expiries, disappointing drug pipelines and the latent threat to prescription prices, while telecoms are threatened by the internet.

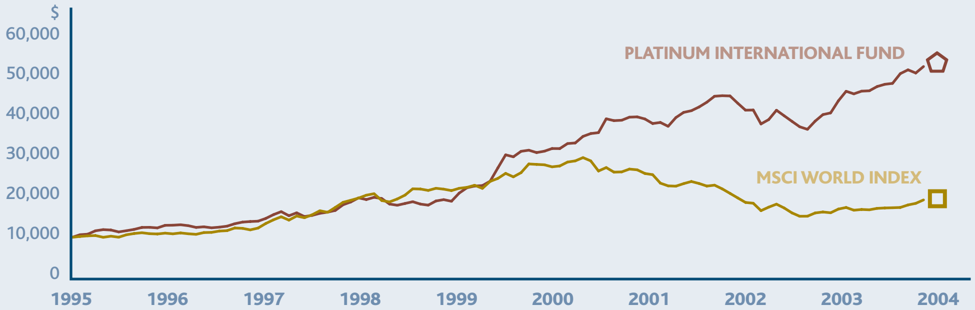
A conspicuous development has been the massive out-performance of small capitalisation companies versus large caps in the last three and a half years. Valuation differentials have reversed with larger companies now typically being on lower valuations than small companies. More recently there has also been a widening of the valuation gap between "high beta" and "low beta" stocks. Having had some benefit from this trend since 2000, we have been adjusting our position in the expectation of a reversal of this pattern.

MSCI WORLD INDEX INDUSTRY BREAKDOWN (A$)

SECTORS	QUARTER	1 YEAR
MATERIALS	9.2%	29.4%
INDUSTRIALS	13.8%	26.5%
INFORMATION TECHNOLOGY	9.4%	21.9%
ENERGY	15.9%	21.4%
CONSUMER DISCRETIONARY	10.0%	19.7%
FINANCIALS	6.6%	18.2%
CONSUMER STAPLES	10.9%	15.4%
UTILITIES	8.7%	12.4%
HEALTH CARE	12.6%	5.4%
TELECOMMUNICATIONS	5.8%	5.0%

Source: Bloomberg

VALUE OF $10,000 INVESTED SINCE INCEPTION 1 MAY 1995 TO 30 JUNE 2004



Source: Platinum and Factset. Refer to Note 2.

CURRENCY

We sense that the highly lop-sided position that many investors had against the US$ has been squared. This, together with our longer term concerns, has caused us to exit the US currency again in favour of the Yen and Euro. We added to the hedge into A$, which is now around 29%, but are ambivalent as to its prospects versus the Euro and believe it will be slightly weaker than the Yen.

CHANGES TO THE PORTFOLIO

It has been a relatively inactive period with our tending to bolster existing and recent acquisitions. In Japan this included adding to the Toyota group of companies at the expense of the likes of Nippon Yusen K.K., Mitsubishi Heavy Industries and Citizen Watch. The latter has been very strong on profit performance and the appeal of its electronic components subsidiary. We switched out of Yamanouchi Pharmaceutical to add to the position of its rival, Takeda Chemical. The valuation gap had become too great on account of the market's excitement with Yamanouchi's near term prospects, seemingly ignoring Japan's largest drug company's potential.

One new position was Sumitomo Mitsui Financial Group. Along with Mitsubishi Tokyo Financial (which we own) we see it taking advantage of the much weakened position of the banking sector and exploiting the advantages it has to expand as a more diversified provider of services to the consumer.

In the US, we have added to Agere and Agilent and have shuffled the biotechs, after losing Tularik to a bid from Amgen.

In Europe the most significant new purchase is **Alcatel**. This traditional provider of telephone switchgear and other electrical engineering services has morphed into a more streamlined company to focus on *next-generation* communication. By this is meant high speed internet access, Voice over Internet Protocol (VoIP), satellite and mobile communication, as well as converting traditional copper wired networks to function as fully digital systems. These complex solutions go by acronyms like DSLAM (digital subscriber line access multiplexing) or FTTH /FTTN (fibre to the home or to the node). Technical developments are advancing so fast that solutions which were hitherto regarded as compromises are proving more than adequate. So now we find that DSLAMs are allowing the telecoms to continue to use their installed paired copper wires to deliver full video, high speed

DISPOSITION OF ASSETS

REGION	JUN 2004	MAR 2004
WESTERN EUROPE	**31%**	**28%**
JAPAN	**28%**	**31%**
NORTH AMERICA	**13%**	**11%**
EMERGING MARKETS (INCL. KOREA)	**12%**	**15%**
AUSTRALIA	**2%**	**2%**
CASH	**14%**	**13%**
SHORTS	**30%**	**29%**

Source: Platinum

BREAKDOWN OF FUND'S LONG INVESTMENTS BY INDUSTRY (% OF ASSETS)

CATEGORIES	EXAMPLES OF STOCK	JUN 2004	MAR 2004
CYCLICALS/MANUFACTURING	TOYOTA MOTOR, SCHINDLER, SIEMENS, LINDE, OCÉ	**21%**	**22%**
FINANCIALS	CREDIT AGRICOLE, MITSUBISHI TOKYO FINANCIAL, MITSUI SUMITOMO INSURANCE, NORDEA	**15%**	**16%**
TECHNOLOGY/HARDWARE	AGERE, INFINEON TECH, SAMSUNG, AMD, SUN MICROSYSYTEMS, NEC	**9%**	**9%**
MEDICAL	TAKEDA, SCHERING, NOVARTIS, MERCK KGaA, GLAXOSMITHKLINE	**8%**	**8%**
GOLD AND OTHER	SHELL, BARRICK GOLD, NEWMONT MINING, GOLD FIELDS, NORANDA	**7%**	**7%**
RETAIL/SERVICES/LOGISTICS	VEOLIA ENVIRON, DEUTSCHE POST, HORNBACH, MITSUBISHI CORP	**7%**	**7%**
CONSUMER BRANDS	HENKEL, ADIDAS SALOMON, LOTTE	**7%**	**7%**
SOFTWARE/MEDIA	SKY PERFECT COMMS, SEOUL BROADCASTING, NEWSCORP	**6%**	**7%**
TELECOMS	ALCATEL, ERICSSON, NTT DOCOMO	**6%**	**4%**

Source: Platinum

data and voice to the home. (FTTH is a much more elegant solution, giving remarkable bandwidth with the added attraction of low maintenance costs, though installation involves relatively high initial outlays).

Much as the large telecoms would love to wind back the clock, the internet has permanently changed the structure of their business. **They have no choice but to invest** to protect their existing relationships. Cable TV operators and satellite transmission are eroding their position while the regulatory environment has deteriorated and often forces them to give new competitors access to their networks (eg. pre-selection of carrier).

Alcatel is well placed for this telecom-centric investment boom. Having dominated the global market in traditional closed circuit switching, it has an excellent understanding of the telecoms needs in a digital convergent world. Moreover, it has developed the necessary *kit* (software and hardware) to meet their needs. It is also able to help large corporations move to VoIP by virtue of being a global leader in this arena. The company is behind others in third generation mobile technology, but that may be compensated in due course by its leading position in optical networking. This division has seen sales more than halve since the glory days but metro DWDM (dense wavelength division multiplexing) is improving and prospects are brightening. Traditionally Alcatel has had a lower rating than its peers like Ericsson (which we also own), but this valuation gap now looks excessive.

COMMENTARY

The downward revision of the US GDP numbers for the first quarter, together with some disappointing releases and company announcements, should be treated with caution as until now most of the indicators suggested the lure of cheap money was working its magic to induce a solid expansion of that economy. One explanation may be that householders are responding to **pressure on real wages** from the delayed impact of higher costs, notably fuel, and the expiry of the tax refunds.

We subscribe, however, to the view that employment will gradually rise in synchrony with the expansionary trend and that this will allow real wages to grow. The recovery has now been in effect for around 2.5 years and it would be a very odd cycle indeed for it to abate on its own. It is too early to conclude that a significant shift in consumer behaviour has taken place. We have not been able to detect signs of debt aversion yet. However, the Federal Reserve Board's suppression of real interest rates ameliorated the downturn and has created some distortions in our view. Yes, the Fed has now moved the short term cost of money up one notch to 1.25%, as was widely anticipated, having waited more than twice as long as normal to start the rising rate cycle. The peculiar part of the **puzzle is the behaviour** of the longer end of the interest rate curve. Without clear evidence of foreign government intervention or other extraneous events, the yields on the **long bonds** have been edging down for some while now. This indicates perhaps that we are back to the earlier debate about inflation versus deflation.

Contrary to the popular view that inflation is a regular cyclical phenomenon, it can be shown that there have been long periods of economic history when prices have been stable to flat. In his excellent book, ***The Great Wave****, David Hackett Fischer identifies four episodes of great waves of inflation since the middle ages followed by **protracted periods of price stability**. These coincided with the Renaissance, the Enlightenment and much of the 1800s. This latter episode is particularly interesting for it was a period which included civil wars, mass population growth and migration, and, indeed, the discovery and production of significant amounts of gold. Prices were flat for some 80 years. They spiked around times of war but then fell back to earlier levels. What is more, this price stability seems to have been evident across continents. In each of these periods of price stability, Fischer identifies that real wages rose, **returns on capital diminished** (rents on land and bond yields) and importantly, inequalities narrowed after a noticeable lag. (This in itself led to significant improvements to the crime rate and a drop in moral turpitude in general).

Now clearly we are addressing decades rather than the more intimate time horizons our clients favour. However, we have long believed that the early **1980s witnessed the taming of inflation** in developed countries and that we may experience a similar pattern seen in the 19th century. Behavioural psychology can explain the unwillingness of investors to believe in this new paradigm. This is particularly so when historically the benefits of financial leverage have so helped borrowers. As many clients will know, we strongly believe the **property boom** in the US, Australia, the UK etc is a **direct consequence of tax and interest rate distortions**, combined with a latent trust in the "inflation bail-out". Globalisation, with its facilitation of the free movement of goods, capital and technology, is clearly lubricating the arbitrage of labour costs between East and West. The unpopular dislocation it implies can however be expected to result in periodic temptations towards protectionism. Further, we are not suggesting all prices will be flat, on the contrary we suspect that **many commodities will reach new higher clearing levels** as a consequence of expanded markets. These may, however, be off-set by continued pressure on the prices of traded manufactured goods.

A digression to suggest that there may be an outcome different to that of recent decades. We favour the view that **the burden of debt will ultimately squash the growth trajectory** and that the pump priming need not necessarily cause widespread inflation. In this instance, US short term interest rates which are a full 1.75% below the base line of the 1994 trough, may not rise as far as might be expected. Currency instability is likely to play an important part of the adjustment process.

Turning to other markets, notably those of Asia. The curious phenomenon has been the absence of follow-through buying by domestic investors. Back in the halcyon days of the 1990s "Tiger economies", domestic investors exhibited furious enthusiasm for their share markets. Valuations were high, PEs typically in the high 20s to 30s, and there was no interest in discussing inscrutable subjects such as the marginal return on factor inputs etc. Now that these economies are growing again and financial rectitude has returned at both the national and company level, and compliance is stronger, it seems that foreigners are the only interested players. The scars of the 1998 IMF crisis do not seem to have healed.

Who will then take up the running from the foreigners? This may be necessary if the traditional pattern is followed and foreigners continue to exit their positions. Between late January and April of this year, foreign funds have been transferring their attention away from markets like China, India, Korea and Thailand to Japan. In some cases this is having an impact on their foreign exchange reserves and causing their domestic rates to rise. Once investment fund flows stabilise it will be interesting to see whether exchange rates take away some of the pressure that would otherwise be exerted by higher interest rates alone. This might indeed alleviate some of the pressure on the US dollar.

Some observers are cautious in the aftermath of the Indian election and the formation of a new coalition government under the Congress party. Our interpretation is that the decline of the stock market reflects the inevitable cooling off after a very strong run. The compromises that the new coalition may be forced to accept are in our view no more worrying than the dangerous Hindu nationalist card that the BJP periodically play. The economy is continuing to grow healthily and under Prime Minister Manmohan Singh it seems that reform is still fully on the agenda.

It is too early to assess the degree to which the credit freeze will impact China. Inflation, particularly in basic foods, is rampant (some grain prices are up over 30% on last year) and the official CPI is trending upward with May prices being 4.4% higher than last year. Early reports on the sale of cars and heavy construction machinery suggest a sharp contraction of demand (20% and 60% respectively). However, the less visible markers, such as the loss of revenue to the Provincial authorities from the cessation of land sales and news on the sale of the stock of new housing, has still to surface. At this stage we are inclined to believe that a manageable slowing will be achieved from what was evidently an unsustainable and **disorientating pace**. Here we are relying on the sheer excitement of the new order to carry the economy over this adjustment phase.

An issue that we feel receives less emphasis than it should is the country's **impending water crisis****. Industrialisation and a higher protein diet is placing an unsustainable burden on available water supplies. Domestic planners are increasingly concerned about the faltering flow of the Yellow River. This is showing a worsening trend and failing to even reach the coastal province of Shandong for extended periods of the year. In addition, the depletion of aquifers is evident with the water table of the North China plain falling precipitously. (This area accounts for 40% of the nation's grain harvest, which itself is 75% dependant on irrigation). There are schemes to divert some 40 billion cubic metres of water a year from the Yangtze but these flows are relatively insignificant in terms of the increasing needs caused by rapid urbanisation and industrialisation. More efficient usage will be essential (and the statistics show the country to be way in excess of world standards in terms of tonnes of water used per tonne of steel or paper produced) but the **longer term implications for employment and agricultural prices is of world significance**.

As China continues to grow, albeit at a less hectic pace, its neighbouring suppliers like Japan and Korea will enjoy the slip stream. These economies are anyway gaining momentum and we see no reason to revise our optimistic view regarding their prospects. As is the case in Europe, rather than having specific macro economic views, it is the quality of the companies and their prospects that drives our portfolio construction. On account of the changes of investment fashion, invariably there will be industries and individual companies that become neglected.

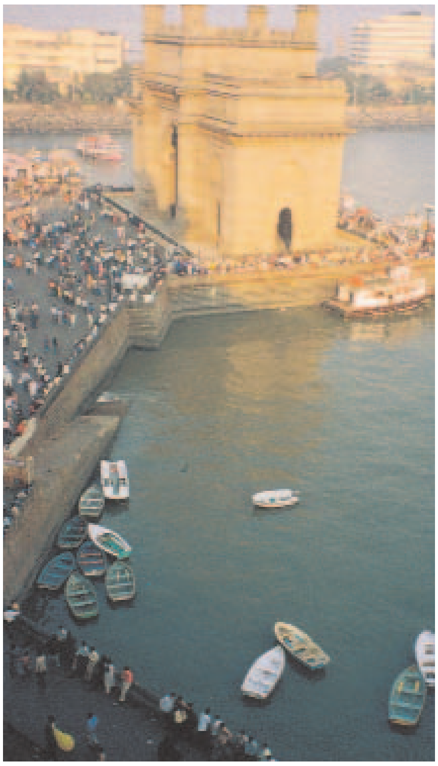
* *The Great Wave, David Hackett Fischer, 1996,Oxford University Press*

** *For further information, please see World Watch Magazine, July/August 1998 issue, Worldwatch Institute*

CONCLUSION

World growth seems to be broadening but inflation is rising and consumers' real incomes are under pressure. As is common, analysts' forecasts are getting well ahead of themselves and are likely to lead to specific disappointments. We believe the **peak of earnings momentum** has been crested which, together with a tightening of liquidity, caused by resources being diverted to real activity, **will limit broad market advances**. Asia, seems behind in this evolution and hence may be more prospective.

Kerr Neilson Managing Director



1: Champs Elysées takes on many shapes

2: Company meetings in the tropics can be fun

3: Don't underrate Japanese chic

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 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, investment returns can be negative (particularly in the short-term).

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

   Platinum International Fund:
   Inception 1 May 1995, MSCI World Accumulation
   Net Return Index in A$

   Platinum Asia Fund:
   Inception 3 March 2003, MSCI Asia Free ex Japan
   Net Return Index in A$

   Platinum European Fund:
   Inception 1 July 1998, MSCI Europe Accumulation
   Net Return Index in A$

   Platinum Japan Fund:
   Inception 1 July 1998, MSCI Japan Accumulation
   Net Return Index in A$

   Platinum International Brands Fund:
   Inception 18 May 2000, MSCI World Accumulation
   Net Return Index in A$

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

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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The Platinum Trust Product Disclosure Statement No. 5 (**PDS**), is the current offer document for the Funds. You can obtain a copy of the PDS from Platinum's web site, **www.platinum.com.au**, or by contacting Investor Services on 1300 726 700 (*Australian investors only*), 02 9255 7500 or 0800 700 726 (*New Zealand investors only*) or via invest@platinum.com.au.

Before making any investment decision you need to consider (with your financial adviser) your particular investment needs, objectives and financial circumstances. You should consider the PDS in deciding whether to acquire, or continue to hold, units in the Funds.