sold first. Because the new machine is more automated and suits the major hospitals and laboratories, the demand for reagents will increase significantly.

An exciting development is the scheduled launch next year of the 'Immugold' machine which uses a revolutionary diagnostic process for rapid results. Traditional tests normally take more than an hour because the blood has to be incubated with the reagent for a set period. The new technology, patented by Diagnostic Products, detects fluorescence occurring when sample blood molecules bind to the reagent on a thin strip of gold. Initially targeted at emergency rooms and doctors' offices where the rapid results would be in demand, this may also be the accepted testing technology of the future. This very impressive technological advance could have a very significant effect on the value of such a small company.

Although large companies have an advantage in distribution and name recognition, they have no monopoly on major innovations. We would expect to pay handsomely for a company with this record of growth and innovation, and with a predictable, bright future. It seems like a steal on less than 15 times next year's earnings and twice book value (the US market is on 23 times those earnings and almost six times book value).

Kerr Neilson
Platinum Asset Management

For those investors who wish to receive the quarterly report direct by e-mail, please e-mail us at platinum@platinum.com.au.

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investor
REVIEW
AUGUST 1998

MLC - Platinum Global Fund

QUARTERLY REPORT AS AT 31 JULY 1998

Performance

Fund Size: $376 mn	1998 Year to Date	Return Since Inception
MLC-Platinum Global Fund	24.4%	91.3%
Morgan Stanley Capital International World Index (Accumulation)	24.9%	125.3%

Our theme of restructuring in Europe has paid off handsomely in the first half of this financial year. Our leading performers were in Italy and France which we accumulated at a time when those markets were considered doubtful contributors to Monetary Union. Further it may surprise you that our holdings in Japan, despite that country's problems and much diminished image, have given us good returns (18% versus 3% for the Japanese market (A$)). We agree with most that Japan has a dysfunctional economy and for that very reason believe there are unusually attractive opportunities to be had from the mispricing of shares within its stock market. The small proportion of holdings in America failed to fully capture that market's advance and the near fully hedged position was a drag on our performance.

Commentary

The markets have been heaving in every direction especially in the latter part of the quarter. This has been brought on by a deepening concern about Asia. The region has been more heavily damaged than most would have imagined. Flows for capital investment and trade finance are scarce and this has a ripple effect on other countries dependent on foreign capital to augment their domestic savings, notably Russia and many of the commodity producing countries of the southern hemisphere.

Apart from the threat of diminishing aggregate demand for goods and services, the other worry about Asia is its effect on corporate profits. The fall in the value of Asian currencies, (varying from 80% for the Indonesia Rupiah to 18% for the Japanese Yen in the last 12 months), has intensified worries about deflation (ie. falling prices on many consumer goods). Asian exports are pouring into the healthy western economies; for example, volumes passing in through the US west coast ports are running 20% higher than last year! The flow is suppressing the price of traded goods internationally and damaging the profitability of those companies competing against such imports. Furthermore, the earnings from this region are translating into far fewer dollars or Euro currencies. In attempting to anticipate the future, investors are concerned that earnings will fall short of forecasts and that in many countries so-called growth assets will fail to achieve higher earnings in the medium term.

It has been interesting to witness the gradual souring of the view of the Tiger economies. Late last year, the consensus was that a contraction of imports and a surge in exports (induced by a massive fall in their currencies) would ensure that the region would have no more than a temporary setback. As time has passed, the picture has become increasingly grim. Social harmony has been threatened, unemployment has surged and hunger stalks. Far from being a blip, the disruption is now endemic. The IMF's intervention is being seen as a grand failure and in some circles, it is regarded (sadly) in a more sinister light. The consensus forecast is now for a much more gradual recovery with the bottom not quite in sight. Adding to concerns is the poor performance of

Report from Platinum Asset Management (Continued)

Top Ten Holdings (as at 31 July 1998)

STOCK	COUNTRY	INDUSTRY	% HOLDING
Rinascente	Italy	Retail	5.3%
Siemens	Germany	Electrical Engineering	3.3%
Swiss Industrial Group	Switzerland	Packaging/Engineering	3.2%
San Paolo	Italy	Banking	3.0%
Sony Corporation	Japan	Electrical Equipment	2.8%
Yamanouchi Pharm.	Japan	Pharmaceuticals	2.8%
Lagardere	France	Media/Defence	2.7%
Acuson	US	Medical Equipment	2.6%
Mikuni Coca Cola	Japan	Bottler	2.3%
Hornbach	Germany	Retail	2.3%
TOTAL			30.3%

Japan and the prospect of China falling well short of expectations.

Fear mutated into perceptions of opportunity in the markets of the west. By late December 1997, the interpretation had started to alter to regard Asia's woes as the west's gain. Cheap imports from Asia and the view that the Federal Reserve Board needs to keep interest rates low (to accommodate Asia, among other things) were seen as favourable stimuli for stock markets. The so-called Goldilocks environment ('not too hot, not too cold… just right'), which allows for slow but steady growth and minimal inflation encouraged valuations not seen even in the booming 1960s (some enthusiasts even argue that the economic cycle has disappeared).

The great disparity in outlook is causing stocks in weak economies to be pummelled while the strong growth companies in the western hemisphere are being extravagantly praised. It is difficult to find a historic precedent where such large differentials have existed.

The relatively small number of stocks leading the charge in western markets (narrowness) is indicative of the growing tensions within the system and are a good reason for caution. Putting this another way, tacit concerns about slowing growth is causing investors to discriminate against smaller sound companies in favour of those with highly visible prospects and predictable growth. The risk premium attached to smaller companies has therefore risen, even though as a group, they have historically grown the fastest. Given our philosophy to invest in under-priced, neglected stocks, it is evident that we find the oppressed more interesting than the lauded. However, we are unwilling to simply buy the deeper value because of the great uncertainties and weak macro-economic factors which will bear down on many businesses for the time being. Our preference is to mostly occupy the middle ground of companies with strong businesses that are growing and where valuations are attractive in a world where the 'risk free rate' (ie. government bonds) is likely to stay at around 5%. In Europe, this growth is often seen in companies engaging in restructuring and rationalisation and/or consumer sensitive companies. Our shares have long been screened for their sensitivity to Asia and in general it is low. In Japan, our focus is very specific with the emphasis split almost evenly between pharmaceuticals, Coca Cola bottlers and exporters/technology stocks which will benefit from the weak yen. The few holdings we have in the United States are enterprises where profit margins are likely to rise significantly led by new product introductions. Sprinkled throughout the portfolio there are several deep value plays.

Outlook

In the coming three to six months, the main point of interest for the markets is likely to be a level of economic growth rather than concerns about inflation. In particular, investors will be seeking evidence that the Japanese economy is starting to improve and that Europe continues to gather momentum. An eye will also be kept on the US consumer who was particularly active in the malls in the second quarter and who, on average, no longer chooses to save (they think the stock market will do it for them).

As we believe most western markets are extravagantly priced, it is likely that there will be an on-going debate about growth versus the appropriate discount rate for shares. By this we mean the questioning as to the appropriate earnings yield one is prepared to accept in order to participate in growth assets (shares) in an environment of very low inflation. A strong case will be made for an abnormally low yield on the presumed scarcity of alternative choices. While we are able to understand this line of argument, the offsetting case is that low inflation has its origin in a changing world environment which in many instances is adding to risk. Hence we are reluctant to participate as enthusiastically as those whose objective is to keep up with a benchmark representing world stock markets.

Conclusion

Though our caution may result in our unitholders failing to maximise their returns in the short term, we believe the argument for weight of money is a supporting factor in the bull market, not the underlying reason for the bull market. Earnings and their valuations will remain our principal criteria in assessing the degree of risk we wish to expose you to.

Stock Story

– Diagnostic Products Corporation (USA)

Diagnostic Products is a David fighting against the Goliaths of the medical equipment and pharmaceutical sectors. A small, family-run business, it was started in 1971 in the kitchen of the founder to develop tests ('assays') to detect such things as infertility, folic acid, prostate cancer, and thyroid problems. The company has a strong track record of growth but despite compounding sales at over 20% remains small, with less than US$200 million in sales.

In the seventies and eighties, tests were done by combining a patient's blood sample with a radioactive reagent (the key product supplied by the diagnostic company) and measuring the radiation using a standard geiger counter. However, over time the industry has been shifting away from radioactive tests because of safety concerns and the high labour costs of manual testing. Test volumes have been increasing as physicians, wary of litigation, make sure that all relevant tests are carried out. Furthermore, new diseases such as AIDS, and new viral strains, creates new sources of demand for tests. But the good growth of the industry has forced a shift to high volume test methods.

Automated testing using non-isotopic antibodies has grown rapidly, with as many as two hundred tests being run on the fastest machines every hour. The equipment involves a carousel to incubate the test tubes containing combined blood/reagent samples. These are fed into a device that fires light photons at the mixtures and measures the reaction, achieving high levels of accuracy. The test tubes are barcoded which eliminates human error and allows minimal labour input. Once the samples are loaded in the carousel, a computer controls the process: the appropriate reagents are added, incubation times monitored, test results measured and reported, and on the company's new machine further tests are ordered and carried out if the results are inconclusive. Once a machine has been leased or bought by a laboratory, supplies of reagents must be ordered frequently to carry out the tests, making this an attractive 'razor and blades' business. Indeed, when we visited the company we found them adjacent to Los Angeles airport, a convenient location for shipping reagents with a limited shelf life to laboratories around the world.

The Goliaths of the industry are companies such as Abbott, Roche, Chiron and Johnson & Johnson. With ample resources, these companies were quick to bring automation to the market. Diagnostic Products was late in following the shift in testing and bought an embryonic company, Cirrus Diagnostics, in 1992. This allowed the company to make the transition to automation and over 3,500 'Immulite' machines have now been placed in laboratories around the world. However, although the machine offers one of the widest arrays of tests and superior accuracy, it is less automated than the competition. Equal to the challenge, the company developed a new generation machine which has been introduced ahead of competitor proposed new offerings and appears to exceed their performance. Selling or leasing machines is important because the reagents are specific to each company's machine; the blades cannot be sold if the razor is not

Disposition of Assets

REGION	31 JULY 1998	30 April 1998
Western Europe	48%	44%
Japan	24%	25%
North America	9%	7%
South America	4%	5%
Other Asia	3%	3%
Australia	2%	2%
Total Invested	90%	86%
Cash	10%	14%
Total	100%	100%