MLC - Platinum Global Fund

Quarterly Review as at 31 July 1999

Performance (to 31 July 1999)

Fund Size: $490m	Last Quarter	Last 12 months	% pa Compound Return over 5 years	Return Since Inception
MLC-Platinum Global Fund	13.0%	22.9%	18.1%	133.7%
Morgan Stanley Capital International World Index (Accumulation)	2.0%	7.4%	19.7%	142.0%

Unitholders may find the emphasis on investment process and philosophy rather tiresome but it is indeed the principal driver to delivering results. There are times when the tenacious adherence to one's philosophy is costly in the short term but it is our experience that in the end a well thought through approach that is well executed will deliver superior results. We are therefore delighted to highlight the good returns the fund has earned over the last twelve months where it outstripped the Morgan Stanley Capital International Index (MSCI) by a factor of three achieving close to 23% versus 7.4%. More importantly though, this has made your fund the best performer over one, two and five years of locally available international funds (per the Mercer survey) with a compound return of 18.1% pa. over the five years. By comparison, the average manager achieved 14.5% pa. Although we note that this is still a little shy of the MSCI, we believe that should be remedied over time. In terms of a global reference, the average manager in the Micropal Global Equities performance tables turned $100 into $180 over 5 years while that same investment in the MLC-Platinum Global Fund rose to over $230.

Helping the performance in the last six months has been the remarkably strong rise in many of our Japanese holdings. In addition, the broadening of the economic recovery has favoured many of the companies with a greater sensitivity to economic growth, as well as smaller companies. Your fund had accumulated these companies previously when they were out of favour.

Disposition of Assets

Region	31 July 1999	30 April 1999
Japan	40%	38%
Western Europe	28%	32%
North America	9%	6%
Other Asia	6%	6%
Australia	2%	2%
South America	1%	1%
Cash	14%	15%

Top Ten Holdings

Stock	Country	Industry	% Holding
DDI Corporation	Japan	Mobile Telephony	4.2%
Sony	Japan	Electronics/Entertainment	3.7%
Alcatel Alsthom	France	Telecom Equipment	3.1%
Siemens	Germany	Electrical Engineering	2.9%
Suzuken	Japan	Pharmaceuticals	2.7%
NTT	Japan	Telecoms	2.5%
NTT Mobile	Japan	Mobile Telephony	2.5%
Acuson	US	Medical Equipment	2.4%
WPP	UK	Advertising	2.4%
Swiss Industrial Group	Switzerland	Packaging/Engineering	2.3%
TOTAL			28.7%

As the shares we owned in Japan and Korea rose past inherent value, we began to trim the holdings. The new additions to the portfolio principally related to telecoms and telecom equipment manufacturers. We added to our holding of Alcatel in France, introduced Ericsson, and added three telecom operators; GTE in the US, Korea Telecom, and Hellenic Telecom (when it was depressed by the Kosovo crisis). We have also made a start on acquiring enterprise resource planning (ERP) companies such as JD Edwards and Peoplesoft and returned to our old friend Novell.

In addition to the normal table of assets by geographic location, we have also provided a table of assets according to their principal business activity. While globalisation is today a common catch phrase, it has particular meaning in investment markets where we are seeing unprecedented aggregation of economic power through mergers and acquisitions. This, together with the internet and e-commerce, is changing many historic relationships and requires analysts to be particularly vigilant. It is no longer profitable to view a company purely in its local context and hence the importance of a multi-national perspective.

Breakdown of Portfolio

Manufacturing	SIG, MHI, Schindler, Lagardere	16%
Consumer Goods	Sony, Canon, Citizen Watch, Lotte Confectionery	16%
Telecoms	DDI, NTT, Korea Telecom, GTE, Hellenic Telecom	14%
IT Hardware	Toshiba, Fujitsu, Samsung Electronics, Kyocera	12%
Services	Star City, Jupiters, WPP, Suzuken	9%
Medical Science	Daichi, Acuson, Diagnostic Products, Draegerwerk	8%
IT Software	Intec, Softbank, Trans Cosmos, Novell, Samsung Corp	6%
Retail	Rinascente, Douglas, Hornbach	6%
Finance	Deutsche Bank, Toro, ICICI, Daiwa Securities, San Paolo	5%

Commentary

There is a clear pattern of convergence in world economic activity, with momentum in Asia and Europe increasing.

i) Japan

The economic figures coming out of Japan are tending to be more positive and while still cautious, the consumer is becoming more confident. Further we take comfort from improved trade figures with the rest of Asia and anecdotal evidence from US companies, at the leading edge of information technology, which are reporting very strong order growth. The official figures such as those of the Tankan survey show an improvement in business confidence although the intention to cut capital spending remains in place. The explanation for our large position in Japan remains unchanged. The country has in the past been afflicted with too little respect for the cost of capital. With its banks in disarray and globalisation requiring the adoption of more open and less interventionist policies, companies are now having to change the employment practices that have prevailed since 1940. This is important as it will lead to capital winning a larger share of National Product at the expense of labour. We therefore anticipate a situation where profits lift even in the face of a dull economy. In addition, with an economy this size, (US$5 trillion), there will be some highly vibrant areas as Japan catches up on IT, deregulation and outsourcing. Further, the technical aspects of the stock market are most compelling: the population has an unfavourable age profile and yet pension funds are underfunded and invested principally in bonds and cash. There is a clear need for these funds to reweight their portfolios towards riskier assets if they are going to have any hope of meeting their long term obligations. Additionally, private investors have a mere 11% of their financial assets invested in shares and in the recent run-up of the Nikkei, they, like the institutions, have been selling to foreigners.

ii) Other Asia

The renewed economic expansion that became evident at the beginning of this calendar year has broadened in some areas, particularly exports. In Korea, Singapore and Taiwan, industrial production is up over 10% on a year ago with Korea leading the field with an advance in excess of 29% in June. Intra-Asian trade is tending to bolster the laggards and it is likely that Thailand and Malaysia will be growing in the second half of 1999 which could lead to production across Asia, excluding Japan, rising by around 10% in the latter half of this year. Helping these economies has been the inward flood of foreign capital which has had the twofold benefit of replacing debt with equity and also causing their currencies to appreciate. This, in turn, has allowed their governments to intervene in the foreign exchanges thereby adding to liquidity and causing further falls in interest rates. Ironically, the absence of western style insolvency laws or, in other cases, the reluctance by banks to call-in the assets behind non-performing loans, has allowed many entrepreneurs to leapfrog their way back into solvency. Under normal circumstances these businesses would have closed but the informal structure allowed them to continue trading even though technically insolvent. As interest rates came down and with the benefit of highly competitive exchange rates they are now flourishing though owing the banks many favours. The last piece of the puzzle has fallen into place with some stock markets rising to levels above those before the crisis which reinforces balance sheets.

iii) Latin America

Just as Asia has surprised professional forecasters with its resilience, even in the face of a bankrupt banking system, so Latin America has surprised with its remarkably low inflation in the face of currency devaluations. However, without the strong savings culture that pervades Asia and in light of their exposure to commodities, these countries have not responded with the same élan. Argentina in particular has been hobbled by having a currency linked to the US dollar.

iv) Europe

An element of patchiness remains in the economies of Europe which are sensitive to capital spending such as Germany and Italy. However, with the strength of the small European economies and the prospect for improving exports, it is likely that Europe will finish the year strongly. Evidence of a more friendly attitude towards business was shown in Germany with the passing by the Centre-left coalition of a tax reform bill which will reduce corporate taxes to 35% in 2001. However, legislators continue to drag their feet on important but sensitive reforms such as pensions.

v) USA

It is important to recognise the role that debt has played in bolstering activity in the strongest economy of all, the US. In the 18 months since Mr Greenspan's celebrated enunciation on market exuberance, debt has risen by US$3.3 trillion or 40% of GNP. House owners, who constitute 66% of households, have taken full advantage of falling interest rates to do two things. They have rolled-down their mortgages into lower rates, mostly on fixed terms, and they have added to their indebtedness; they have drawn out an average of US$15,000 per household for use elsewhere. This is a significant sum in relation to median household pre-tax income of US$37,000 per annum. Personal debt now stands at US$5.6 trillion of which US$4.2 trillion is mortgage debt. The non-mortgage obligations will be sensitive to further rises in interest rates while existing mortgagees will only typically face rising rates when they wish to buy a new home - normal occupancy is for seven years.

The long duration and steadiness of the present phase of economic growth has done wonders to inject assurance across all strata of consumers such that the index of consumer confidence is now close to a thirty year high. This goes a long way to explain retail sales growing at close to 6% versus income growth of 3.5%, pushing the official measure of the savings rate to minus 1%. With this in mind, we were puzzled by the Fed's meek measure of restraint of only one quarter of a percent rate hike in the Federal Funds rate in June and believe it is going to be a game of catch-up through the rest of the year. The Fed is evidently looking for more concrete evidence of price inflation. We believe there are very strong reinforcing elements within the US economy such that the interest rate medicine that is eventually administered will need to be a lot stronger than many presently contend. Hence the risk is that bond yields will peak at much higher levels than investors presently envisage. This will help support the US$ but the sheer size of the trade deficit makes the dollar vulnerable to any adverse change in sentiment towards US financial assets.

Outlook

In the short term and with eyes closed to valuations, markets still seem to have forward impetus. The central banks, led by Japan's, continue to feed liquidity into the system. Corporate activity continues to absorb outstanding shares at a faster rate than new stock is being issued. While economic expansion will broaden in Europe and Asia it seems unlikely to grow at a pace that will threaten inflation or, indeed, fully absorb the pool of cheap funds. Share markets will respond with enthusiasm to an environment of positive earnings surprises though rising interest rates should detract from the valuations of high growth companies. In most markets, there is an absence of attractive alternative investments and only in the US and UK, among the major markets, are we seeing much leakage of funds into property. While the Japanese market has run hard in anticipation of better things, we do not believe any retracement will be particularly harsh in the context of a continuing flow of positive news and the need for domestic savings to seek higher rewards.

Despite all the above, we nonetheless intend to maintain the short position against our US holdings. Exact timing is immensely difficult but it is virtually certain that, at some stage, investment principles will assert themselves. It is clear that at current levels, valuations on Wall Street are highly stretched. It is also the case that the US economy is in a much more advanced phase of its economic cycle than virtually any other, which supports our belief that some time relatively soon, Wall Street will come under pressure from rising interest rates. It may be true that any sharp sell-off will temporarily be seen as a buying opportunity by the now well-trained public. Following each recent setback, the market has been characterised by a new emerging component, be it information technology or the internet, that has taken the index to yet higher levels. Obviously we cannot know that there will not be other large engines to drive the index higher, but as other economies improve there will be growing competition in terms of opportunities and certainly a significant absorption of the liquidity, which has been such an important driver of all markets.

Currency

At present the fund is 53% hedged into Australian dollars, 18% in Yen, with residual exposure of 9% to US$ and related currencies, and 20% to European currencies.

Stock Story

With all the excitement about the internet and e-commerce our shareholders must wonder what we're doing about 'getting a share of the action'. The problem is to identify which are truly durable businesses versus ones that start well only to fizzle out on account of the e-road taking an unexpected turn. Having looked at a wide range of offerings we have concluded that the most attractive way to pursue the inevitable growth of e-commerce is to invest in companies that are not directly in the spotlight but yet will play a significant role in this emergent industry.

Ericsson (Sweden)

A company we have long followed found itself unusually friendless a few months ago. The shares of the giant telecoms equipment manufacturer Ericsson experienced two years of virtual hibernation as investors expressed concern about its relatively poor showing in mobile hand-set model releases (mobile phones) and continuing losses in its traditional business of telephone switches (exchanges). As is usually the case, the market was right in having reservations, particularly as newcomers such as Cisco were completely changing the rules by offering 'routers' which in the internet protocol (IP) world all but obviate the need for traditional exchange equipment. Further, the street's blue-eyed boy, Nokia, had gained a lead over Ericsson in the highly profitable and fast-growing arena of mobile handsets. Adding to the discomfort was concern about the company's exposure to big markets that were caught up in a credit crunch, in particular China and Brazil.

Our assessment is that these were purely transient matters and did not detract from Ericsson's core position in the emerging scene of mobile internet access. There is a lot written about the diffusion of personal computers (PCs) and availability of bandwidth but already in the advanced markets for mobile telephony, such as Finland and Sweden, the volume of data is exceeding that of voice. Before entering that domain, let's examine what Ericsson has to offer. Firstly it is by far the world's largest provider of wireless infrastructure, the base stations and network management software which are the heart and soul of the network, with more sales than its three top competitors, Lucent, Motorola and Nortel combined. Even more importantly, unlike these competitors it can offer the full range of standards, GSM, TDMA and CDMA. Secondly, it is number two to Nokia in the supply of mobile phones and is likely to ship about 33 million units this year, some 14% of the world market. The profitability of the handset division should benefit from the release of several new high performance models in the second half of 1999. The business that has been causing problems is that of the traditional wireline exchanges. Here, too, the company is a global leader with an installed base of 105 million lines and is presently downsizing the business, a task made necessary by the fact that as these facilities become more sophisticated they rely on more embedded software to the extent that Ericsson's latest AXE switch occupies one tenth of the space of its predecessor.

The growth in mobile telephony is truly colossal: from a base of about 300 million users at the beginning of 1999 the market is likely to expand to 1200 million users by 2003 with the peak in growth rate of new subscribers only expected to be reached in 2002 at 200 million pa. For those having concerns about our optimism, spend a moment on a street corner observing passers-by. Australian usage is now 30% of the population while in Finland it is 60%. Crucially, the US market is just coming alive with penetration at 28% and climbing fast. The spend on infrastructure is, therefore, likely to grow at over 20% pa over the next four years.

The mobile phone market is equally interesting as users upgrade to take advantage of smaller phones or new features and standard changes from analogue to digital. Half of this year's sales, perhaps 120 million phones are expected to come from replacement demand. The problem one can envisage is that the very evident scale of demand will encourage the entrance of new suppliers. This will be exacerbated by the convergence of standards which sees the Asian suppliers, Panasonic and Samsung, joining the fray significantly this year. Hand-set prices have been falling by around 20% pa and are expected to average US$196 in 1999. Ericsson's strength in infrastructure rather than phones, compared to its principal rival Nokia, sits well with us on this account. Nokia, though, has stayed at the top end of the market and, by adding new features and by clever manufacturing and marketing, has continued to earn high margins even as prices have fallen.

All this points to Ericsson achieving sales growth of around 20% pa for several years. Profits could even do better as the traditional wireline switching business returns to profit and the US based CDMA business expands. The most exciting part of all though, is the build-up in the use of mobile data transmission. In a digital age, all information, speech and images can be converted into ones and zeros. Hence data can mean sending a 'movie' to a phone or laptop PC or, alternatively, a salesman can interrogate the company's databank remotely, using a hand held device, while in the field. Kyocera has already released a mobile phone with a built-in video camera plus display for those who like to chat and gaze! The world of fully mobile multi-media is right upon us. Ericsson is at the forefront of this aspect of e-commerce and, just as the use of mobile phones has astounded some of us, so too will mobile commerce. The Japanese mobile operator NTT DoCoMo will be the first to roll-out the new wide band CDMA standard in 2001 which will allow full video transmission to a mobile terminal at 2 megabytes per second. In the meantime operators everywhere are beginning to introduce equipment upgrades which will allow mobile users to receive and transmit data at high speed.

Unlike some areas of the internet, this roadmap is fairly clear and Ericsson's place in the market reasonably well defined. Once the present restructuring problems are out of the way, the company is likely to resume its trend growth rate of the last 15 years of about 15% pa.

Kerr Neilson
Platinum Asset Management

For a greater insight into our process, please visit our web site at www.platinum.com.au.

If you have any questions about your investment in the MLC-Platinum Global Fund, please contact MLC Customer Service on **131 831** from anywhere in Australia or **0800 442 550** from New Zealand or **61 2 9466 7114** from overseas.

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