investor
REVIEW
AUGUST 2000

PLATINUM
ASSET MANAGEMENT

MLC - Platinum Global Fund

QUARTERLY REPORT
AS AT 31 JULY 2000

We occasionally hear the MLC-Platinum Global Fund being described as risky compared with other international equity funds. When pursued it seems that this description is attributed to the fact that the Fund does not track a prescribed index and hence may behave differently from say the Morgan Stanley Capital International Index (MSCI).

This seems an odd description of risk. Surely, co-unitholders* share our view that risk is better described as the prospect of absolute loss. We believe losing money is a lot more painful than merely under-or over-performing some statistical concoction. In our attempt to minimise loss (and be sure that we may not always succeed), we follow two courses. Firstly, we invest in those companies which are generally out of favour and where the market seems to be under-pricing their potential. Secondly, we use derivatives and hold cash when there is a dearth of attractive investments. (By contrast, the conventional approach is to manage to an index and remain fully invested at all times).

The interesting outcome of our investment approach is that over-time we have achieved very attractive returns (22% per year compound over the last 5 years). More interesting still, in achieving this return the Fund has fluctuated somewhat less than the average, and produced better returns than average.

**All but two of the staff of Platinum Asset Management has elected to have their entire super invested in the MLC-Platinum Global Fund.*

Performance

Fund Size: $938mn	Last Quarter	Last 12 months	% pa Compound Return over 5 years	Return Since Inception
MLC-Platinum Global Fund	0.9%	37.7%	22.2%	221.7%
Morgan Stanley Capital International World Index (Accumulation)	-1.3%	23.7%	21.6%	198.5%

The quarter was characterised by much churning of leadership in the large markets of the US, UK, Germany and Japan with each falling and in the case of Japan dropping sharply (-9.6%). The pattern was not uniform across Europe however, with France, Italy, Switzerland and the Netherlands achieving 5 to 10% gains. The emerging markets faired poorly after a very strong start to the year with Indonesia suffering the most on account of political uncertainty -21%, while India dropped 12%, as it fell in sympathy with the Nasdaq (some Indian software companies are now capitalised at multiple billions of dollars).

We are pleased with the performance of the Fund which has ridden out the weakness in Japan remarkably well. Our Japanese holdings did better than their market and our other holdings have performed well.

Report from Platinum As

PORTFOLIO ANALYSIS OF BUSINESS ACTIVITY

		July 2000	April 2000
Telecoms & Equipment	DDI, NTT, Verizon, Alcatel	14%	13%
Manufacturing	SIG, Schindler, Linde, Bayer, Akzo Nobel	12%	13%
IT Hardware	Toshiba, Fujitsu, Samsung Electronics, AMD	11%	9%
IT Software	JD Edwards, Novell, PeopleSoft	9%	11%
Finance	Nomura, Daiwa and Nikko Securities, Nordic Baltic	8%	9%
Consumer Electrical	MEI, Sony, Citizen Watch	7%	5%
Consumer Goods	Unilever, Wella, Lotte Confectionery, Coke Bottlers	6%	5%
Medical	Suzuken, Diagnostic Products	5%	6%
Retail	Rinascente, Douglas, Hornbach	4%	3%
Services	Kuhne & Nagel, Stinnes	3%	4%

Changes to the Portfolio

Activity was principally directed at consolidating our larger holdings at the expense of the more recently acquired positions. Some of these had been purchased opportunistically on earlier price weakness and had achieved their price objective notably Komatsu, Nippon Express and Galileo. Among the new ideas introduced were Anritsu (a long established Japanese electronic devices maker that is creating new markets in telco equipment and meeting exploding demand for optical testing equipment). Ambac (a US-based financial company that specialises in underwriting municipal debt and which is now finding new markets outside the US as deregulation accelerates); Loews Corporation (managed by the legendary Tisch family which will benefit significantly from the turnaround in the insurance cycle and the acceleration of activity in oil and gas drilling in response to gas shortages in the States), Mercury General (an auto insurance specialist with a fine record which is now establishing a presence in states outside California). Another old world company acquired was the Finnish based paper products giant, UPM. While evidently a highly cyclical business, we suspect that pressure from shareholders will cause management in the industry to be less willing to add capacity until very late in this cycle and as a consequence, there could be a period when the industry earns some of the highest profits in the last forty years. (Sceptics should note that additions to paper capacity in the US are running at the lowest levels for forty years and indeed below the inherent growth rate of demand).

DISPOSITION OF ASSETS

Region	31 July 2000	30 April 2000
Western Europe	30.5%	25.4%
Japan	26.7%	32.8%
North America	19.5%	16.3%
Other Asia	5.2%	6.6%
South America	0.2%	0.3%
Australia	0.0%	0.2%
Cash	17.9%	18.4%

Currency

Presently 39% of assets are hedged into A$; 36% remain in the Euro, Pound and Swiss Franc; 5% in Yen and the balance, 20%, in US$ and related currencies.

Commentary

Last quarter we flagged the prospect that the bursting of the cyber bubble could give rise to investors alighting upon the prospect of a soft landing. Since then, several leading US

TOP TEN HOLDINGS

Stock	Country	Industry	Holding
PeopleSoft	US	Enterprise Software	4.7%
Akzo Nobel	Netherlands	Chemicals, Pharmaceuticals	2.8%
NTT	Japan	Telecoms	2.6%
Advanced Micro Device	US	Semiconductor	2.5%
Matsushita Electric	Japan	Electrical Consumer Goods	2.4%
Siemens	Germany	Electrical Engineering	2.4%
Linde	Germany	Industrial Gases	2.3%
Bayer	Germany	Chemicals, Pharmaceuticals	2.1%
Citizen Watch	Japan	Consumer Goods	1.9%
Kuraya Sanseido	Japan	Pharmaceuticals	1.2%
TOTAL			**24.9%**

economic indicators such as retail sales, employment growth and housing starts have turned down. The view now predominates that the Fed can hold off tightening further and that the economy can fall back to a growth rate which is within the bounds of its inherent capacity, thereby obviating the need for further rate hikes.

By the nature of such forecasts, we can't know whether high interest rates, a weaker Nasdaq and higher gasoline prices induce anything more than a temporary lull in consumer effervescence. Unlike some, we believe that the strong stock market has significantly influenced consumer confidence and the willingness to borrow and spend. Further, we believe that this influence has grown and indeed partly explains the apparent dissaving by the American public. As has been well documented, stock ownership now far exceeds its previous peak of the mid-sixties when more than a third of households owned shares compared to the present figure of over one half. More importantly, the appreciation relative to GNP from 54% to 170% of the capitalisation of the stock market over the last ten years, has contributed to a massive rise in capital gains. Bridgewater Associates calculates that realised and unrealised gains now account for close to 40% of other forms of household income, principally salaries. This factor, combined with the rising use of credit, which we have highlighted in earlier reports, increases consumers' sensitivity to market values and does raise the risk of a slowing economy turning into something less attractive. We need to watch consumer confidence closely. At present it is very high.

By contrast, European consumers have been very reluctant shoppers notwithstanding surging industrial production, and consumer confidence recovering steadily over the last 18 months to reach a 15 year high. The main culprits are the Italians and Germans; in peripheral Euro zone countries such as Ireland and Spain, consumer spending is very strong. The counterpoint to this is a deteriorating current account for Spain and inflation of over 5% in Ireland. However, as employment increases we strongly believe that consumption will follow the traditional pattern in Germany and Italy – just as we have seen occur in France. In that country, retail sales have strengthened as unemployment has fallen markedly from 12.5% to under 10% over the last 18 months.

These divergences clearly reveal strains within this one-size-fits-all monetary area. To offset cyclical inflationary pressures, there is a need for individual governments to have countervailing fiscal policy. However, tax reform (influenced by competitive pressures) is working against this in some countries, notably in the high fliers like the Netherlands, Spain and Portugal. This clearly exacerbates the task facing the European Central Bank (ECB) and leads to mixed views in the currency market. Nevertheless, the prospect of Europe growing faster than the US over the next year or so, plus the prospect of further rate hikes by the ECB suggest that the Euro will continue to strengthen against most other currency blocks. From an investment stand point, this has important implications amongst other things for currency flows, corporate profitability and stock selection.

Turning to Japan, most commentators are still among the half-empty brigade. We are optimistic given the strong recovery in industrial production (though the rate of change will taper off over the second half of the year from the present 10% growth rate). Measures such as job creation, price levels, auto and housing sales suggest a gradual broadening of confidence and economic activity. From lamentably low levels, corporate profits are rebounding strongly and look set to rise over 20% for this year and next. There is a tendency to believe that the economy will automatically fall back into recession as it did on occasions in the 1990s. However, care should be taken when analysing the past to exclude special factors such as the introduction of the consumption tax, the decline of public investment and of course, the Asian crisis.

It is the prospect of companies earning a satisfactory return on invested capital that is at the heart of our exposure to Japan. Encouragingly, the recent half year profit announcements have far exceeded our expectations. There is however some disappointment with the apparent lessening of urgency of corporate reform but the legislative framework for reform has improved immeasurably. While still in the formative stages, merger & acquisition activity is growing and one can expect various forms of buy-outs and divestments to become more common. Even though the Japanese bull market has been in place for two years, it strikes us as an extraordinary opportunity when still 50% of companies in the first section of the Tokyo Stock Exchange are selling below book value. Goldman Sachs have identified over 100 companies selling at less than cash backing alone. Your Fund owns three such holdings.

The magnitude of these discounts suggest wariness on the part of investors as they consider the many fundamental hurdles that still lie ahead, not least the future funding of government debt. This is at unsustainably high levels and will not be resolved easily. The recent setback in the Nikkei index is, in our view, a classic correction that accompanies a bull market, the so-called “wall of worry”.

If we look at the world at an enterprise level, the striking feature has been the magnitude of corporate activity. Mergers and acquisitions in the first half of the year totalled $874 billion in the US and $1,900 billion in Europe. Industry consolidation remains the catch phrase with mammoth deals in Telecoms (Vodaphone acquired Mannesman and France Telecom acquired Orange); Entertainment (AOL acquired Time Warner, Vivendi bidding for Seagrams); Banking (Bank of Scotland acquired NatWest, Citibank acquired Schroders); Drugs (Glaxo bidding for SmithKline); Autos (Daimler Benz taking 33% of Mitsubishi Motor, GM 20% of Fiat and Volkswagon 19% of Scania). In food, Unilever has bid for Bestfoods having earlier revealed plans for slimming its workforce by 25,000. The whole area of food and packaged goods is finding profit growth elusive in the face of low inflation, scant volume growth and growing market power by the retail chains – who themselves have grown through acquisition. In many cases, these depredations signal an underlying deterioration of profit growth in many industrial sectors. This has led to highly dichotomous market valuations. For example, perceived high growth markets like Nasdaq sell at 130 times earnings while the S&P500 index trades on 23 times this year’s earnings. Further, within the S&P, smaller and/or traditional companies are rated well below the average with the median PE being about 15 times. The same pattern prevails in Europe where shares on the *Neuer* market sell at multiples of sales while traditional old world shares are seemingly punished for their lower growth rates.

Conclusion

Stock markets can look forward to another northern summer of debate about the strength or weakness of consumer spending. Should spending prove stronger than is presently anticipated, central banks can be expected to squeeze rates higher. Though outside the US, there is spare capacity, rising input costs will be evident in most countries. Hence, equity markets look to be range bound until some of the generously priced growth expectations are met.

Kerr Neilson

Managing Director

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 MasterKey on
131 831
from anywhere in Australia or
0800 442 550
from New Zealand or
61 2 9466 7114 from overseas
www.mlc.com.au