However, without more flexibility in the exchange rate of the Chinese yuan, the door to all those nations trying to resolve their problems through shifting resources abroad (ie. exporting) looks discouragingly narrow.

Turning to the matter that perplexes us most: the **sustainability of corporate profitability.** We have long questioned the above trend of corporate profit share; the high level of company earnings in relation to sales and assets compared to their long-term trend, particularly those in the US. Clearly, the opening up of vast pools of competing manpower in Asia and elsewhere has diminished the bargaining power of labour to the advantage of capital. In addition, the cost savings from outsourcing have initially been kept by capital as new cost levels are slow to be reflected in selling prices. However, having lived with portfolios dedicated to Japan and Europe we have also witnessed the difficulty companies face when that lubricating salve of inflation is absent or small.

We have started to see some slippage of earnings with the likes of Best Buy, Dell and Paychex. Rather like the "buy on the dips" of the bull market of the 1990s, the subsequent bull period was sustained by a leap-frogging of earning estimates in the face of rather subdued sales rises. Intuitively we feel this will now reverse and the game will be to stay ahead of the analysts as they try to guess the deterioration forward curve. This will be a gradual process as there have been structural changes and consolidation in some industries. This is the environment we are building into our thinking as we try to navigate our way through the troubled times ahead.

CONCLUSION

It is easy to see lots of issues facing equity markets. What gets less airplay than it perhaps deserves is that the corporate sector is cashed up[2] and valuations are as low as they have been for years.

The skill will lie in the bets one makes regarding stock selection, as the returns from the underlying market may be dull due to the de-risking process which is part of an ongoing deleveraging process.

Kerr Neilson
Managing Director

If you have any questions about your investment in the MLC-Platinum Global Fund, please contact the MasterKey Service Centre on

132 652 from anywhere in Australia or
0061 2 9466 7180 from overseas

[1] For enthusiasts, we can recommend you read "Debt Defaults and Lessons from a Decade of Crisis" by Federico Sturzenegger and Jeromin Zettelmeyer.

[2] For example, total liquid assets of the US non-farm, non-financial sector expressed as a percentage of net worth is at its highest level in 60 years at over 14%. This, in part, is because the recession reduced equity by about 22% but also because of the strong kick-back of profits and the historically low level of capex. The mean over these years has been 8.9%!

Platinum Asset Management is an Australian based international fund manager.
For greater insight into our process, please visit our website at *www.platinum.com.au*

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MLC-Platinum Global Fund

QUARTERLY REPORT

PERFORMANCE (as at 30 June 2010)

Fund Size: $1.49 bn	Last Quarter	Last 12 months	5 years (compound pa)	Since Inception (compound pa)
MLC Platinum Global Fund	-3.0%	15.0%	6.8%	11.7%
Morgan Stanley Capital International All Country World Net Index (A$)	-4.5%	7.0%	-0.9%	4.4%

Source: MLC Investments Limited and Platinum

Having started with some promise, markets had a roller coaster quarter. The gains from the beginning of the year extended into April but the advance was arrested by growing concern about the solvency of Greece and the general level of Club Med sovereign debt. This was temporarily resolved by the intervention of the International Monetary Fund (IMF) and European Central Bank (ECB) with a €750 billion standby facility. However, the focus then shifted to China's efforts to cool their trundling property bull market and concerns developed about a slowing in that country. The news that they would resume the floating of their exchange rate gave a temporary reprieve but the focus then shifted to the disappointing growth statistics coming out of the US. Mirroring these oscillations were big rises in the price of long-dated US treasuries and other favoured sovereign issuers as investors sought defensive assets; currencies danced to the unfolding views about world growth, with commodity producers losing favour.

The final outcome was a decline in the MSCI World Index of 4.5% for the quarter and 3.5% for the six months to June but a gain of 7% for the rolling 12 months. The accompanying table shows the movement by sector, the pattern of which has not materially changed either for the last six months.

The Fund has done better than the MSCI World Index over the quarter but performance in the last six months has been flat. The picture is brighter on a twelve month view with a return of 15%. Importantly, our longer term returns suggest that we can achieve positive returns even in difficult markets.

MSCI* WORLD INDEX SECTOR PERFORMANCE (AUD)

Sector	Quarter	1 Year
Telecommunications	1%	2%
Consumer Staples	1%	12%
Utilities	-1%	-4%
Consumer Discretionary	-2%	16%
Health Care	-3%	5%
Industrials	-4%	14%
Information Technology	-5%	10%
Financials	-7%	5%
Materials	-8%	13%
Energy	-8%	-4%

* Morgan Stanley Capital International — Source: MSCI

CURRENCIES

As noted above, the currency markets were particularly volatile. Fortunately we held our ground, avoiding loading up on Australian dollars when the market's belief in growth was still strong. Further, we profitably traded the June intra-month move and cut the position before quarter end to leave our net exposure about level at 16%.

There are clear sovereign risks within the Euro zone but our belief is that in a relative sense, the Euro is far from a basket case. The resilience of gold suggests that all fiat currency is generally distrusted and that following the recent large realignments, the market is responding to relative attractions rather than absolutes. We do, however, remain predominantly long the US dollar although hints of the need for more fiscal stimulus could readily cause a further shift in our position in favour of the Asian bloc.

At quarter end the portfolio was positioned with 35% exposure to the US dollar; 24% to assorted Asian currencies; 16% Euro; 7% other European currencies and 16% Australian dollar.

PORTFOLIO POSITION

DISPOSITION OF ASSETS (NET INVESTED POSITION)

Region	Jun 2010	Mar 2010
Europe *	27.6%	27.9%
Asia and Other	22.2%	20.3%
Japan	20.1%	20.6%
North America *	16.5%	17.8%
Australia	0.2%	0.3%
Cash	13.4%	13.1%

Source: MLC Investments Limited

* At 30 June 2010, the Fund had a short position in the US against the S&P Index of 6.7% (31 March 2010: 4.5%), the Russell 2000 Index of 2.6% (31 March 2010: 2.5%) and the Dax of 1.0% (31 March 2010: nil).

We have been progressively moving the portfolio to a more defensive stance. As you can see from the schedule over, which is a proprietary classification of sector exposures, the portfolio has little invested in cyclicals (materials and energy), industrials and financials. To the extent that we own financials they tend to be non-banks principally located in Asia. The same bias applies to our exposure to the consumer. Within information technology, we favour software vendors and there is a conspicuous weighting to large pharmaceutical companies in health care.

Johnson & Johnson, **Merck and Sanofi-Aventis** are among our biggest holdings and recently we have been adding **Roche**. Together with its peers, this company has been adversely affected by concerns about government spending cuts, drug development issues and seemingly pedestrian earnings prospects. While these worries are legitimate, it comes back to the question of price! The sector is now trading on a multi-year low versus other sectors and some are valued as though their businesses will actually shrink in the years to come! Some are far better placed than the average regarding impending patent expiry of blockbuster drugs. Often under-emphasised too are the changes within these companies such as the cutbacks on sales and marketing (which is helping to ameliorate the effect of weaker drug pricing); the risk sharing on drug development; alliances with biotech boutiques; the development of their over-the-counter portfolios, which includes branded generics; and lastly, the growing significance of their emerging market businesses.

In the case of Roche, its portfolio is heavily weighted towards biologics. Unlike chemical drugs, bio-similars face a different kind of competition once the patent expires. Competitors need to achieve similar efficacy which cannot be deduced from simple chemical analysis. This results in a significantly different decay path as the drug ages. Unlike other large pharma, Roche has cemented its position with the development of molecular diagnostics at the genetic level. This permits far greater specificity to match the drug to the patient. These tests are good for their own drug development in identifying appropriate patient target pools and will also augment revenues when the tests are used for competitors' products.

In contrast to health care, we find it difficult to raise much enthusiasm for the supposed turnaround sector, **banking.** As we have noted before, western banks face a barrage of political and operational issues that will depress return on equity in the years ahead. Yes, there will be trading opportunities, but this can be said of many other sectors.

Within western financials we have developed a liking for **insurance companies** that are often cheaper than banks and generally took their restructuring punishment following the 2001 bear market in equities. True, the yields on their bond portfolios are going the wrong way (falling) in relation to their promises to their policyholders. Further, in sophisticated markets, their share of such gains that they do make on their investment portfolios are tightly regulated but equally, the level competition reflects a highly consolidated industry. Our significant holdings are **Allianz** (a composite insurer with a strong continental European base but broadening into the US and Asia) and **T&D** in Japan. Both sell below their embedded value, a measure that has become scorned following the loss of asset values. However, we regard these as resilient companies that actually benefit in a world of uncertainty and stressed government finances.

This easy-going, slow growth picture does not apply in Asia where we have been buying **Ping An Insurance** to complement a reduced position in **China Life**. Unlike the latter market leader, Ping An has its origin as a private venture and has been quick to adopt western practices in the way it runs its consolidated back office and its sales force. It has made errors in venturing ahead of itself in acquiring a stake in Fortis. With this fresh in the management's mind, we feel it is unlikely to stray abroad for a while to come.

The share has been weak, having retreated 14% from its 2008 peak, even as it has grown at over 30% a year exploiting strongholds in Beijing and Shanghai and gradually deepening its distribution in the smaller cities.

At present, life insurance is very much a middle class product in China and as prosperity spreads we can, at this stage, see little to interrupt both a strong growth and unusual profitability.

In information technology, our predilection is towards the ticket-clipping companies that supply software solutions like **Microsoft**, **SAP** and **Amdocs** or those that have a strong grip on the hardware plumbing of the internet like **Cisco** and **Qualcomm.** The latter is a new holding which is suffering from the broad de-rating of quality companies that we have been alluding to for several quarters now.

Qualcomm is unique in that it has parlayed its founding technology of CDMA (code division multiple access) to become a virtual gatekeeper to the much broader Wideband CDMA technology that is core to all third and fourth generation mobile devices. Hence it **collects a royalty on every mobile device being shipped** other than those employing the now fading GSM standard. The company is the quintessential play on internet mobility and with adoption quickening as manufacturers use their own or Google's Android platform to try to replicate the success of Apple's iPhone, volume will explode. Of course, there are competitors such as Broadcom, MediaTek and prospectively Intel. The other threat is price decay of devices shipped. We see this as the principal threat to this company's earnings growth. So long as price declines of smart phones in the West do not exceed high single digits, we figure that volume gains will more than compensate for falling unit value.

In a world where we see pricing power being central to achieving positive investment returns, Qualcomm should be able to achieve low teens EPS growth. The same applies to **Infineon**. This is a company that has been through major restructurings and a share price action to match. We bought it well at the lows, traded the position down and now are doubling our holding to participate in the realisation of its remarkable credentials as market leader in power chips to auto assemblers and industry. These mysterious products that have acronyms like IGBT and MOSFET are crucial to the conversion of energy from direct current (read green energy) to alternating current (that which drives motors) and puts Infineon at the heart of energy conservation and alternative energy sources. The share trades on around 10 times 2011 earnings with 15% of its capitalisation sitting in cash and likely to rise if it sells its mobile device chip business.

MLC PLATINUM GLOBAL FUND INDUSTRY BREAKDOWN VERSUS INDEX WEIGHTINGS (%)

Sector	MLC Platinum Global Fund *	World Index
Technology	19.0	16.8
Health Care	10.8	6.6
Consumer	20.1	17.3
Investment/Industrial	13.4	9.8
Materials/Energy	5.6	16.1
Services/Property	6.8	11.9
Financials	15.4	21.5
	91.1	
Gold	5.8	
Total	96.9	100.0

* Long invested position

Source: Platinum and Factset

COMMENTARY

It seems likely that we will hear a lot about **defaults** in the time ahead. Sitting cosily in the developed world many of us tend to forget how common these have been in the past. As recently as the 1980s we had numerous defaults among Latin America and other countries, with Argentina at the forefront. Delving further back, the record of Spain and France between the sixteenth and the end of the eighteenth centuries reveals a miserable six and eight respective episodes of default in these countries[1]. The style and type of resolution has shifted over time and has become progressively more costly for lenders. For example, the Brady work-outs of the 1980s involving 17 countries left creditors with little for their foregone interest, and haircuts on their principal of typically 30% to 50%. So what you remark, well the world got over those and...

While these write-offs are horrible for the equity of banks and hence likely to impede loan growth, the more worrying development is that **fiscal rectitude** is *de rigueur.* With a Calvinistic view about debt it is hard for the writer to disagree with the stance that is emerging in Europe, but it does point to the need for the private sector to leap into the breach to fill the gap created by government austerity measures. Interestingly, the work-outs of the Nordic countries in the 1980s saw the private sector do just that, admittedly aided by improved competitiveness from meaningful devaluations. This seems to be happening again for countries like Britain and recently Ireland. Though tied to the Euro, Ireland has reported an upturn of its economy in the first quarter on the back of strong exports.