Platinum International Fund

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Performance

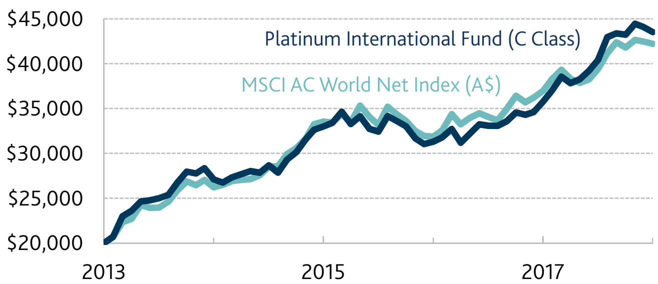
(compound pa, to 31 March 2018)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum Int'l Fund*	1%	22%	10%	17%	13%
MSCI AC World Index	1%	14%	8%	16%	7%

*C Class – standard fee option. Inception date: 30 April 1995.
Net of accrued fees and costs. Refer to note 1, page 6.
Source: Platinum Investment Management Limited, RIMES Technologies.
Historical performance is not a reliable indicator of future performance.

Value of $20,000 Invested Over Five Years

31 March 2013 to 31 March 2018



Net of accrued fees and costs. Refer to note 2, page 6.
Source: Platinum Investment Management Limited, RIMES Technologies.
Historical performance is not a reliable indicator of future performance.

Disposition of Assets

REGION	31 MAR 2018	31 DEC 2017	31 MAR 2017
Asia	37%	39%	37%
Europe	22%	22%	22%
North America	14%	16%	20%
Japan	14%	14%	14%
Russia	1%	1%	<1%
South America	1%	<1%	0%
Australia	<1%	<1%	1%
Cash	11%	7%	6%
Shorts	-14%	-12%	-8%

Source: Platinum Investment Management Limited. See note 3, page 6.

For further details of the Fund's invested positions, including country and industry breakdowns and currency exposure, updated monthly, please visit https://www.platinum.com.au/Investing-with-Us/Investment-Updates.

Top 10 Holdings

STOCK	COUNTRY	INDUSTRY	WEIGHT
Samsung Electronics	Korea	IT	3.0%
Ping An Insurance Group	China	Financials	2.8%
Alphabet Inc	USA	IT	2.6%
Inpex Corporation	Japan	Energy	2.6%
Glencore PLC	Switzerland	Materials	2.4%
TechnipFMC	UK	Energy	2.2%
Siemens AG	Germany	Industrials	2.2%
Royal Dutch Shell PLC	UK	Energy	1.9%
Lixil Group Corporation	Japan	Industrials	1.9%
China Overseas Land & Invt	China	Real Estate	1.8%

As at 31 March 2018.
Source: Platinum Investment Management Limited. See note 4, page 6.

Alas, as the austral summer drew to a close, we witnessed the **return of market volatility**. This derivative, used to measure the likely turbulence of share prices and most widely monitored through the VIX index,[1] had been progressively falling since 2012. The longevity of its falling trend drew the inevitable response from the financial repackaging industry with the offer of an ETF to play this seemingly perfect trend bet. The irony is that volatility cannot incessantly drop (for obvious reasons). When the VIX index spiked in early February, the loss was almost total at an estimated cost of US$3 billion, though with only passing consternation from the media. How slow we seem to learn in this business! Eight years of rest and our memories fade.

Another question around extrapolation relates to the seeming absence of an acceleration of inflation. In the US, unemployment is plumbing the depths, yet the average hourly wage is still increasing very slowly at the current rate of 2.9% p.a. Yield on US 10 Year Treasuries has crept up, but towards the quarter end reversed somewhat to 2.74%, even though the Federal Reserve has declared its hand and raised short-term rates again in March, taking the federal funds rate to 1.75%, compared with 1% a year ago. Unlike earlier cycles, the LIBOR rate, at 2.3%, has moved ahead of the onshore rate. This move has caused some confusion which is partly explained by the 2016 rule changes for money market funds and the unintended consequences of the recent US tax changes. **Money is clearly tightening.**

1 The CBOE Volatility Index (VIX) quotes the expected annualised change in the S&P 500 Index over the following 30 days, priced off option data.

While the **rate of improvement** in the synchronised global recovery, as represented by the PMIs,[2] **has lost some momentum** and the economic surprise indices are fading, evidence of a deteriorating growth outlook eludes us. At present there are the **rising fears about tariffs on trade and concern about tighter control over lending in China** and their adverse consequence for growth. The Chinese data is partly obscured by the timing of the Lunar New Year and the forced seasonal shutdowns of capacity on grounds of air pollution during the winter months. Our own interpretation is that China is quite as worried about the level of debt abroad as it is about that within its own system and is acting accordingly. Granting President Xi Jinping what will surely be a life tenure should be beneficial in the short term, particularly in view of the ministerial reshuffle around his inner circle and important administrative reforms. Some will be dismayed about the longer term implications about which history has a lot to say.

The Trump **tax reform package was well received by analysts who had a field day projecting that most of the value will accrue to shareholders** even though there is the need, and the will, to top up pension reserves and to meet rising minimum wage standards. The corresponding rise in the US fiscal deficit scarcely received a mention, and even the bond market appeared conspicuously unmoved at the prospect of a tidal wave of new bond supply (as Andrew Clifford elaborated on in the Macro Overview). The S&P 500 responded well to the tax legislation initially, but as the quarter came to a close, the misfortunes of Facebook, the presidential threats to Amazon and the malfunctioning of Uber's and Tesla's autonomous vehicles took the gloss off the important tech stocks in the US.

2 The Purchasing Managers' Index (PMI) is an indicator of the economic health of the manufacturing sector. It is derived from monthly surveys of purchasing executives at private sector companies.

MSCI Regional Index Performance to 31.3.2018 (AUD)

REGION	QUARTER	1 YEAR
Developed Markets	**1%**	**13%**
Emerging Markets	**3%**	**24%**
United States	**1%**	**13%**
Europe	**0%**	**14%**
Germany	-2%	13%
France	2%	20%
United Kingdom	-2%	11%
Japan	**3%**	**19%**
Asia ex Japan	**3%**	**25%**
China	4%	38%
Hong Kong	1%	18%
India	-5%	10%
Korea	1%	25%
Australia	-4%	1%

Source: RIMES Technologies

MSCI All Country World Sector Index Performance to 31.3.2018 (AUD)

SECTOR	QUARTER	1 YEAR
Information Technology	5%	29%
Consumer Discretionary	3%	17%
Health Care	1%	9%
Financials	1%	16%
Utilities	1%	5%
Industrials	0%	14%
Materials	-2%	15%
Energy	-2%	6%
Consumer Staples	-3%	4%
Telecommunication Services	-4%	-1%

Source: RIMES Technologies

Unlike earlier periods, the elections in Europe caused barely a stir, mergers and acquisitions and share buybacks, some still funded by debt, continued apace and, surprisingly, even private equity found reason to buy into asset-heavy, low-variable cost businesses. At the same time, other indices were testing their 200-day moving averages as the tightening of money and tariffs were seen as a threat to the Panglossian outlook. The flip side is that companies are increasingly optimistic about the capital expansion programmes. Historically, **capex is sparked by improving corporate profitability**. Contrary to popular belief, capex in the **service sectors accounts for two-thirds of corporate capital spending** in the US. The manufacturing industry only accounts for about 22% of US capex while sectors like finance and insurance account for 9% and mining and oil 7%.

With these strong underpinnings, one might conclude the **high level of share ownership and crowding in hot areas of tech and biotech may have accounted for the weakness** at this quarter's end as investors, full of tech stocks and other 'invincibles', began to apply more caution. Europe and Japan have had the added burden of strong exchange rates to crimp profit growth which had lagged the US.

From the Fund's perspective, this change of tone was only partly helpful. We have been moving to a more cyclical posture, believing that the current strong growth will support more vigorous capital spending and tighter commodity markets. We still believe this to be true and that the softer readings in China are partly seasonal. While the rate of change in the world's largest manufacturing economy may be tapering, there is no evidence that it will be more than a slowdown. In addition, when one compares the valuation of these cyclicals to their invested capital, they are still at remarkably low levels, in particular the hydrocarbon complex (oil companies and the extraction-related support industries), even though the prices of these commodities are well off the bottom.

Our relative performance is showing this uncertainty with a slight underperformance for the quarter, yet we are still far ahead over the last 12 months. The Fund (C Class) achieved 0.7% for the quarter and 21.7% for the year. The MSCI AC World Index (A$) returns over these respective periods were 1.0% and 14.2%.

Changes to the Portfolio

We have been very active rotating out of the notably strong performing areas of the last three to six months into more neglected areas. In particular, we discarded **Wynn Resorts**, **Kering**, **Reliance Industries**, **The Coca-Cola Company**, **Oracle, Qingdao Haier** and most of **Intesa Sanpaolo**, and continued to reduce the Chinese internet names, like **Tencent**, **58.com** and **Sina**. Purchases were made in existing **non-ferrous metal miner holdings**, **Intel** and **Siemens**. We also introduced **Facebook** to the portfolio.

The latter may surprise some for it is hardly an unloved company, though the recent publicity around Cambridge Analytica has seen the stock price fall from US$190 to US$155. There is no doubt that the **political environment facing the three big US internet names** (Facebook, Amazon and Google) **has darkened**. There are many questions about their information controls and the full nature of their earnings sources, as well as disquiet about their business models which depend on offering users free services in exchange for giving potential advertisers access to their personal data. In addition, there are other platforms trying to increase their share of the advertising pool, and even Amazon has succumbed to shifting its business model towards more advertising to exploit the power of its marketplace.

The central question remains '**what is the alternative**?' *Wired* magazine led with an article that proffered alternative apps to displace one's need for Facebook. The problem is that it requires most users to download 10 standalone apps to do the job. Worse still, it requires one's friends to do the same. To date, the consumer response to the 'leak' of one's Facebook friends' data has been remarkably tame. The #DeleteFacebook movement does not seem to be getting traction and the reported change of personal privacy settings has been insignificant. Only 14% of users seem to have made changes since the incident erupted with the majority placidly accepting the notion of an exchange of value. The company has for some time been experiencing defections in North America and the UK with the 12 to 24 age group tending to abandon the platform in favour of alternatives such as Snapchat. Importantly, these are the high value customers in North America and Europe who respectively provide annual revenue-per-user of US$84 and US$27.

The **core social network effect of Facebook remains intact** even if its users are becoming less willing to fully engage and there may be a tendency for new users to be somewhat less valuable, being older users and consumers from lower income countries. The overall network has kept expanding and Facebook claims over 2 billion average monthly users and 1.4 billion daily active users worldwide. In the developed world, it is estimated that users are spending over one hour per day on the platform and it **remains a gateway to other internet applications**. A hint of the longer-term earnings potential may be given by the fact the annual revenue per monthly user in North America is US$84 while that from Europe is US$27 and the Asia Pacific US$8.7 per user!

By the nature of such a phenomenon, the glory days are presumably past. But, like Google, anticipatory acquisitions have been made to broaden the longer-term revenue sources of the company. Facebook's acquisitions of Instagram and WhatsApp are only now starting to contribute revenues.

There are also e-commerce initiatives that can still potentially be harvested. The company itself had been warning of the need for greater investment and a tightening of procedures. In some cases there will be some pressure on revenues and regulation is bound to reduce the efficacy of their offer to advertisers as the melding of bought-in data becomes restricted.

There is likely to be further bloodletting in the days ahead, but the initial reaction had seen the company de-rate to a level that makes it look attractive in relation to the quality of its earnings. It is still growing at probably over 20% p.a., has a clean balance sheet and continues to provide a useful social function. While we recognise that fashion, with all its foibles, is an important adjunct to any social medium, we believe that Facebook's 2018 GAAP P/E of 21 times offers an attractive initiation level.

Shorting

Apart from raising cash by reducing exposure to some of the strong performers noted above, we also added to our short positions. These comprised the NASDAQ index, the Biotech index and a company-specific short position. As at this quarter's end, the Fund's overall short exposure was 14%, up from 12% in December 2017. These positions gave us positive returns that partly offset the weakness in high beta cyclicals that we have been tending to accumulate. Our view remains that, while the growth rate may have peaked and interest rates will gradually tighten credit, **there is a more attractive *geographic balance* to world growth than has been for some time**.

Currency

The US dollar was conspicuous for its weakness. Close to the end of the quarter, we closed our long position on the Norwegian krone to go longer US dollars. The Australian dollar has also been weak and may be bottoming-out on the bilateral rate versus the US dollar given the prospect for improving export receipts, led by natural gas.

CURRENCY	31 MAR 2018	31 DEC 2017	31 MAR 2017
US dollar (USD)	22%	22%	32%
Euro (EUR)	14%	14%	12%
Hong Kong dollar (HKD)	14%	14%	10%
Japanese yen (JPY)	12%	10%	5%
Korean won (KRW)	8%	8%	9%
Chinese yuan (CNY)	7%	7%	-2%
Indian rupee (INR)	5%	6%	7%
British pound (GBP)	5%	5%	4%
Norwegian krone (NOK)	3%	5%	6%
Australian dollar (AUD)	3%	3%	18%
Chinese yuan offshore (CNH)	0%	0%	-6%

Source: Platinum Investment Management Limited. See note 6, page 6.

Commentary

While very cognisant of the problems of excessive debt in the West and China, and hence **the system's greater sensitivity to interest rates**, we cannot become unduly negative. Earlier this year the *Wall Street Journal* described an alarming surge of credit card charge-offs by the smaller US banks, having now reached the same level as in 2006/07. Historically the small banks have been the first to experience this reversal of credit worthiness, being possibly more exposed to those lower down the economic pecking order of credit customers. While the larger banks have started to see an upturn of delinquencies, their experience to date has been subdued. Yes, there is a lot of US consumer debt outstanding: US$1 trillion on credit cards, US$1.3 trillion in auto loans and a further US$1.5 trillion in student loans. But in our experience, the last cause of a crisis, while receiving lots of coverage, is seldom the catalyst for the subsequent economic 'event'.

Earlier we commented on the change in the weight of economic activity globally. It is easy to lose sight of the reweighting of activity over the last 20 years. For example, the traditional economic powers of the West and Japan have seen their share of world activity shrink from 58% in 1996 to 42% in 2016.

A visit to the World Bank website will reveal that while the developed countries have been dawdling along, the so-called developing countries have been galloping. High-income countries have typically experienced a 2.5 fold increase in national income (whether measured in current or purchasing power parity (PPP) terms) from 1990 to 2016, while some large-population countries like India and China have excelled with national income per head rising respectively by 5.8 fold and 15.6 fold. Even populous countries like Pakistan (population of 193 million) and Iran (80 million), with all their conflicts, unhelpful directives from on high and so on, have outshone the West in these terms, admittedly off a low base, to achieve a 2.7 fold improvement. These are not dry numbers. They refer to **the progressive reduction of global poverty** and in particular, are **a forewarning of a further change in the allocation of global physical resources**.

The important statistic seems to be a national income of $5,000 per head at purchasing power parity (PPP). At that point, the broad population is no longer scrambling to survive and discretionary spending begins to show. In particular, the use of fossil fuel and metals takes off. Consider the number of people involved here. If we focus only on the lower-income, high-population countries of Asia, comprising Indonesia, India, Pakistan, the Philippines, Vietnam and Myanmar, we find some 2 billion people on this threshold. Now observe the charts showing this S-curve at work in the rise of the use of crude oil and steel (the same pattern goes for copper and aluminium) for places like Japan, Korea and Taiwan once PPP income per head exceeded $5,000. There will obviously be specific differences relating to each country's consumption, export intensity and other characteristics, but your imagination will likely draw you to the conclusion of a massive impending rise in the demand for these commodities. By way of example, India consumes an average of 1.2 barrels of oil per capita per year. This is similar to China in 2000 when its annual income per head was $940 (current US$). Today China is consuming 12 million barrels per day or 3.2 barrels per capita per year. The charts below also reveal the drop-off in usage in developed countries which obviously offsets some of this competition for resources.

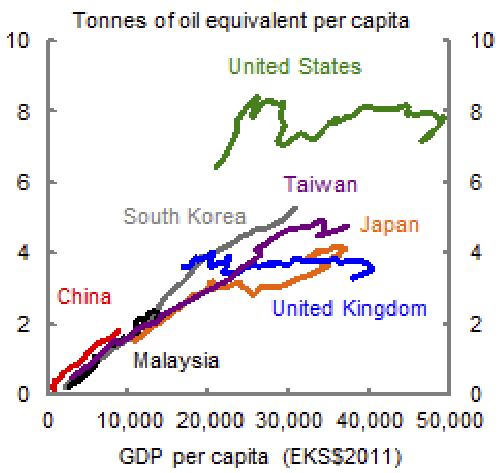
We have written before of the impending tightening of the markets for metals like copper, nickel and cobalt and the market is alive to these prospects, though probably under-estimating the magnitude of this tightness three years hence. The commodity that is conspicuously set up for a surprise is crude oil. Here investors can conjure up stories of substitution, thanks to the electric car or the frugality of new automobiles and the boundless capacity of shale oil. This misses the base case of usage growth caused by the S-curve in developing countries and endorses the observed chronic under-estimation of consumption growth forecasts by the International Energy Agency. While fracking has changed the dynamics of oil supply, the ability of US production to grow exponentially is limited. Already some of the important unconventional basins like the Bakken and the Eagle Ford are showing characteristics of reserve exhaustion while the Permian remains highly productive with significant remaining resources. However, the limits of increasing fracking intensity and endless down-spacing (the idea of decreasing the space between wells) appears to have peaked. Even though US unconventional production will continue to grow, the need to replace conventional production is challenging against the backdrop of a natural field decline rate of close to 5% and a halving of capex from peak levels in 2014. While Brent oil prices have recovered to US$70 per barrel, this is only slightly above the average real level seen over the last 35 years. This theme gives us some interesting investment candidates!

Outlook

The trade conflict and tightening money point to lower valuations. On the trade issue, research reveals that the imbalance is much lower than it first appears if account is taken of the level of activity by American firms in the Chinese domestic economy. When this large American footprint is taken into account, one can see that the negotiating position of the Americans is less secure than the headline trade deficit numbers suggest. Moreover, the newly crowned emperor may prove to be equally sensitive to his constituents' delight in China's re-emerging global status, and this could account for the surprisingly swift rebuttal on the part of the Chinese. Unsettling volatility on Wall Street and possible consumer boycotts will test the resolve of the negotiators!

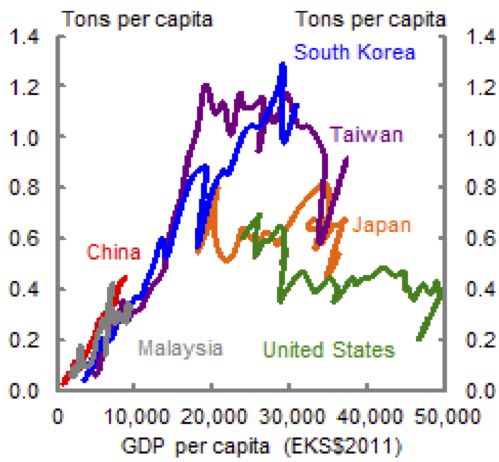
While we have raised our cash and short positions, we are unable to be particularly negative. Some companies' prices have retracted meaningfully and, in addition, many of our holdings look like they will have strong multi-year growth ahead. Valuations are compelling and enhanced earnings growth from buybacks is generally not part of our equation. An interesting calculation by Evercore ISI shows that had US companies not engaged in buybacks since 2000, S&P earnings would be more like US$81 than the current level of US$124. The point is that, prospectively, this aspect of the investment scene may prove to be a weaker driving force than hitherto as capital is repriced. On the other hand, our high exposure to Asia may expose us to greater market volatility as foreign flows are an important constituent of stock market activity there. Some protection is however offered by much lower starting valuations and growth prospects that are arguably superior to those of other markets.

Per Capita Energy Consumption vs. Income (1965-2010)



Source: BP Statistical Review of World Energy 2011; The Conference Board Total Economy Database, January 2012; and CIEC Asia Database. Chart by Brendan Coates and Nghi Luu, the Australian Treasury.

Per Capita Steel consumption vs. Income (1971-2010)



Source: ABARES *Australian Commodities*; World Steel Association *Steel Statistical Yearbooks*; World Metal Statistics; United Nations *World Population Prospects: The 2010 Revision*; The Conference Board Total Economy Database, January 2012. Chart by Brendan Coates and Nghi Luu, the Australian Treasury.

Notes

1. Fund returns are calculated using the net asset value per unit (which does not include the buy/sell spread) of the stated unit class of the fund and represent the combined income and capital returns of the stated unit class over the specified period. Returns are net of accrued fees and costs, are pre-tax, and assume the reinvestment of distributions. The investment returns shown are historical and no warranty can be given for future performance. Historical performance is not a reliable indicator of future performance. Due to the volatility in the fund's underlying assets and other risk factors associated with investing, investment returns can be negative, particularly in the short-term.

   Index returns are in Australian dollars and assume the reinvestment of dividends from constituent companies, but do not reflect fees and expenses. For the purpose of calculating the "since inception" returns of the MSCI index, the inception date of C Class of the fund is used. Where applicable, the gross MSCI indices were used prior to 31 December 1998 as the net MSCI indices did not exist then. Fund returns have been provided by Platinum Investment Management Limited; MSCI index returns have been sourced from RIMES Technologies.

   Platinum does not invest by reference to the weightings of any index or benchmark, and index returns are provided as a reference only. A fund's underlying assets are chosen through Platinum's bottom-up investment process and, as a result, the fund's holdings may vary considerably to the make-up of the index that is used as its reference benchmark.

   The stated portfolio values of C Class and P Class of the Platinum International Fund (PIF) do not include funds invested in PIF by the Platinum International Fund (Quoted Managed Hedge Fund), a feeder fund that invests primarily in PIF. The stated portfolio values of C Class and P Class of the Platinum Asia Fund (PAF) do not include funds invested in PAF by the Platinum Asia Fund (Quoted Managed Hedge Fund), a feeder fund that invests primarily in PAF.

2. The investment returns depicted in this graph are cumulative on A$20,000 invested in C Class (standard fee option) of the fund over the specified five year period relative to the relevant net MSCI index in Australian dollars.

   Fund returns are calculated using the net asset value per unit (which does not include the buy/sell spread) of C Class of the fund and represent the combined income and capital returns of C Class over the specified period. Returns are net of accrued fees and costs, are pre-tax, and assume the reinvestment of distributions. The investment returns shown are historical and no warranty can be given for future performance. Historical performance is not a reliable indicator of future performance. Due to the volatility in the fund's underlying assets and other risk factors associated with investing, investment returns can be negative, particularly in the short-term.

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3. The geographic disposition of assets (i.e. the positions listed other than "cash" and "shorts") represents the fund's exposure to physical holdings and long derivatives (of stocks and indices) as a percentage of the fund's net asset value.
4. The table shows the fund's top 10 long stock positions (through physical holdings and long derivatives) as a percentage of the fund's net asset value.
5. Sector breakdown represents the fund's net exposure to physical holdings and both long and short derivatives (of stocks and indices) as a percentage of the fund's net asset value.
6. The table shows the fund's major currency exposure as a percentage of the fund's net asset value, taking into account currency hedging.

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Some numerical figures in this publication have been subject to rounding adjustments. References to individual stock performance are in local currency terms, unless otherwise specified.

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