Platinum Unhedged Fund

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Portfolio Manager

Performance

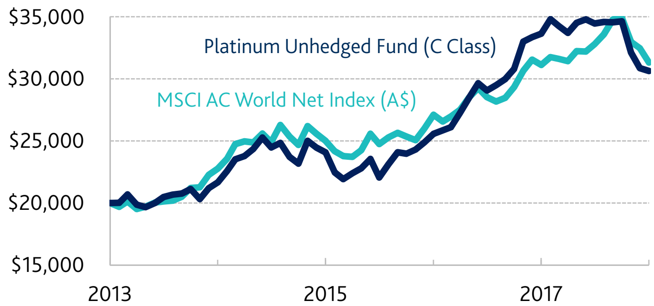
(compound pa, to 31 December 2018)

	QUARTER	1YR	3YRS	5YRS	SINCE INCEPTION
Platinum Unhedged Fund*	-12%	-9%	8%	9%	11%
MSCI AC World Index^	-10%	1%	8%	9%	7%

* C Class – standard fee option. Inception date: 28 January 2005.
After fees and costs, before tax, and assuming reinvestment of distributions.
^ Index returns are those of the MSCI All Country World Net Index in AUD.
Source: Platinum Investment Management Limited, FactSet.
Historical performance is not a reliable indicator of future performance.
See note 1, page 5. Numbers have been subject to rounding adjustments.

Value of $20,000 Invested Over Five Years

31 December 2013 to 31 December 2018



After fees and costs, before tax, and assuming reinvestment of distributions.
Historical performance is not a reliable indicator of future performance.
Source: Platinum Investment Management Limited, FactSet.
See notes 1 & 2, page 5.

2018 saw another year of wide divergence in performance between the US market and its international counterparts. The US index finished the year down 6%, while other major markets like China (-25%), Korea (-19%), Japan (-18%) and Europe (-13%) experienced much steeper declines.[1] If one also takes into account the fact that the US dollar has appreciated between 5-10% against the other major currencies, the performance gap is larger still.

This backdrop did not help the Fund's performance, given that around 75% of the portfolio's investments are outside of the US. Over the calendar year, the Fund (C Class) has fallen 9%, with the majority of the fall being felt in the last six months.

As with our last two quarterly reports, in this report we will again reflect on the key factors that have led to this outcome and examine the portfolio's positioning against the current market environment.

Energy

Of the 9% fall in the Fund's value, around 30% is attributable to our energy holdings.

The swift 36% fall in the oil price since October has adversely impacted all of our oil exposed businesses, but the worst affected were our offshore oil service companies like TechnipFMC, which saw sharp declines in their stock prices.

One of the portfolio's investment themes since 2015 has centred around the recovering oil price, and our strategy included owning a mix of oil producers and oil service companies. In the early stage of the recovery, our holdings were skewed to oil producers who would be the first to benefit from higher oil prices, while more recently our positioning has shifted more towards oil service providers. The oil service industry has been very depressed, with industry capex having been cut 50% from the previous peak, but we expect these companies to benefit from higher levels of investment going forward as oil producers need to replace their depleted oil reserves.

1 Referencing the S&P 500 Index for the US market, the CSI 300 Index for the Chinese market, the KOSPI 200 Index for the Korean market, the TOPIX 1000 Index for the Japanese market, and the Stoxx Europe 600 Index for the European market, each in local currency terms.

With the oil price having now fallen back to US$47 and the industry again in oversupply, a rebound in oil industry capex may feel like a very distant prospect. Why, then, do we remain confident that the rebound will come? The key is the decline rate.

Globally, the world produces and consumes around 100 million barrels of oil per day. This output of 100 million barrels has a natural decline rate of 4-5% per year, driven by the fact that mature fields deplete over time. Global oil demand over the past six years has grown by approximately 1 million barrels per day. The demand growth and the natural decline rate, together, mean that the oil industry, at a minimum, needs to develop new production capacity of 5 million barrels per day to not fall into deficit.

Over the past four years, the vast majority of the 5 million replacement barrels have come from legacy projects coming online (Canadian oil sands, Brazil subsalt, US Gulf of Mexico) that had been commissioned prior to the oil downturn. Over this period, US shale oil output has also grown, but it is worth remembering that annual shale output has never grown by more than 1.1 million barrels per day. Moreover, given the economics of the shale operators as well as the geological constraints, it's difficult to see shale output grow by more than 1.5 million barrels per day without the inducement of oil being priced well above US$60.

With the pipeline of legacy projects soon coming to an end, and shale only able to incrementally add 1 – 1.5 million barrels of oil per day, the question is where the other 4 million replacement barrels will come from.

We think a large amount needs to come from offshore oil developments, and indeed 60% of non-OPEC reserves sits in offshore basins. Like the shale industry, offshore oil service providers like TechnipFMC have re-engineered their technology to lower the cost of offshore developments, to the point where a large number of offshore projects are now able to generate a 10% return on investment at an oil price level of US$50-60 per barrel – economics that are equal or superior to shale.

So while our holdings in offshore oil service companies have recently hurt returns, we remain optimistic about their medium- to long-term prospects. The current level of industry capex is unsustainable and should rise. With our holdings being on price-to-earnings (P/E) multiples as low as 4-7x in a modest recovery scenario (not going back to past peaks), we expect these investments to provide us with good returns in the long run.

Financials

Our financials holdings were the source of another 30% of the fall in the Fund's value over the year, costing the Fund -3% in total performance. The major contributors to this fall were Raiffeisen Bank, KB Financial and Suruga Bank.

The issues and challenges faced by these banks are very different, and so are our re-assessments of their prospects. We added to our holdings in Raiffeisen and KB, whilst Suruga has been a mistake and we have exited the position.

First, on Suruga. When investing in banks, our approach tends to favour buying in the middle of a credit downturn when share prices and earnings are suppressed and bad debt problems are well known. As long as the bank generates enough pre-provision profits (and has enough capital) to handle the losses, this can be a fantastic time to invest, and our successful investments in a number of Italian, Indian and Eastern European banks all fit this mould.

Suruga Bank is a non-standard consumer lender in Japan, lending to niche customer groups such as foreign residents and employees of small and medium enterprises (SMEs) that the major banks tend to ignore. We became interested in the bank after its share price had fallen 60% due to losses from loans it had made to build 'shared houses'.[2]

While we were correct in our assessment that the bank was able to handle the losses without needing to raise capital, a subsequent investigation of its lending practices revealed that Suruga had aggressively moved into far riskier lending company-wide and management had been misrepresenting the true nature of its loan book. This completely changed our view on what the bank could earn in the future and we exited at a loss.

The situation is completely different with Raiffeisen Bank and KB Financial, which we discussed in our September 2018 quarterly report. These are two of our largest holdings in the banking sector. Both are doing well operationally, but have seen their share prices fall roughly 30% from their respective highs. The concerns around each bank relate to issues outside of their control, namely, government interference and regional economic slowdown (refer to the September 2018 issue for more detail).

If we look past these fears and focus instead on the fundamentals of their businesses, we believe that Raiffeisen and KB still represent attractive investments. Both banks are very well capitalised, solidly profitable and can grow in the long-term. The fact that Raiffeisen and KB are both trading below 6x P/E makes them outstanding value in our view, and we have added to both positions.

2 A shared-home is similar to a dormitory where occupants each rent a single room but have shared kitchen, bathroom and living facilities. Shared houses are popular in Japan with students and migrant workers.

China

Finally, any examination of the Fund's performance must include China, given that it was the Fund's largest geographical exposure (representing 28% of the portfolio) and the worst performing major market in 2018. Despite the Chinese market falling 25%,[3] the Fund's China holdings in aggregate fell only by 3% over the last 12 months, an encouraging sign of the strengths of the individual companies we own.

3 CSI 300 Index (local currency).

Over the last year, we have made money in our holdings that are exposed to the environmental remediation and clean energy theme, namely, natural gas pipelines ENN Energy (+25%) and China Resources Gas (+25%). Also our deep value holdings, such as China Overseas Land & Investment (+7%), which were purchased on a P/E of 6-7x, have protected capital well. Offsetting these gains were falls in our more growth-oriented internet advertising holdings, such as Baidu and 58.com which were down 32% and 24% respectively.

So, despite the great volatility in the broader market, our Chinese positions overall have not been a major source of loss for the Fund.

Disposition of Assets

REGION	31 DEC 2018	30 SEP 2018	31 DEC 2017
Asia	35%	36%	42%
North America	27%	27%	20%
Europe	17%	18%	19%
Japan	3%	5%	9%
Russia	1%	1%	<1%
South America	<1%	<1%	1%
Cash	17%	13%	9%

See note 3, page 5. Numbers have been subject to rounding adjustments.
Source: Platinum Investment Management Limited.

Net Sector Exposures ^

SECTOR	31 DEC 2018	30 SEP 2018	31 DEC 2017
Financials	18%	17%	22%
Industrials	17%	17%	18%
Communication Services	12%	12%	7%
Energy	9%	12%	10%
Information Technology	8%	8%	9%
Consumer Staples	6%	7%	7%
Health Care	4%	3%	2%
Materials	3%	3%	4%
Consumer Discretionary	3%	3%	6%
Real Estate	2%	2%	2%
Utilities	<1%	1%	4%
TOTAL NET EXPOSURE	83%	87%	91%

^ A major GICS reclassification was implemented during the quarter. The changes affected the Information Technology, Communication Services (previously Telecommunication Services) and Consumer Discretionary sectors. Historical exposures have been updated for continuity.
See note 4, page 5. Numbers have been subject to rounding adjustments.
Source: Platinum Investment Management Limited.

For further details of the Fund's invested positions, including country and industry breakdowns and currency exposures, updated monthly, please visit https://www.platinum.com.au/our-products/puf.

Net Currency Exposures

CURRENCY	31 DEC 2018	30 SEP 2018	31 DEC 2017
US dollar (USD)	34%	34%	25%
Euro (EUR)	14%	14%	15%
Hong Kong dollar (HKD)	13%	17%	16%
Japanese yen (JPY)	12%	7%	9%
Chinese yuan (CNY)	6%	7%	8%
Indian rupee (INR)	5%	5%	8%
Korean won (KRW)	4%	4%	5%
Norwegian krone (NOK)	3%	3%	3%
British pound (GBP)	3%	3%	4%
Canadian dollar (CAD)	2%	3%	0%
Australian dollar (AUD)	2%	2%	5%
Danish krone (DKK)	1%	1%	1%

See note 5, page 5. Numbers have been subject to rounding adjustments.
Source: Platinum Investment Management Limited.

Top 10 Holdings

COMPANY	COUNTRY	INDUSTRY	WEIGHT
Raiffeisen Bank	Austria	Financials	3.6%
Applus Services	Spain	Industrials	3.0%
Jiangsu Yanghe Brewery	China	Consumer Staples	3.0%
IHS Markit Ltd	USA	Industrials	2.9%
Kweichow Moutai	China	Consumer Staples	2.9%
Alphabet Inc	USA	Comm Services	2.8%
PICC Property & Casualty	China	Financials	2.8%
KB Financial Group	Korea	Financials	2.8%
Sanofi SA	France	Health Care	2.7%
Seven Generations Energy	Canada	Energy	2.4%

As at 31 December 2018. See note 6, page 5.
Source: Platinum Investment Management Limited.

Changes to the Portfolio and Outlook

With multiple global markets in decline, investors are understandably asking 'are we slipping into a global recession?' and 'how much further can markets fall?'.

While we devote considerable time attempting to understand where we are in the economic and market cycle, the problem with these questions is that they can never be answered with certainty.

However, there are some meaningful observations we can make, with certainty, today:

- Many major markets have fallen by 20% or more from their highs in early 2018. China is down 30%. Korea and Japan are down 20%.
- Investor sentiment is negative.
- Most importantly, a whole range of stocks have now fallen by 30-50% and are trading on single digit P/E multiples. These stocks have already priced in a recession happening now.

Falling prices, low valuations and a more cautious sentiment are all indications that **risk has reduced and the prospect for better returns has increased.** These factors indicate one should be adding to stocks, and that's what we have been doing. Over the quarter, we have initiated new positions in **General Electric** and **Bharti Airtel**, and added to our existing holdings in **Seven Generations**, **Skyworks**, **Microchip**, **Weibo**, **Intesa Sanpaolo** and several more.

While the outlook has improved and we have been adding to stocks, this does not mean we believe markets are about to take a V-shaped recovery. From a pure timing perspective, history shows that after markets experience circa 20% declines, they tend to remain volatile for some time. Basically, investor confidence has been shaken and it will take time to rebuild. The Fund has a reasonable cash balance, and we will be looking to use that cash to increase our investments over the coming months.

Notes

1. Fund returns are calculated using the net asset value (NAV) unit price (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. Fund returns are net of fees and costs, are pre-tax, and assume the reinvestment of distributions. Returns for P Class are net of any accrued investment performance fee.

   The MSCI Index returns are in Australian Dollars and are inclusive of net official dividends, but do not reflect fees or 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 Index was used prior to 31 December 1998 as the net MSCI Index did not exist then. Fund returns are provided by Platinum Investment Management Limited; MSCI index returns are sourced from FactSet.

   Platinum does not invest by reference to the weightings of the Index. 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. Index returns are provided as a reference only.

   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.

   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 specified Fund over the specified period relative to the specified net MSCI Index in Australian Dollars.
3. The geographic disposition of assets (i.e. the positions listed other than "cash" and "shorts") represents, as a percentage of the Fund's net asset value, the Fund's exposures to the relevant countries/regions through direct securities holdings and long derivatives of stocks and indices.
4. The table shows, as a percentage of the Fund's net asset value, the Fund's exposures to the relevant sectors through direct securities holdings as well as both long and short derivatives of stocks and indices. In the case of the Platinum Unhedged Fund, the Fund does not undertake any short-selling. Its net exposures are therefore the same as its long exposures.
5. The table shows the effective net currency exposures of the Fund's portfolio as a percentage of the Fund's net asset value, taking into account the Fund's currency exposures through securities holdings, cash, forwards, and derivatives. The table may not exhaustively list all of the Fund's currency exposures and may omit some minor exposures.
6. The table shows the Fund's top 10 long equity positions as a percentage of the Fund's net asset value, taking into account direct securities holdings and long stock derivatives. The designation "China" in the "Country" column means that the company's business is predominantly based in mainland China, regardless of whether the company's securities are listed on exchanges within mainland China or on exchanges outside of mainland China.

Disclaimers

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