

Monthly Report to Shareholders of the Optimal Japan Absolute Long Fund 5th September, 2005

	OJAL NAV*	Performance
31 August 2005	\$11.06	+6.76%

* Price is NAV after performance fee at the Fund level but is subject to equalisation at the investor level.

Despite the uncertainty usually found with elections approaching, the Japanese equity market rose 5.5% in August and closed at the highest level since June 2001. On August 8th, Prime Minister Junichiro Koizumi made good his threat to dissolve the Diet should his postal privatisation bill fail and called an election for September 11th. The 8th also marked the low point for the index and by month-end, Topix was almost 7% higher. Although the opinion polls show a likely win for Mr Koizumi on the 11th, we do not believe the alternative result – a government formed by the Democratic Party (DPJ) – is any reason to turn negative on the outlook for Japanese equities. The DPJ is centrist in policy and in many ways, closer to Mr Koizumi's view of a modernised LDP than the existing government. Moreover, with the economy recovering and corporate profits set for a record fourth consecutive year of growth, few voter groups have strong incentives to seek a change of course.

We have seen far better economic data in areas that bode well for consumption and corporate capex. Full time employment has recently turned positive for the first time in seven years and with better wage and bonus payments, this should boost the propensity to consume. Prolonged underinvestment by Japanese companies through the 90s has greatly aged Japan's capital stock and renewed capex is not only desirable, but essential for ongoing efficiency gains. Manufacturing capacity utilisation rates are running at 100% in most industries and with inventories now worked off, this area should be a positive contributor to GDP and profits.

Although the market as a whole was strong in August, it was noteworthy that the best performance came from large caps. Topix gained 5.5% but the Topix Core 30 index rose 6.42%. In contrast, the Jasdax index was up only 0.24% whilst the Tokyo Second Section also underperformed with a 1.48% gain. The tiny Mothers index – such a strong performer in the past couple of years – fell 1.99%. On the numbers we look at, all these small cap indices are trading at premium valuations to that of the broad Topix index, and accordingly, leads us to expect worse relative performance in a generally stronger market.

A bullish view on Japan is always best reviewed in a scenario where the US market is weak. Can Japan “decouple” or will it assume its usual dependency and decline with other large markets. Well in August, Japan rose strongly while the US (S&P500) fell 1.1%. This was in a month when Japan's currency also rose by 1.9% or so versus the US dollar, so the relative return from Japanese equities was even greater. Although we expect general weakness to hurt Japan as well, the outlook for a “go it alone” Japan bull market is stronger given the foundations for the economy are so much better than they were in 1999 or in 2003. The case for a bullish view is, in our opinion, the best it has been for fifteen years.

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Optimal FUND MANAGEMENT

Month-end investments (as % NAV): 89.27 %

Fund size: US\$ 26.7 mil

Total number of positions: 27

Top 5 positions:

	% of NAV
Toyota Motor	6.27%
Mizuho Financial	6.14%
Mitsui Fudosan	5.45%
Mitsui OSK	5.44
Sumitomo Metal	4.70%
Total	28.00%

Best Performers: Mizuho Financial Group, Tokyo Tatemono, Mitsui Fudosan, Mitsui OSK

Worst Performers: Ishihara Sangyo, Ajinomoto, Chintai Co

Historical Returns

Below we provide a table detailing the monthly returns of the Fund since its inception in September 2004.

Optimal Japan Absolute Long Fund Net Monthly Returns in USD													
Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2004									-1.6	-1.32	6.18	2.52	5.70
2005	1.61	2.05	-3.83	-0.47	-1.81	-0.58	1.17	6.76					4.64

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