Optimal FUND MANAGEMENT

Monthly Report to Shareholders of the Optimal Japan Absolute Long Fund 13 September, 2006

	OJAL NAV*	Performance
31 August 2006	$13.89	-0.29 %

**Please note that the Fund is now quoted with only an NAV price rather than with subscription and redemption prices so the return shown at the Fund level may not be the same as the return of a discrete investment that might be subject to performance fees through equalisation.*

The Topix index had a gain of 3.97% in August to mark the second largest monthly gain this year – so far. Because the Yen was quite weak against the USD, the return in dollars was only 1.55%, but even with that lower hurdle, our funds struggled overall. It was not an investment style issue – as the MSCI Japan Value index return exceeded that of the Growth index in August – but reflects a more cautious tone to the global economic outlook and for the demand for resources and capital goods. The Machinery and Wholesale (mainly trading companies) sectors both performed poorly in August whilst Mining and Oil & Coal Products both had negative returns. We had reduced our position in Kubota over the past few months, but were hurt nevertheless by the 8% drop in the stock price, while other machinery plays we hold such as Makino Milling, Komatsu and Hitachi Construction Machinery also fell.

The largest percentage decline amongst our stocks was in the mid-cap stock Arrk. This was offered at the daily limit down on both August 14th & 15th after which it was changing hands 33% below the previous traded price. Our colleagues in Tokyo have already met with a director of Arrk to discuss the disappointing revision down and on September 21st, we travel to Arrk's head office in Osaka to meet their President and senior management. From discussions to date it appears that the bulk of the shortfall is expected from their Asian operations and 90% of that is due to Korean subsidiaries. We will assess our options after the meeting but at the current price it trades at just over 1x book value so would not appear to have too much downside. Fortunately our position at the start of August was only 1% so the portfolio's loss was significant, but not disastrous.

We have written before about the attractions of some Japanese companies with large market shares in businesses that have seen global consolidation. The autos, the steels, the metal refiners and precision equipment areas all come to mind but the problems come when we search the domestic sectors for similar stories of industry consolidation and better profit margins. Daiwa's strategist has compared companies with at least 30% of sales coming from overseas with those that have less than 30% external dependency. The results are interesting and paradoxical – at least to us. As a group, the "international" companies have significantly higher profit margins than the "domestic" ones, and yet they trade at lower multiples of earnings, cash-flow and book value. The logic in this escapes us, unless you believe that the market is so prescient and long-term in nature, that it is pricing in 1) a significant slowdown in global economic growth and/or loss of market share by the Japanese, or 2) a major boom in M&A and consolidation in the domestic sectors that will lead to greatly improved

Level 5
175 Macquarie Street
Sydney NSW 2000
Phone: 61 2 8239 3300
Fax: 61 2 8239 3333
optimal@optimalasia.com
www.optimalasia.com

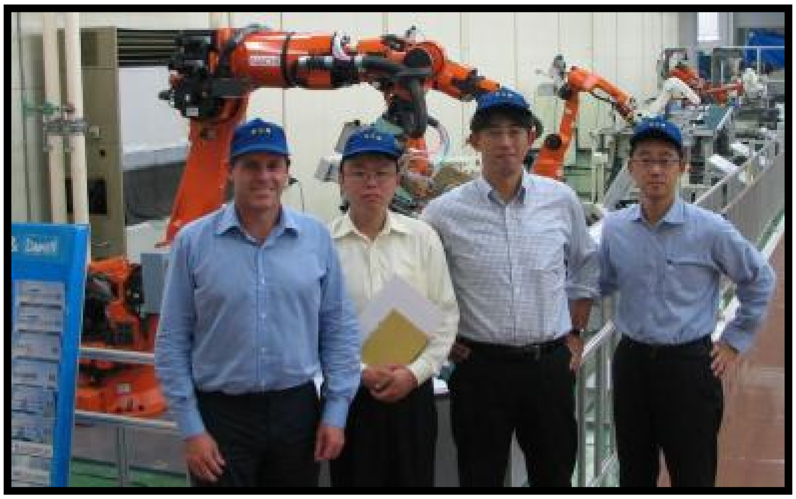
6F Izumikan Kioicho
4-3 Kioicho, Chiyoda-ku
Tokyo 102-0094
Phone: 81 3 3238 1671
Fax 81 3 3238 1687

profitability. We would love to believe that scenario 2) is imminent, but we do not think this would make us much money – or at least not much any time in the next couple of years. The potential is certainly there for consolidation as evidenced by the following data. These are Nikkei sector classifications and show, in brackets, the number of listed companies in a selection of domestic-focused industries:

Electrical machinery trading companies (89)
Textile trading companies (46)
Food trading companies (39)
Construction materials trading companies (21)
Machinery & metal trading companies (70)
Chemical trading companies (28)

When evidence emerges that consolidation is occurring in these sectors, we will be waiting to identify the acquirees, but for now, our sense is that these companies do not deserve a premium valuation.

Optimal visits Nachi-Fujikoshi's Toyama Plant in August 2006



(L-R) Warwick Johnson, Hideo Takagi, Hiroshi Maeda, Hisashi Yatsuo

To finish on an administrative matter, we wish to stress that any applications for redemptions or subscriptions in our funds that come in to EFA (administrator) after the dealing deadline will be rejected. Please visit our website www.optimalasia.com for related information and we encourage you to contact us through the web-site.

Month-end investments (as % NAV):
Equity Long: 96.35%
Net exposure: 96.35%

Fund size: US$ 131 mil

Total number of positions: 33

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Top 5 positions:

	% of NAV
Tokyu Corp	5.13 %
JFE Holdings	4.76 %
Toyota Motor Corp	4.70 %
Mizuho Financial Group	4.62%
Showa Denko	4.44 %
Total	**23.65%**

Best Performers: Tokyu Corp, Nippon Steel, Tokyo Tatemono

Worst Performers: Kubota, Arrk, Makino Milling

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	9.32	-0.75	3.25	8.64	27.25
2006	3.57	1.22	3.55	2.74	-4.40	-1.32	-1.55	-0.29					3.27

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