

## Monthly Report to Shareholders of the Optimal Japan Absolute Long Fund 10<sup>th</sup> March, 2006

	OJAL NAV*	Performance
28 February 2006	\$14.10	1.22 %

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

The aftershocks from the Livedoor collapse have continued through February with internet stocks (and other asset poor/concept rich companies) selling off sharply. Although the Topix index fell almost 3%, the Hercules and Mothers indices were down 13% & 14% respectively and have fallen by a third since their highs on January 16<sup>th</sup>. In CY2005, the Hercules index rose 76% and Mothers was up 48% so one is reminded of the oldie “if you can’t take the heat, get out of the kitchen”. We never made it to the kitchen and missed out on the upside last year as we concentrated our attention in other parts of the market. Thanks to that, we also missed out on the damage wrought last month. Whether the market fell because of Livedoor, or it was a case that Livedoor’s problems coincided with a bit of buyers’ fatigue is hard to judge, but it did not strike us as odd that the market ran into selling above 1700 on Topix.

Economic data remains highly supportive of an optimistic outlook for the year ahead. Tokyo office vacancies have fallen below 4% to the lowest level since 2001. In mid 2003, this had reached 8.5% so the improvement has been strong. We are also hearing very persuasive anecdotal evidence that rents are rising by hefty margins in central locations and these will lead to revaluation of assets in many real estate companies. Bond yields have risen, near term futures for three month Yen are reflecting higher interest rates and the Bank of Japan has termed the recent private consumption data as solid.

Two of our Sydney team made separate trips to Tokyo in February and were both struck by the greater sense of optimism at company visits. This willingness to expand again is reflected by national bank lending figures which turned positive year-on-year in Q4 2005 for the first time since 1996. After more than a decade of balance sheet repair, corporate Japan is now feeling ready to spread its wings and the resultant capital spending will support domestic demand. Visits to two major equipment manufacturers confirmed that they were running their operations at 100% utilisation rates and were hoping to boost output with modest additions to plant. Interestingly, their margins were higher overseas than in Japan – a situation they ascribed to excess competition in Japan whereas in foreign markets, their field is dominated by three players. It is a familiar story and one that goes a long way to explaining the persistently low returns on capital seen in most domestic industries such as retail, construction and food.

The Fund’s return was helped in no small way by a successful short position in the Topix futures that we opened on February 2<sup>nd</sup> and closed on the 17<sup>th</sup>. For the Optimal Japan Absolute Long Fund, the resulting profit contributed almost 150bps and made the difference between a negative and positive return for the month.

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# Optimal FUND MANAGEMENT

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

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

**Equity Long: 73.39%**

**Net exposure: 73.39%**

**Fund size: US\$ 109.1 mil**

**Total number of positions: 26**

**Top 5 positions:**

	% of NAV
Sumitomo Metal	5.02%
Kubota Co	4.88%
Mizuho Financial G	4.53%
Mitsubishi Co	4.65%
Sumitomo Trust Bank	4.48%
<b>Total</b>	<b>23.56%</b>

**Best Performers:** Nippon Steel, Kubota Co, Toyota Motor, JFE

**Worst Performers:** Sumitomo Trust & Banking, Tokyu Co, Fujitsu

***Historical Returns***

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

<b>Optimal Japan Absolute Long Fund Net Monthly Returns in USD</b>													
<b>Year</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>	<b>May</b>	<b>Jun</b>	<b>Jul</b>	<b>Aug</b>	<b>Sep</b>	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>YTD</b>
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											4.83

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