

## Monthly Report to Shareholders of the Optimal Japan Absolute Long Fund 9<sup>th</sup> February , 2005

	OJAL NAV*	Performance
31 January 2005	\$10.74	1.61%

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

The new year began in uninspiring fashion with a decline – albeit tiny – of 0.3% in the Topix index. Value, as measured by the MSCI Japan Value index, outperformed Growth to continue on in the same vein as 2004. In absolute terms, both were down. More telling was the strong performance from mid and small cap indices and the weakness in the Topix 100 index. The latter measures the performance of the 100 largest stocks listed on the Tokyo Stock Exchange and it has been a dismal (relative) story for these stocks over the past year. In that time, the Topix index has risen 13%, the TSE2 (second section) is up 47% but the Topix 100 has risen only 8%. We do not consciously target small caps but as we do search for value, it does push us into the smaller company area when valuations favour them. Despite (or because of) the strong performance from smaller stocks of late, we are wary of becoming too exposed to this group as they are no longer cheaper than the market as a whole and earnings growth is no better than the average. If we can find well-run large caps that are as cheap with growth in earnings, we would prefer be in them, so we have been reducing some of our less liquid names in the past month or two.

Banks and Real Estate have led the market since it bottomed in late October despite the fact that investors and economists generally remain only mildly positive on domestic demand. Based on our own company visits and research, the gains in land prices, increased investor interest in property investments and the desire of the major banks to expand again after a long contraction, tells a positive story for the stocks in these areas. In late January we visited Mitsui Fudosan and Mizuho Financial Group and came away very confident that our (core) holdings in these stocks are justified. One fact we found of particular interest was that Mizuho's group securities companies would report pre-tax profits this year (ending March 2005) of more than Y50bn. We, like most investors I believe, had thought they were sub-scale and in all likelihood, profitless. At Y50bn, their profit ranks well behind Nomura's, but is approaching two thirds that of Nikko Securities and is more than twice the profit of Mitsubishi Securities. Although those with long experience in Japanese equities may rue the passing of the old stalwart brokers such as Nippon Kangyo Kakumaru, Wako, New Japan, Dai-Ichi (now all trading under the Mizuho umbrella), the reborn bank-owned brokerages must be causing their domestic and foreign rivals to rethink their approach to the business. It remains to be seen whether the banks can regain any of their vitality in the same way. Although improving, Mizuho's return on assets trails in the wake of large foreign banks – but that in itself is one of the attractions if you believe the tide has turned.

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# Optimal FUND MANAGEMENT

The Fund's return in January was hurt by the strength of the USD against the Yen. As the Fund's assets are all in Yen, the translation back into dollars for NAV calculation causes fluctuations that might work for or against us. The monthly gain in our long/short funds exceeded that of this Fund partly due to currency effects and also because there were gains from the short positions in January. One other factor – touched on above in the first paragraph – is that this Fund tends to hold fewer small cap names and thus lacked the positive impact that the long/short funds felt from gains in a few of these small stocks. We believe small cap outperformance will soon come to an end.

## Major Positions

Toyota Motor, Mitsubishi Co, Tokyo Tatemono, Haseko, Mizuho Financial

Month-end investments (as % NAV): **87.49%**

Fund size: **US\$ 13.6 mil**

Total number of positions: **23**

## Top 5 positions:

	% of NAV
Toyota Motor	6.38%
Haseko Co	5.72%
Tokyo Tatemono	5.48%
Mizuho Financial	5.41%
Mitsubishi Co	5.14%
<b>Total</b>	<b>28.13%</b>

**Best Performers:** Haseko, Tokyo Tatemono, Ushio, Kubota, Nippon Mining

**Worst Performers:** Mitsubishi Co, Toyota Motor, Sumitomo Trust & Banking

## 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												1.61

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