

Monthly Performance % - as at 29 January 2010

	NAV	January	YTD	Asset size
Offshore Feeder	\$10.72	2.58%	2.58%	\$210M

Nothing occurred in January that would make one want to change one's view of the opportunities in equity markets. Generally speaking, stock prices rose in the first half of the month and then fell away to close the month lower. Europe and the eastern US had dreadful winter storms and Haiti suffered a devastating earthquake. All in all, the omens were not good.

Markets in all parts of the world now take close note of events in China. Daily equity market movements are still highly correlated to those of Wall Street, but most investment strategies incorporate a view on China in a way that was barely dreamed of a decade or so ago. We invest in Chinese companies and spend a lot of time assessing the risks and opportunities there, but generally find more to admire (economically speaking) than to deride. A sizeable minority of investors – or at least commentators – believe that the Chinese economy is a bubble waiting to be pricked and that the mistakes made by the Japanese during the '80s and early '90s are being repeated by the Chinese with inevitably ugly consequences. They might be right, but we are not so bearish on China. For one thing, the Chinese are not ignorant of the imbalances that Japan created, and are not as indifferent to the cost of capital as Japanese companies were in the 1980s. They may not be working to maximise their returns on capital at all times, but investors are also able to decide which companies are worth owning shares in and will generally avoid the chronic wasters of capital.

Unlike China, events in Japan do not feature highly in forming global investment strategies. It is a market that is neither loved, nor reviled - merely ignored. We think that this situation is hard to fathom and believe that the times are changing in Tokyo.

In the 1990's, the weakened state of the Japanese banks meant that borrowing became more difficult for most Japanese companies. As a result, companies needed to improve their returns (and cash flow) to justify loans or raise fresh equity from the market. Returns on capital bottomed in 1995 and have been on an improving trend since then until disrupted severely by the 2008-2009 economic crisis. Coming out of the economic slump, we expect that returns could be heading higher on a sustained basis through a reduction in capex as Japanese companies look to lower costs and manage their businesses in a more efficient manner. Cost cutting has been dramatic in the past 18-24 months and a growing number of company forecasts show operating profits recovering to the March 2008 peak levels in the year ending March 2012 despite overall sales forecast being lower. Margins are recovering rapidly as costs are cut and management decisions

improved.

The greatest potential for surprise lies in the area of government policy. Many observers have been disappointed by political developments – or lack thereof – since Mr Hatoyama's DPJ won government last year. I am not sure whether they are going to make a success of their time in office, but I am more confident that Japan has a greater chance of success with them in power than it would have with the moribund LDP in charge. They face very real and very large problems – and no one is unaware of them. There needs to be wholesale, root-and-branch reform of the system of taxation and the provision of pensions. Too much of the tax burden falls on relatively few companies – usually the larger, listed ones - and on the declining number of salaried workers supporting an increasing population of retirees. Japan needs to introduce an identification system (tax file number, or social security card) to record incomes and taxation and to remove the current incentive for people to create small private companies through which they can push expenses and lower their taxable income.

These schemes are not easy to design and implement, but the need is obvious. Japan has a very low tax take because of these inefficiencies and the system is increasingly unfair on the salaried and those willing to be profitable.

We intend to concentrate our research on these areas of public policy and will write again on the issues in the months ahead.

SYDNEY: Level 5, Wyoming, 175 Macquarie St, Sydney NSW 2000 **Phone:** 61 2 8239 3300 **Fax:** 61 2 8239 3333 **Email:** optimal@optimalasia.com

TOKYO: KS Building 10th Floor, 2-9 Minami Aoyama 6-chome, Minato-ku, Tokyo 107-0062 **Phone:** 81 3 5774 6507 **Fax:** 81 3 5774 6508

DISCLAIMER:

This Material is for your private information and we are not soliciting any action based upon it. Opinions expressed are our opinions only. The material is based upon information, which we consider reliable, but we do not represent that it is accurate or should not be relied upon as such. Past performance is not an indication of future performance. This material is not intended for distribution in Japan or for Japanese domiciled entities.

Recent 3 month Fund Exposure

% of NAV in	Nov 09	Dec 09	Jan 10
Long Stock Position	89.76	84.49	93.51
Index Futures	-	-	-
Net Exposure	89.76	84.49	93.51

Optimal FUND MANAGEMENT

Should you wish to make an investment or further enquiry about the Optimal Japan Absolute Long Fund, please see our website – www.optimalasia.com or contact us at – optimal@optimalasia.com

Position Concentration

	Top 5	Top 10
Longs	30.32%	47.55%
Total no. positions	31	

Top Five Positions

Nippon Telegraph & Telephone Corp
Mitsui & Co Ltd
Toyota Motor Corp

Mitsui Trust Holdings Inc
Mitsubishi Estate Co Ltd

Winners

Elpida Memory Inc

Sony Corp
Nippon Telegraph & Telephone Corp
Mitsui Trust Holdings Inc
All Nippon Airways Co Ltd

Losers

Toyota Motor Corp

Bridgestone Corp
Nippon Steel Corp

Kirin Brewery Co Ltd
Gulliver International Co

Sector Exposure as at 29 January 2010

	Longs	Shorts		Longs	Shorts
Materials	9.23%		Consumer. Non Disc	3.29%	
Industrials	17.35%		Consumer Disc	31.35%	
Technology	6.59%		Telecom	6.90%	
Financials	18.80%		Utilities	-	
Energy	-				

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 Monthly Returns in USD (before Performance Fees) %

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	6.66	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	-1.51	3.73	1.48	1.94	9.14
2007	1.50	3.69	-1.88	0.33	1.71	1.49	1.27	-4.97	2.18	-1.04	-5.37	-6.57	-7.97
2008	-6.00	2.60	0.15	4.21	1.40	-9.57	-3.85	-7.26	-5.49	-5.14	-4.01	8.78	-22.95
2009	-5.28	-11.56	3.78	4.75	9.49	2.12	3.11	4.76	-3.58	-2.26	-2.78	-0.38	0.38
2010	2.58												2.58