

Monthly Performance % - as at 31 January 2012

	NAV	January	YTD	AUM
Offshore Feeder	US\$11.24	2.84%	2.84%	US\$15M
Topix - <i>Topix Return is in USD unbedged using WM London 4pm close</i>		4.60%	4.60%	

Japan welcomed in the new year with a “risk-on” month that saw the Topix index rise by 3.7% in January. Contrary to the commonly held view that Japan usually starts off the year strongly, this was the best start to the year since January 1998’s 8.3% leap. It left the index still 17% lower than a year earlier however, and unsurprisingly, last year’s best sectors were January’s worst while 2011’s dogs (brokers and insurers) had a blinder. Early days yet, but the increased dispersion in sector and stock returns is welcomed by active managers and hopefully will persist.

Our performance suffered as we had no exposure in brokers, insurers, machinery or construction (the top four sectors in January) while retail and telecom – where we are well represented – both lagged the market.

We are currently in the midst of Q3 company earnings reporting season “hell”. We suspect that this whole process adds very little to the sum of anyone’s knowledge, but it is here to stay and can’t be totally ignored – no matter how much one would like to. The impression we have so far is that companies in many industries – especially manufacturers – are seeing the disruptions of this year as an opportune time to write down assets (inventory) and pave the way for a large increase in profits for FY2012. Stock prices are still moving on quarterly announcements in some cases, but revisions down for the year ending March 2012 are having little effect as the better sentiment in equity markets is leading to more optimism for the year ahead.

As the US economic data continues to impress, auto analysts are becoming more optimistic about US car demand and the Japanese makers’ prospects for 2012 and beyond. Toyota and Honda have both lagged the market significantly over the past two calendar years but are both up close to 20% this year as confidence in the demand outlook and their line-up and delivery prospects rises. Even quite bullish analyst forecasts for Toyota’s operating profits are still a mere fraction of what they achieved in the strong years of 2006 & 2007. In FY2006, Toyota’s Operating Profits were Y2, 239bn which on revenue of over Y24tn represented a profit margin of 9.3%. The following year, sales peaked at almost Y26.5tn and Operating Profits reached Y2,270bn – an 8.6% margin. This year (to March 2012), consensus estimates show Toyota reaching OP

of Y308bn which will rise to Y805bn in FY12 (ending March 2013). On estimated revenue of Y20.2tn, this gets Toyota’s OP margin back to just 4%. A good part of this is the decline in overall auto sales in the US and the change in profitability of the type of vehicle Toyota sold. An equally important factor behind the decline in profit margins is of course the strong Yen. In FY2006 when the OP margin peaked, the average Yen/Dollar rate was Y117 whereas the average over the past year has been Y79. More Americans buying more Toyotas will be a very welcome development for the company, but some Yen weakness – especially vis-à-vis the USD and the Korean Won – would really get profits soaring. We have owned Nissan in the portfolio for some time and recently took small starting positions in both Honda and Toyota and will look to increase these.

Much has been made of Japan’s trade balance falling into deficit in recent months (the past 5 to be exact) and a strong Yen does not help this either. The main reason however has been the enormous rise in fuel imports (oil, gas and coal) since the Fukushima nuclear reactor disaster and the subsequent closure of other reactors for safety checks and maintenance. Our bet is that 2012 will see opinion soften towards nuclear energy and many reactors will come back on line and reduce the demand for hydrocarbons. Barring a further jump in the Yen, this will see the trade account go back to surplus and add to (rather than detract from) the already significant current account surplus. Another long-term headwind for Japan has been price deflation, but this too has been easing and on certain measures, Japan is back in (very modest) inflation. The Yen’s level is of considerable significance in this area as well, but it would seem too much to hope for international support for the Bank of Japan to weaken the Yen. That will more likely have to rely on market forces.

Finally, we are watching the rise in international lending by Japanese banks with great interest. Loans to overseas borrowers by the big three city banks have been rising strongly and now account for over 20% of total loans in the case of MUFG (which we own). There are clear opportunities for Japanese banks – flush with deposits and strong capital adequacy – and it is encouraging to see them taking advantage of their privileged position in a world where developed world banks are still shrinking.

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Recent 3 month Fund Exposure

% of NAV in	Nov 11	Dec 11	Jan 12
Long Stock Positions	85.88	91.79	91.36
Index Futures	-	-	-
Net Exposure	85.88	91.79	91.36

Optimal FUND MANAGEMENT

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

Position Concentration

	Top 5	Top 10
Longs	24.41%	44.45%
Total no. of positions	33	

Top Five Positions

Asahi Kasei Corp
 Aeon Co Ltd
 JS Group Corp
 Hitachi Ltd
 Inpex Corporation

Winners

JS Group Corp
 Inpex Corp
 Don Quijote Co Ltd
 Mitsubishi UFJ Financial Group Inc
 Itochu Corp

Losers

Skymark Airlines Inc
 Aeon Co Ltd
 Yamada Denki Co Ltd
 Canon Inc
 Benesse Holdings Inc

Sector Exposure as at 31 January 2012

	Longs		Longs
Consumer Discretionary	23.52%	Industrials	13.29%
Consumer Non-Discretionary	5.13%	Information Technology	10.03%
Energy	4.29%	Materials	12.94%
Financials	16.56%	Telecommunications	5.60%

Historical Returns- 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	Topix* YTD
2004									-1.60	-1.32	6.18	2.52	5.70	8.16
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	24.59
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	0.94
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	-6.37
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	-28.24
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	2.85
2010	2.58	0.19	4.19	1.88	-8.25	-3.15	3.36	-2.39	5.77	3.79	0.36	8.26	16.65	13.67
2011	1.31	3.89	-9.20	1.72	-0.51	1.02	3.69	-6.40	-3.98	2.70	-4.91	0.83	-10.34	-14.55
2012	2.84												2.84	4.60

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