

Monthly Report to Shareholders of the Optimal Japan Absolute Long Fund 13th December, 2005

	OJAL NAV*	Performance
30 November 2005	\$12.38	3.25%

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

The 4th Quarter of calendar year 2006 has been good for a number of equity markets but amongst the larger ones, Japan's performance must surely rank first. As of yesterday's close, the Topix index return is up 14.5% and takes the YTD return to over 40%. With the exception of the ugly TMT year of 1999, this would be Japan's best return from equities since 1986. Most fund managers who ran money in Japan in 1986 have long since moved on to other markets (or retired) but we remember it with a good deal of nostalgia and hope lessons learned then might even be of use today.

You might recall early in 2005, we targeted a Topix index level of 1700 as a realistic goal to be reached by the second half of 2006. Extrapolating the rate of increase in the Topix index seen in the first twelve days of December, we are on track to hit 1700 by Christmas Eve. Even assuming it does not reach 1700 by Christmas, it will take a mere 5% move to get there so what do we do then? On current estimated EPS of Y80 for the Topix index constituents for the year to March 2007, the market would be trading on 21 times PER or a 4.7% earnings yield. Relative to the yield on the 10 year JGB of 1.6% and relative to Tokyo commercial property yields of 4-4.5%, this is reasonably attractive. The real issue is what happens to earnings in the years ahead. If Japanese companies can continue to improve profitability and returns on assets, there is no reason why the market should stop at 1700. With the economic outlook improving and asset deflation behind us, domestic investors are showing tentative signs that they are willing to reconsider buying equities for the first time since most Japanese fund managers wore shorts. We continue to feel that this process would be accelerated if Japanese companies paid out more of the profits to shareholders by way of dividends. It is quite possible to refute this theory however on the basis that it behoves Japanese corporates to reinvest the majority of their profits in the business as returns on equity rise to (and above) 10% in an environment when competing returns are modest at best. Time will tell, but for now, it is foreigners, Japanese investment trusts and individuals (on margin) who remain the buyers and Japan's pension fund managers the sellers.

What is clear is that we are in a market when earnings growth is rewarded with rising share prices whilst earnings disappointments yield poor share price returns. In the half year to September 2005, the sectors with the biggest profit gains also saw the biggest rise in stock prices – and vice-versa. Whilst Topix rose 19.46% in H1, the steel (Operating Profits +62% and prices +50%), mining (OP +62%, +49%) and Oil & Coal (61%, 38%) sectors soared. Airlines, Utilities, Electricals (how the mighty have fallen) and Paper all showed poor returns in both profits and prices. For the moment, the former group still trade on cheaper multiples than the latter, so we will continue to look for outperformance in line with profits growth.

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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 for related information and we encourage you to contact us through the web-site.

Month-end investments (as % NAV):

Equity Long: 77.73%

Net exposure: 77.73%

Fund size: US\$ 67.5 mil

Total number of positions: 28

Top 5 positions:

	% of NAV
Mitsubishi Co	5.19%
Mitsui OSK	5.13%
Mitsui Fudosan	4.69%
Sumitomo Metal	4.60%
Kubota Co	4.33%
Total	23.94%

Best Performers: Mitsui Toyota Motor, Ushio, Sumitomo Metal Mining, Mizuho FG

Worst Performers: Nippon Steel, Chintai Jutaku News, Ishihara Sangyo

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		17.12

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Level 32, The Chifley Tower
2 Chifley Square
Sydney NSW 2000
Phone: 61 2 8239 3300
Fax: 61 2 8239 3333
optimal@optimalasia.com

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