

Optimal FUND MANAGEMENT

Monthly Report to Shareholders of the Optimal Japan Absolute Long Fund November 10th, 2006

	OJAL NAV*	Performance
31 October 2006	\$14.19	+3.73 %

**The NAV shown above is after expenses and management fees but before any performance fees. The Fund return may thus not be the same as the return of a discrete investment that might be subject to performance fees through equalisation.*

Please note that the Fund's PPM is available on the Optimal website (www.optimalasia.com)

The main corporate news in October continues to be the tighter controls to be imposed on the consumer finance companies' lending rates. This sector – of which there are four main listed companies – has long fascinated foreign investors who have marvelled at the juicy profits and returns on equity that have been generated. It was a constant source of amazement that the large banks would not try and muscle into what were obviously very high margin businesses. In recent years, a number of the large Japanese banks have formed joint ventures with the big consumer loan companies but one always had a strong sense that they never felt comfortable in this area. Foreign banks were not quite as circumspect with at least one major banking group taking over one of the larger (unlisted) consumer finance companies. Recent court rulings in Japan have imposed restrictions on the rates at which the finance companies can lend and the finance companies are setting aside reserves to make “compensation” payments to aggrieved borrowers who have been overcharged. The trouble we have always felt when trying to understand these companies was the opacity of the laws and guidelines that governed their operations. It also beggared belief that the massive returns generated could go unchallenged either by increased competition or vigilante politicians.

Finally, our scepticism seems to have been justified – although we must add that the our funds have not profited from short positions in these stocks (sadly).

To illustrate how rough it has been, Takefuji has seen earnings per share fall from Y525 in FY03 to Y488 in FY04 to Y333 last year and is expecting a loss of Y743 in the current year to 3/07. This year alone, the shares have more than halved from their high on January 5th of Y8470 to Y4100 yesterday – despite boasting a stated book value per share at last balance date of over Y6900. It is an interesting situation when a large company (with a market capitalisation still in excess of US\$5bn) trades at only 0.6x book value and normally one which would peak our interest at the very least. With maximum loan rates being slashed from 28% to between 18-22% however, the operational gearing has dramatically deteriorated and we do not believe that there is sufficient clarity to start bottom fishing.

There was remarkably little news (that we noticed) during the month other than the constant flow of announcements from companies releasing their results for the half-year to September. Recurring profits are up between 10-13% year-on-year but still Japanese company management insist on keeping full year estimates to 3-5% growth. We will, of course, find out in due course, but our expectation is that share prices will be considerably higher by the time the truth becomes evident.

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Month-end investments (as % NAV):

Equity Long: 94.26%

Net exposure: 94.26%

Fund size: US\$ 227 mil

Total number of positions: 34

Top 5 positions:

	% of NAV
Tokyu Corp	5.34 %
Toyota Motor Corp	5.23 %
JFE Holdings	4.80 %
Tokyo Tatemono Co	4.46%
Sumitomo Trust Banking Co	4.40 %
Total	24.23%

Best Performers: Makino Milling, Suzuki Motor, Toyota Motor

Worst Performers: Tokyu Corp, Fujitsu, Ushio

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	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			5.50

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