Report to Shareholders of the Optimal Japan Absolute Long Fund – *September 2010*

Optimal FUND MANAGEMENT

Performance % - *as at 30 September 2010*

	NAV	September	Qtr	YTD	Asset size
Offshore Feeder	US$10.81	5.77%	6.71%	3.44%	US$150M
Topix (*Return is in USD unhedged using WM London 4pm close)*		3.62%	4.43%	1.85%	

** 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.*

After reaching a 2010 low at the end of August, the Japanese Topix index had a strong month in September and closed up 3.1%. Had it not been for another dismal performance from the banks sector (-2.4%), the Topix return would have been somewhat closer to that of the Nikkei index which rose by 6.2% in September. We have written before about the pesky Nikkei index and its unsuitability as a representation of the broader market but the fact is electricals (exporters) have a greater weight in the Nikkei while banks have a greater weight in the Topix. After twenty years of decline, the Banks' sub-index weight in the Topix is now only 9%, but given that the combined weight of the largest five banks represents less than 1% of the Nikkei index, a lot of the discrepancy in the returns from these two indices can be explained by the performance of banks. It doesn't necessarily follow that bad performance from the banks means Topix underperforms the Nikkei however, as the year-to-date returns to end September demonstrate. Despite the banks being down 13.6% in the period, the Topix is down 8.6% while the Nikkei return is worse - being down 11.2%. The Nikkei's double digit decline is due in no small part to the 32% fall in the share price of Fast Retailing which was the largest component of the 225 names in the index. But enough of that.

In financial markets, the biggest event of the quarter was the move by the Japanese authorities to intervene in the foreign exchange market by selling Yen. On September 15th – the day after Naoto Kan defeated a challenge from Ichiro Ozawa for the position of leader of the DPJ - the market was shocked by a sudden burst of Yen selling (USD buying) by the Bank of Japan acting on Ministry of Finance instructions.

On the previous day, the Yen had risen to the Y82/$ level, marking close to 10% appreciation against the dollar during the quarter. Having been out of the currency markets for over six years, this action came as a shock and had the immediate and dramatic effect of weakening the Yen and boosting Japanese equities. Lack of follow through, however, has seen the Yen drift higher and equities drift lower since then, but it was a welcome sign that at least the Japanese government is concerned by the deflationary effect of a much stronger Yen at a time when all of their major trading partners are happy to see their currencies weaken.

In general, the direction of the Japanese market continues to be a tug-of-war between those with a positive view of equities based on earnings and valuations and those holding a negative view of an economy that struggles with ongoing deflation. Other subjects that affect investors' views on Japan include the gradual improvement in aspects of corporate governance (such as the increasing number of independent directors appointed to boards) and the difficulty of attracting attention when competing with the razzle-dazzle of faster growing countries in the Asian region. There is little doubt that the short-term trading segment of the investment community has a default position of hedging long positions in high beta Asian equities with short positions in Japan. To date, this has not hurt them for long, or to any great extent.

Our view is of a more positive hue, and yet we often find it frustrating that there appears so little personal interest felt by senior management in the share price of their companies. Were that not the case, there would be far fewer companies issuing new equity when balance sheets are strong and at share prices below book value. It is a fact that banks continue to exert a great influence over their borrower companies and are always pushing them to bolster their balance sheets with an extra buffer of fresh equity. If Japanese managers' prospects for a happy retirement were more dependent on the value of their investment in shares in their own companies, the stranglehold of the banks over balance sheets might not go unchallenged as often seems to be the case. Unfortunately, it has been wise to assume that most companies that conduct IR activity overseas are doing so because they wish to issue more equity and that despite the attractions of their business

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

prospects, this factor will have a greater impact (downwards) on the share price. The companies that seem to value their share price are invariably ones where the founder/owner still has a large personal stake in the equity. The banks need to accept that it is more valuable to them that they help their corporate customers achieve long-term growth than having the "comfort" of knowing that there is excess equity in the customer's business. When that happens, corporate Japan's collective RoE will no longer remain lower than other countries and a significant re-rating of the stock market will occur.

Until we reach that point, we will concentrate our efforts to find companies that care about their share price and, by extension, their investors. The good news is that they are more numerous than they once were.

Recent 3 month Fund Exposure

% of NAV in	July 10	Aug 10	Sept 10
Long Stock Position	92.51	92.12	84.90
Index Futures	-	-	-
Net Exposure	92.51	92.12	84.90

Performance Statistics

Last 12 Months	-2.08%
3 Yr Annual Average Return	-11.20%
5 Yr Annual Average Return	-2.20%
Average Annual Return Since Inception	1.29%

Position Concentration

	Top 5	Top 10
Longs	27.88%	46.93%
Shorts	-	-
Total no. positions	34	

Top Five Positions

Mitsubishi Estate Co Ltd
Chuo Mitsui Trust Holdings Inc
Hitachi Ltd
JS Group Corp
FUJIFILM Holdings Corp

Winners

Hitachi Ltd
Mitsubishi Estate Co Ltd
Daihatsu Motor Co Ltd
Sumitomo Realty & Development
Nippon Electric Glass Co Ltd

Losers

Chuo Mitsui Trust Holdings Inc
Mizuho Financial Group Inc
Ryohin Keikaku Co Ltd
T&D Holdings Inc
Nippon Paper Group Inc

Sector Exposure *as at 30 September, 2010*

	Longs	Shorts	Total
Materials	3.51%	-	3.51%
Industrials	21.23%	-	21.23%
Financials	23.80%	-	23.80%
Energy	-	-	-
Consumer Non-Disc	5.37%	-	5.37%
Consumer Disc	13.82%	-	13.82%
Utilities	-	-	-
Telecom	4.59%	-	4.59%
Technology	12.57%	-	12.57%
Total Equity	84.90%	-	84.90%
Index Futures	-	-	-
Net Exposure	84.90%	-	84.90%

September Qtr Sector Performance – P&L

	Longs	Shorts	Total
Materials	-0.53%	-	-0.53%
Industrials	0.15%	-	0.15%
Financials	-0.63%	-	-0.63%
Telecom	0.05%	-	0.05%
Consumer Non-Disc	0.25%	-	0.25%
Consumer Disc	0.59%	-	0.59%
Utilities	-	-	-
Technology	0.70%	-	0.70%
Index Futures	-	-	-
FX and Others	-	-	6.12%
Total	0.59%	-	6.71%

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	Topix [1] YTD
2004									-1.6	-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				3.44	1.85

[1] *Topix Return is in USD unhedged using WM London 4pm close*

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