

## Monthly Report to Unitholders of the Optimal Japan Trust 10<sup>th</sup> March, 2006

Date	NAV	Monthly % Return*
28 February 2006	A\$ 16.88	+0.42%

\* After all fees

\* NAV is ex-distribution of **A\$ 1.4218 (for Yr to 6/05)** A\$0.4713 (for Yr to 6/04) A\$ 0.8983 (for Yr to 6/02) A\$0.8989 (for Yr to 6/01) and A\$ 1.4158 (for Yr to 6/00)

\* Returns are based on the redemption price of the initial series

*Important: The Optimal Japan Fund and Optimal Japan Trust are not accepting new investments. The administrator (HSBC Institutional Trust Services) will only accept applications for investment from those with agreements with the manager.*

The aftershocks from the Livedoor collapse have continued through February with internet stocks (and other asset poor/concept rich companies) selling off sharply. Although the Topix index fell almost 3%, the Hercules and Mothers indices were down 13% & 14% respectively and have fallen by a third since their highs on January 16<sup>th</sup>. In CY2005, the Hercules index rose 76% and Mothers was up 48% so one is reminded of the oldie “if you can’t take the heat, get out of the kitchen”. We never made it to the kitchen and missed out on the upside last year as we concentrated our attention in other parts of the market. Thanks to that, we also missed out on the damage wrought last month. Whether the market fell because of Livedoor, or it was a case that Livedoor’s problems coincided with a bit of buyers’ fatigue is hard to judge, but it did not strike us as odd that the market ran into selling above 1700 on Topix.

Economic data remains highly supportive of an optimistic outlook for the year ahead. Tokyo office vacancies have fallen below 4% to the lowest level since 2001. In mid 2003, this had reached 8.5% so the improvement has been strong. We are also hearing very persuasive anecdotal evidence that rents are rising by hefty margins in central locations and these will lead to revaluation of assets in many real estate companies. Bond yields have risen, near term futures for three month Yen are reflecting higher interest rates and the Bank of Japan has termed the recent private consumption data as solid.

Two of our Sydney team made separate trips to Tokyo in February and were both struck by the greater sense of optimism at company visits. This willingness to expand again is reflected by national bank lending figures which turned positive year-on-year in Q4 2005 for the first time since 1996. After more than a decade of balance sheet repair, corporate Japan is now feeling ready to spread its wings and the resultant capital spending will support domestic demand. Visits to two major equipment manufacturers confirmed that they were running their operations at 100% utilisation rates and were hoping to boost output with modest additions to plant. Interestingly, their margins were higher overseas than in Japan – a situation they ascribed to excess competition in Japan whereas in foreign markets, their field is dominated by three players. It is a familiar story and one that goes a long way to explaining the persistently low returns on capital seen in most domestic industries such as retail, construction and food.

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# Optimal FUND MANAGEMENT

The Trust's return was helped in no small way by a successful short position in the Topix futures that we opened on February 2<sup>nd</sup> and closed on the 17<sup>th</sup>. For the Optimal Japan Trust, the resulting profit contributed almost 75bps and made the difference between a negative and positive return for the month.

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](http://www.optimalasia.com) for related information and we encourage you to contact us through the web-site.

Positive contributors (long) Nippon Steel, Kubota, Toyota Motor, JFE  
(short) Funai Electric, Murata, Goldcrest, Shiseido

Negative contributors (long) Sumitomo Trust & Banking, Tokyu Corp., Fujitsu  
(short) Mitsubishi UFJ, Oji Paper, Eisai

## Major Positions

Sumitomo Metal Mining, Sumitomo Trust & Banking, Kubota, Sumitomo Co, Mitsubishi Co

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# Optimal FUND MANAGEMENT

Return Snapshot	
Period	%(AUD)
Year to Date Return	2.24
Return since inception Inception 20 Dec, 1999	119.86
Fund size at 28 Feb 06	AUD 64.6 mil

Portfolio Composition at Month End			
% of NAV	Dec 05	Jan 06	Feb 06
Long Stock Position	78.89	79.40	76.16
Short Stock Position	(22.13)	(16.68)	(20.02)
Index Futures	(10.50)	(9.05)	
Equity Derivatives			
Net Exposure	46.26	53.67	56.14

## Historical Returns

Below we provide a table detailing the monthly returns of the Fund since its inception in December 1999. The returns are of the Trust's Initial Series

Optimal Japan Trust Net Monthly Returns in AUD													
Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
1999												0.58*	0.58
2000	-0.32	12.76	8.99	-1.53	2.45	11.82	-9.05	4.02	-0.37	0.90	-0.18	-3.86	26.63
2001	-2.34	3.13	1.36	8.46	-2.14	3.96	-2.88	1.49	-3.58	1.77	-3.89	-5.46	-0.25
2002	1.10	1.47	2.07	-0.26	7.2	-2.9	-1.43	-1.47	2.04	-4.47	-3.65	-0.42	-0.59
2003	1.80	1.98	0.41	-0.20	2.55	3.97	1.91	5.90	3.81	3.58	-1.73	3.02	30.43
2004	-0.33	1.22	7.01	0.23	-1.20	3.67	-2.26	4.03	0.82	-1.55	1.65	1.92	15.95
2005	2.83	2.05	0.0	-0.13	1.04	1.37	2.38	4.15	6.71	1.31	2.39	4.30	30.03
2006	1.82	0.42											2.24

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