

Monthly Performance % - as at 29 January 2010

NAV	January	YTD	Asset size
A\$10.44	1.95%	-3.15%	A\$41M

Nothing occurred in January that would make one want to change one's view of the opportunities in equity markets. Generally speaking, stock prices rose in the first half of the month and then fell away to close the month lower. Europe and the eastern US had dreadful winter storms and Haiti suffered a devastating earthquake. All in all, the omens were not good.

Markets in all parts of the world now take close note of events in China. Daily equity market movements are still highly correlated to those of Wall Street, but most investment strategies incorporate a view on China in a way that was barely dreamed of a decade or so ago. We invest in Chinese companies and spend a lot of time assessing the risks and opportunities there, but generally find more to admire (economically speaking) than to deride. A sizeable minority of investors – or at least commentators – believe that the Chinese economy is a bubble waiting to be pricked and that the mistakes made by the Japanese during the '80s and early '90s are being repeated by the Chinese with inevitably ugly consequences. They might be right, but we are not so bearish on China. For one thing, the Chinese are not ignorant of the imbalances that Japan created, and are not as indifferent to the cost of capital as Japanese companies were in the 1980s. They may not be working to maximise their returns on capital at all times, but investors are also able to decide which companies are worth owning shares in and will generally avoid the chronic wasters of capital.

Unlike China, events in Japan do not feature highly in forming global investment strategies. It is a market that is neither loved, nor reviled - merely ignored. We think that this situation is hard to fathom and believe that the times are changing in Tokyo.

In the 1990's, the weakened state of the Japanese banks meant that borrowing became more difficult for most Japanese companies. As a result, companies needed to improve their returns (and cash flow) to justify loans or raise fresh equity from the market. Returns on capital bottomed in 1995 and have been on an improving trend since then until disrupted severely by the 2008-2009 economic crisis. Coming out of the economic slump, we expect that returns could be heading higher on a sustained basis through a reduction in capex as Japanese companies look to lower costs and manage their businesses in a more efficient manner. Cost cutting has been dramatic in the past 18-24 months and a growing number of company forecasts show operating profits recovering

to the March 2008 peak levels in the year ending March 2012 despite overall sales forecast being lower. Margins are recovering rapidly as costs are cut and management decisions improved.

The greatest potential for surprise lies in the area of government policy. Many observers have been disappointed by political developments – or lack thereof – since Mr Hatoyama's DPJ won government last year. I am not sure whether they are going to make a success of their time in office, but I am more confident that Japan has a greater chance of success with them in power than it would have with the moribund LDP in charge. They face very real and very large problems – and no one is unaware of them. There needs to be wholesale, root-and-branch reform of the system of taxation and the provision of pensions. Too much of the tax burden falls on relatively few companies – usually the larger, listed ones - and on the declining number of salaried workers supporting an increasing population of retirees. Japan needs to introduce an identification system (tax file number, or social security card) to record incomes and taxation and to remove the current incentive for people to create small private companies through which they can push expenses and lower their taxable income.

These schemes are not easy to design and implement, but the need is obvious. Japan has a very low tax take because of these inefficiencies and the system is increasingly unfair on the salaried and those willing to be profitable.

We intend to concentrate our research on these areas of public policy and will write again on the issues in the months ahead.

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Recent 3 month Fund Exposure

% of NAV in	Nov 09	Dec 09	Jan 10
Long Stock Position	81.15	74.05	86.24
Short Stock Position	-13.84	-10.89	-5.56
Index Futures	-18.73	-19.14	-23.88
Equity Derivatives			
Net Exposure	48.58	44.02	56.80

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Position Concentration

	Top 5	Top 10
Longs	29.03%	45.64%
Shorts	-5.56%	-
Total no. positions	36	

Top Five Positions

Mitsui & Co Ltd
Nippon Telegraph & Telephone Corp
Toyota Motor Corp
Mitsui Trust Holdings Inc
Mitsubishi Estate Co Ltd

Winners

Nikkei Index Future (Short)
Elpida Memory Inc
Sony Corp
Nippon Telegraph & Telephone Corp
Hitachi Construction Machinery Co Ltd

Losers

Toyota Motor Corp
Yahoo! Japan Corp (Short)
Nippon Steel Corp
Gulliver International Co
Kirin Brewery Co Ltd

Sector Exposure as at 29 January 2010

	Longs	Shorts	Net
Materials	6.89%	-	6.89%
Industrials	15.12%	-0.93%	14.18%
Technology	6.66%	-1.21%	5.45%
Financials	18.58%	-0.79%	17.80%
Health Care	-	-0.88%	-0.88%

	Longs	Shorts	Net
Consumer Non Disc	3.24%	-	3.24%
Consumer Disc	29.73%	-	29.73%
Telecommunication	6.03%	-1.75%	4.28%
Futures	-	-23.88%	-23.88%

Historical Returns - Distributions Reinvested

Optimal Japan Trust Net Monthly Returns in AUD %

The table below outlines the monthly returns of the Fund's Series 1 since its inception in August 2002.

Year to June	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	YTD
2002													
2003			1.68	-4.38	-3.66	-0.42	1.80	1.98	0.41	-0.10	2.55	3.48	3.06
2004	1.54	5.20	3.86	3.55	-1.67	3.06	-0.33	1.24	7.11	0.15	-1.14	3.93	29.47
2005	-2.14	4.01	0.23	-1.21	1.30	1.51	2.74	2.02	0.07	-0.14	0.99	1.47	11.24
2006	1.81	3.68	6.81	1.36	2.41	4.38	1.82	0.43	3.86	0.35	-4.05	0.18	25.14
2007	-0.79	1.43	0.13	2.10	0.77	2.49	1.99	0.55	-1.03	1.35	3.45	2.28	15.66
2008	-0.87	-6.98	1.88	0.35	-6.70	-4.69	-6.67	2.21	-0.67	6.20	1.34	-5.91	-19.57
2009	-0.83	-5.34	-0.09	-0.44	-6.38	3.22	-1.74	-2.15	1.91	0.47	0.84	-0.46	-10.84
2010	0.28	2.59	-4.87	-0.66	-5.15	3.02	1.95						-3.15

The table below outlines the monthly returns of the Fund's Initial Series since its inception in December 1999.

2000						0.58	-0.32	12.76	8.99	-1.53	2.45	11.82	39.0
2001	-9.05	4.02	-0.37	0.90	-0.18	-3.86	-2.34	3.13	1.36	8.47	-2.14	3.96	2.82
2002	-2.88	1.49	-3.58	1.77	-3.89	-5.46	1.10	1.47	2.07	-0.26	7.13	2.92	-4.55
2003	-1.46	-1.39	2.04	-4.47	-3.65	-0.44	1.80	1.98	0.41	-0.20	2.65	3.97	0.89
2004	1.91	5.90	3.81	3.58	-1.73	3.02	-0.33	1.22	7.01	0.23	-1.20	3.95	30.56
2005	-2.26	4.03	0.82	-1.55	1.65	1.92	2.83	2.05	0.00	-0.14	1.04	1.37	12.22
2006	2.38	4.15	6.71	1.31	2.39	4.30	1.82	0.42	3.79	0.34	-4.04	0.24	26.09
2007	-0.77	1.46	0.13	2.72	0.99	2.62	1.96	0.58	-0.99	1.35	3.47	2.23	16.82
2008	-0.89	-6.99	1.85	0.40	-6.68	-4.73	-6.62	2.17	-0.71	6.19	1.42	-5.97	-19.60
2009	-0.78	-5.37	-0.08	-0.42	-6.38	3.23	-1.74	-2.21	1.90	0.53	0.79	-0.44	-10.82
2010	0.26	2.54	-4.79	-0.72	-5.15	3.05	1.94						-3.16

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