

Monthly Performance % - as at 31st January 2011

NAV	January	YTD	Strategy AUM
A\$11.33	3.38%	11.41%	US\$56M

As fears of deflation recede in developed economies, and inflationary pressures grow in the faster growing Asian economies, Japan has benefited from improving fundamentals and sentiment. Since early November last year, Japan's Topix index has beaten the MSCI Asia (ex-Japan) index by almost 20%, but before one leaps to a premature conclusion - the usual one being "sell Japan" - it is worth looking at just how much, and for how long, Asian markets have been outpacing Japan. In the ten years since early 2001, Asia has outperformed Japanese equities three-fold and unsurprisingly trades on a multiple of book value more than twice that of Japan's meagre 1.0x.

Given the persistence of deflation in Japan since the mid-90s, and the dreary cocktail of either inaction or misguided policy from Japan's *many* governments, the Japan "discount" is understandable. We think the reasons for the discount are receding and while bullish on Asian investment opportunities, suggest it is right to be adding – or perhaps initiating – an investment in Japanese equities.

In no particular order of importance, we would offer the following points as areas of support to this view:

- Leverage to global growth
- Profits growth
- M&A on the increase
- Government policy (tax; inflation)
- Under-owned (by locals and foreigners)
- Valuations

Like many countries in the region, wholesale prices in Japan are rising but more interestingly, consumer prices have stopped falling. In the inflation mix one has a great variety of price levels that ultimately reflect demand and supply. Processed food prices are up, as are steel, petroleum and metals, but there is also discernible easing of falling prices in autos, general machinery, electronic products and IT equipment. The latter are sectors that have seen consistent downward price pressures over the past 15 years – competing as they do with aggressive companies in the trade surplus manufacturing countries such as China, Taiwan and Korea. Margins are habitually razor thin in many of these sectors, but our research shows that weaker players are dropping out

or being subsumed by stronger ones and supply is no longer increasing as it had in past years.

In our portfolio, we have been adding new positions in the domestic sectors and now have well over half of our holdings in stocks that depend in the main on domestic demand. We have also added a number of small cap stocks, as these also offer an inexpensive way to play improvement in the Japanese economy. It is not all domestic of course, and we continue to hold a large position in Hitachi – despite it having been a star performer over the past year. NTT is another of our biggest holdings and if it was a footballer, you would be cutting its match payment and demanding more. The shares have done next to nothing for the past year, but their recent Q3 results were encouraging and it is dirt cheap and seeing growth. It is also buying back shares and warrants a place in our starting line-up.

Last year we saw a good start from Japan and then suffered a dreadful six months through to November. Global conditions are different now, and we can have much more confidence that the rally to date is not the best we can expect for 2011.

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Recent 3 month Fund Exposure

% of NAV in	Nov 10	Dec 10	Jan 11
Long Stock Position	85.13	86.52	86.41
Short Stock Position	-5.77	-6.82	-10.83
Index Futures	-32.70	-31.16	-39.63
Equity Derivatives	-	-	-
Net Exposure	46.66	48.54	35.95

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Position Concentration

	Top 5	Top 10
Longs	25.76%	43.15%
Shorts	-9.34%	-
Total no. positions	42	

Top Five Positions

Hitachi Ltd
 JS Group Corp
 Mitsubishi Estate Co Ltd
 Nippon Telegraph & Telephone Corp
 Sumitomo Realty & Development Co Ltd

Winners

Teijin Ltd
 Itochu Corp
 Zeon Corp
 Hitachi Ltd
 Fanuc Ltd

Losers

NABTESCO Corp (Short)
 Kirin Holdings Co Ltd
 Mitsui Chemicals Inc
 Mitsubishi Materials Corp
 Toshiba Corp

Sector Exposure as at 31 January 2011

	Longs	Shorts	Net
Materials	14.60%	-2.01%	12.59%
Industrials	17.27%	-5.84%	11.43%
Technology	11.09%	-	11.09%
Financials	18.74%	-	18.74%
Health Care	-	-1.49%	-1.49%

	Longs	Shorts	Net
Consumer Non Disc	6.15%	-	6.15%
Consumer Disc	13.61%	-1.49%	12.12%
Telecommunication	4.95%	-	4.95%
Futures	-	-39.63%	-39.63%
Energy	-	-	-

Performance Contribution

	Longs	Shorts	Futures	Others	FX Forwards	Total
January 2011	2.87%	0.18%	0.02%	0.31%	NA	3.38%

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	-1.53	5.74	2.76	-5.91	-3.24	-5.66
2011	0.49	-1.96	2.89	0.97	1.34	3.89	3.38						11.41

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	-1.54	5.81	2.70	-5.94	-3.25	-5.71
2011	0.47	-1.86	2.84	1.01	1.36	3.86	3.37						11.46

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