

**Monthly Report to Unitholders of the  
Optimal Japan Trust**

10 July, 2000

<b>DATE</b>	<b>NAV</b>	<b>Monthly % Return*</b>
30/6/00	A\$13.899	11.82

\* After all fees

The Japanese indices' high correlation with the US market has been in stark evidence this year and as NASDAQ hit bottom (at least for now) in late May -- so too did the Nikkei 225 and Topix. The rise in June has been attributable to a very different group of companies from those that propelled the Topix index to a 58% local currency gain in 1999 and led the market in the TMT-liquidity bubble that ended in March. Prominent contributors to the recent rally were non-ferrous metals, airlines, shippers, machinery, textiles and chemicals while the majority of sectors outperformed the index. Buying -- much of it domestic institutional and individual -- has been spread more broadly than the very concentrated investment approach of foreigners and mutual funds last year and in the first quarter. The Fund had a strong return in June with positive contributions from both the long and short positions pushing the NAV up by 11.82% against a Topix index (AUD) return of 1.69%.

The most significant event in June was the general election held on the 25<sup>th</sup>. Although government remains in the familiar hands of the LDP, the election was important, as it may have ushered in an era of more conventional two-party politics. The strong showing from the Liberal Party and the decline in support for the Socialists and the Komeito (a coalition partner of the LDP dependent on a Buddhist sect for members and money) means the LDP have a credible opposition to fight against. It would be no surprise if the LDP splintered further into hard-liners supported by the rural vote and urban conservatives wanting some degree of reform.

On the policy front, most commentators are agonising over whether the Bank of Japan will

raise interest rates for the first time in many years. The hawks (predicting a rate rise) cite the Q1 Tankan report on business sentiment as supportive of tighter monetary policy but others see continuing excess capacity and a weak pricing environment arguing strongly for monetary policy to remain ultra-loose. We find the latter argument more convincing, but accept the fact that political forces within the LDP will apply pressure on the BoJ for a rise - albeit a minimal one - in the discount rate. Eventually, Japanese interest rates will rise but with the corporate sector's low return on capital at present, it is very hard to see rates being pushed very far.

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# Optimal FUND MANAGEMENT

We take comfort from recent signs that domestic investors are back in the equity market and looking further afield for bargains. Liquidity in many medium and smaller cap stocks has improved of late (witness one of the Fund's holdings - Central Glass) and the Japanese investment trust industry's aggregate assets (akin to US mutual funds) have passed Y 60tn (US\$560bn) for the first time. The previous peak in assets was in 1989 although the asset mix then was heavily weighted towards equities whereas there is far more in bond and cash management funds now relative to equities. A revealing statistic has been the high correlation between changes in the Topix index and subsequent flow of funds by foreign investors in Japanese stocks. Although foreign investors used to pride themselves on their leading indicator status in the Japanese market, it would appear that they are behaving in a very mechanistic and lagging fashion. Our advice to investors is to focus more on the actions of the domestic investors this year and don't read too much into the investment moves of the non-resident.

## Performance

Positive contributors (long) Central Glass; Nippon Chemical; Keiyo; Kajima; Toshiba Tec  
(short) Goodwill; Shizuoka Bank; Nichiei  
Negative contributions (long) Sakura Bank; Kitagawa Industries  
(short) Tokyo Seimitsu

## Major Positions

### Long

Arrk; Central Glass; Kawasaki Kisen; Oki Electric; Denso; M.E.I.

### Short

Ito-Yokado; Sumitomo Bank; Toyoda Gosei

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<b>Returns Snapshot</b>	
<b>Period</b>	<b>% (AUD)</b>
<b>Year to Date Return:</b>	38.19
<b>Return since inception: *Inception 20 Dec, 1999</b>	38.99

<b>Portfolio Composition at Month End</b>			
<b>%of NAV in:</b>	April 2000	May 2000	June 2000
<b>Long Stock Position</b>	110.38	102.26	98.22
<b>Short Stock Position</b>	(27.98)	(22.11)	(27.05)
<b>Index Futures</b>	(25.31)	(23.35)	(21.12)
<b>Equity Derivatives</b>	5.68	5.14	3.74
<b>Net Exposure</b>	62.77	61.94	53.79

### ***Historical Returns***

Below we provide a table detailing the monthly returns of the Trust since its inception in December 1999.

<b>Optimal Japan Trust Net Monthly Returns in AUD</b>													
<b>Year</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>	<b>May</b>	<b>Jun</b>	<b>Jul</b>	<b>Aug</b>	<b>Sep</b>	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>YTD</b>
1999												* 0.58	0.58
2000	-0.32	12.76	8.99	-1.53	2.45	11.82							38.19

Trust Inception 20 December, 1999

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