

## Monthly Report to Unitholders of the Optimal Japan Trust

June 5th, 2002

DATE	NAV	Monthly % Return
31/05/02	A\$11.63	7.2

- After all fees
- NAV is ex-distribution of A\$ 0.8989 (for Yr to 6/01) and A\$1.4158 (for Yr to 6/00)

### Monthly return composition

	Mar 02	Apr (from Mar 29 <sup>th</sup> )	May
<b>Topix %</b>	6.77	-0.03	3.51
<b>OJF longs %</b>	7.45	2.43	12.43
<b>OJF shorts %</b>	-9.30	-3.80	-2.68

### Trailing 3 months NAV

Mar 02	Apr 02	May 02
A\$10.88	A\$10.85	A\$11.63

Japan's recovery continued with the Topix index gaining 3.5% for its fourth consecutive monthly gain to be up 8.5% for the year to date. Adding the US dollar's weakness to the mix gives a return of 15% in USD against an S& P 500 decline of 9% and Europe of around 5%. If this sounds like gloating I can confirm it is. We Japan bulls have had so little opportunity to wave our flags these past dozen years that we'll take what we can – when we can.

The lurking fear that won't go away is that we are experiencing a typical seasonal phenomenon whereby Japan's equity market performs well in the first half then runs out of puff with the onset of summer and wilts through the second half of the year. What makes 2002 any different? The first difference is that the outlook for corporate profits in the year ahead is a lot brighter than it was a year ago. The reporting season for companies with March year-ends is winding up and aggregate profits are down between 30 & 60% - depending on how you measure them. In the year to March 2003, company forecasts are for recurring profits to rise by more than 50% which would put the market on an average PER of 32 times. Some are more sceptical (for example GS strategist Kathy Matsui expects profit growth of 25% to give a market PER of 39 times) – but what is clear is that Japan's abysmally low return on assets/equity has begun to rise through a combination of shrinking assets (equity) and rising profits. From a stock pickers point of view, however, the market feels cheap. We are value investors but

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# Optimal FUND MANAGEMENT

not of the hair-shirt variety and do not seek to buy only the stocks trading on the lowest PERs. Nevertheless our long holdings trade on a weighted average PER of 20x and a PBR of 1.5x. If our aim were to construct a “cheaper” portfolio we could probably halve both of these without spending too much effort. With certain exceptions – most notably 1999 – value investing has performed better than growth in Japan and there is plenty of value there now.

A second difference about the year ahead is the flood of share buy-backs announced over the past month or so. Since the changes to the Commercial Code in October 2001, the scale and implementation rate of share buy backs has risen considerably and we would warn investors not to be overly sceptical about the effect and longevity of this sea change. As we mentioned in last month’s letter, the aggregate demand from buy backs this year should exceed the supply of stock from cross-shareholding unwinding and remove a major impediment to recovering prices.

<u>Positive contributors</u>	(long)	Nikko Cordial; NTN; Japan Energy; Marubeni; MTFG
	(short)	Shinko Electric; Nikon; Acom
<u>Negative contributors</u>	(long)	Wowow; Drake Beam Morin; Pioneer
	(short)	Meitec; Nichirei; Shohkoh Fund; Toto

## **Major Positions**

Nikko Cordial; Central Glass; Toyota; Japan Energy

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# Optimal FUND MANAGEMENT

Returns Snapshot	
Period	% (AUD)
Year to Date Return:	11.9
Return since inception: *Inception 14 Oct, 1999	39.45

Portfolio Composition at Month End			
% of NAV in:	Mar 2002	Apr 2002	May 2002
Long Stock Position	79.25	76.23	73.32
Short Stock Position	(33.59)	(35.60)	(31.13)
Index Futures			
Equity Derivatives	5.41	4.14	0.90
Net Exposure	51.07	44.77	43.09

## Historical Returns

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

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								11.9

- Trust Inception 20 December, 1999

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