

## Monthly Report to Unitholders of the

### Optimal Japan Trust

December 12<sup>th</sup>, 2003

Date	NAV	Monthly % Return*
28 November 2003	A\$11.94	-1.73%

\* After all fees

\* NAV is ex-distribution of 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

### Success – Longs & Shorts

	Sept03	Oct03	Nov03
Topix %	1.68	3.58	-4.18
OJF longs %	13.31	10.00	-5.62
OJF shorts %	-8.71	-8.23	6.51

In an unwelcome - though perhaps inevitable - reversal of form, equities were down and bonds up in November. The 4.2% fall in the Topix index was the largest monthly decline this year but less painful than the ones we suffered in July (-5.8%), October (-6.4%) and December (-5.5%) last year. The rise in appetite for risk (at least amongst non-Japanese investors) since April had major implications for sector and stock selection as well as the obvious attraction of equities over bonds. Risk indigestion in November saw the 10 year JGB yield fall from 1.5% to 1.29%. It is worth taking a look at the generic Japanese Government bond futures (see Bloomberg ticker: JB1 <CMDTY> ) and check first daily, then weekly and finally monthly charts. The daily and weekly time scale makes this year's correction look impressive, but when viewed on a monthly scale since 1988, one gets a very different view. The consensus is that Japan will not grow at anything more than 2% or so for years to come and that the financial sector will be forced to keep buying JGBs. In that world, JGB yields of 1.5-2.0% might be realistic. We have not shorted JGBs this year (regrettably) but if one looks at the long term chart and believes that most assets mean revert over time, it is still a mouth watering temptation.

Sector performance in November also revealed strong mean reversion as most of the worst performers were the sectors that had done best since the March low. Construction, Wholesale (trading companies generally and Softbank in particular), Steel, Securities and Real Estate all fell between 8 and 19% while Pharmaceuticals (boo!) were predictably strong up 4.3%. Does this mean the end of the rally and yet another false dawn in Japan's inexorable demise? I don't think so. Company earnings are growing strongly, but there is plenty more room for margin improvements even in a slow growing economy. Earnings in the first half (ended September) grew at the recurring level by 16.1% versus

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# Optimal FUND MANAGEMENT

the year earlier and full year estimates (for year to March 2004) are for 59.2% annual growth. On the basis of no less an authority than Goldman Sachs global research, Japanese companies are cheaper than both their US and European counterparts and are seeing faster earnings growth. A stronger Yen would hurt the profits of the exporting sectors but as they account for a smaller proportion of forecast earnings growth in 2003 and 2004 than they have in recent years, the overall effect is not so dramatic. Although hugely sympathetic to the negative case for the US dollar, it is a view increasingly well held by global investors and thus one I am uncomfortable in relying on. The Yen has strengthened by around 8% this year and the Bank of Japan seems happy to keep selling it in large amounts. We will remain agnostic and keep our Fund's currency position Yen neutral.

Positive contributors (long) Komatsu Ltd, Yokogawa Electric, Sumitomo Trust & Banking ,  
Toyota Motor

(short) Yamato Transport, Comsys Holding, Shimamura

Negative contributors (long) Haseko, Oki Electric, Mitsubishi Co

(short) Sanken Electric, Daiichi Pharm, Tostem Inax

## Major Positions

Nippon Steel, Toyota Motor, Kawasaki Kisen, Tokyo Tatemono, Mitsubishi Co

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# Optimal FUND MANAGEMENT

Return Snapshot	
Period	%(AUD)
Year to Date Return	26.62
Return since inception Inception 20 Dec, 1999	51.53

Portfolio Composition at Month End			
% of NAV	Sept 2003	Oct 03	Nov 03
Long Stock Position	79.19	85.42	62.79
Short Stock Position	(43.99)	(33.12)	(19.23)
Index Futures	(15.77)	(28.27)	(16.23)
Equity Derivatives	4.63	3.53	1.49
Net Exposure	24.06	27.56	28.82

## Historical Returns

Below we provide a table detailing the monthly returns of the Fund since its inception in mid-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	-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		26.62

\* Trust inception 20 December, 1999

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