

Monthly Report to Unitholders of the Optimal Japan Trust October 8th, 2004

Date	NAV	Monthly % Return*
30 September 2004	A\$13.52	0.82

* After all fees

* NAV is ex-distribution of A\$ 0.4713 (for Yr to 6/04) 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 of the initial series

Contribution – Longs & Shorts

	Jul04	Aug04	Sept04
Topix %	-4.23	-0.86	-2.43
OJF longs %	-7.56	4.38	-0.10
OJF shorts %	3.72	0.76	0.85

Important: The Optimal Japan Fund and Optimal Japan Trust are both soft-closed. The administrator (BTFE) will request any applicant for investment to contact the manager and require Directors' consent before acceptance.

The Topix index closed above 1100 in mid-October last year and only due to a strong final day did it regain the 1100 level at the close of September this year. Despite all the favourable articles, rediscovered interest in Japan and strategist upgrades, Japan has been a dull old place for equity investors over the past year. Added to the lack of capital gain is the low dividend yield of just over 1% so these returns only give cheer when compared with the annual interest received on a Yen deposit (not a lot). Again, the real fun is inside the index where the best performing sector (shipping) is up 63% whilst the worst (telco) is down 16%. On the eve of the fifth anniversary of the Optimal Japan Fund, it is striking that this relative return spread is the polar opposite of the situation when we launched. As you would recall, in those days telcos were a buy at any price, whereas ships were Old Economy and thus decidedly undesirable. How long the current "retro" boom continues is a question that we frequently chew over at odd times of the night, but as long as NTT continues to think that a 14% dividend payout ratio is all that they need to lure razor sharp equity investors onto their share register, I'd rather have my money on the high seas.

The low pay-out ratio in Japan is starting to attract some justifiable criticism now and we hope that as the banks begin to write back provisions they've made for bad loans, so will companies begin to increase their dividends. After all, with earnings growth expected to be almost 20% this year and the market trading on a 6.5% earnings yield, there is a strong case to be made for higher dividends.

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Optimal FUND MANAGEMENT

In our monthly for July, we wrote about the dramatic improvements in energy efficiency in Japan since the high-inflation years of the '70s oil shocks. As crude oil prices reach \$52/bbl, it is worth revisiting this subject. In a report of a speech given by Mizuho Securities chief equities economist Nobuyuki Saji at the Foreign Correspondents Club of Japan, Dow Jones Newswires (October 5th) states that the Japan uses only 130 grams (I thought this would be “mls”) of crude oil to generate \$1 of nominal GDP. By contrast, the USA needs 230, Sth Korea 460 and China 800g. His rationale for this is that Japan's manufacturers largely focus on value-added production as opposed to products based from raw materials. Japanese households also spend less on petrol as they drive fuel-efficient cars and drive less than other developed countries. In Japan, he estimates that only 1.2% of household spending goes on gasoline whereas in the USA it is almost 3%. In short, whilst high oil prices are not good news for Japan, the effect on the GDP will be lower than that of most oil importing countries (approximately half as much as that of Germany and about one third that of the USA). It would be best of all if oil fell back into the \$20s but if it stays high, Japan might be an unlikely winner of the hairy beauty parade.

Positive contributors (long) Ryowa Life Create, Nippon Mining, Kawasaki Kisen, Fuji Photo
(short) Ito-Yokado, Shimizu, Goldcrest, Nippon Unipac

Negative contributors (long) Tokyo Tatemono, Nichiiko Pharm, Mizuho Financial, Edion
(short) Funai Elec, Nippon Yusen, Sky Perfect, Asatsu-DK

Major Positions

Toyota Motor, Mitsubishi Co, Fuji Photo, Tokyo Tatemono, Mitsui Fudosan

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Optimal FUND MANAGEMENT

Return Snapshot	
Period	%(AUD)
Year to Date Return	13.75
Return since inception Inception 20 Dec, 1999	72.04

Portfolio Composition at Month End			
% of NAV	July 04	Aug 04	Sept 04
Long Stock Position	78.48	83.17	75.26
Short Stock Position	(36.73)	(25.36)	(28.46)
Index Futures	(21.14)	(20.43)	(19.20)
Equity Derivatives	3.55	2.91	1.77
Net Exposure	24.16	40.29	29.37

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	3.02	30.43
2004	-0.33	1.22	7.01	0.23	-1.20	3.67	-2.26	4.03	0.82				13.75

* Trust inception 20 December, 1999

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