MONTHLY REPORT TO SHAREHOLDERS OF OPTIMAL JAPAN TRUST

Optimal FUND MANAGEMENT

Monthly Performance % - *as at 29 January 2016*				
	NAV	**January**	**YTD**	**AUM**
A$ Series 1	A$11.021	-6.82%	-6.82%	A$11M

Watching Japanese – and other – equities meltdown this year, we have been waiting to find some inspiration to write this January monthly letter. Thanks to the ever-reliable and invariably interesting daily *BLAH!* , we have found words that seem to fit the moment:

"What should equity investors be doing now (in Japan and elsewhere)? My immediate answer would be to say that the current weakness represents an unmissable opportunity to buy stocks that would have been unthinkable only a couple of months ago. I have to admit, however, that I did not see the current collapse coming and have been inappropriately optimistic all year. BLAH! readers may thus choose to give my ideas a wide berth."

We, too, have been guilty of the same misplaced optimism, and also think current stock prices offer many genuine bargains, but that is clearly no guarantee that buying enthusiasm will match selling panic and offer support at current prices. It is too hard to predict the timing, even if one can assess the value.

One can't help wonder whether this severe weakness is a mania of pessimism in financial circles that will be shown to be baseless. Clearly, that is one view which we find attractive. Countering that is the gnawing sense of unease that has refused to go away since markets – especially interest rates - have increasingly become the instruments of government policy. Making debt available at zero is not conducive to a disciplined and rational allocation of capital, and while asset prices fall, the unchanging nature of debt owed just increases the pain for a leveraged investor. Being an investor in the Nikkei index from the recent peak in early August 2015 has not been any fun, but spare a thought for those in the twice leveraged and massive Nomura-managed NEXT Funds Nikkei 225 Leveraged ETF (TSE code: 1570 JP) which has fallen 42% over the same time. Even if you are borrowing at virtually nothing, the collateral has become uncomfortably thin.

The 29 January decision by the BoJ to usher in negative interest rates on new bank reserves held at the BoJ has contributed to the ferocious sell-off in banks and other financials and coincided with a fall of almost 12% in the broader market. The effect of this move on bank earnings is calculated by analysts to be around 5% while the banks sector has fallen 23%. The yield curve out to ten years is now flat and financials usually perform best with upwards sloping yield curves – notwithstanding the support from valuations. For now, fears of credit impairments due to bad loans to the resources sector have markets spooked and give sellers – and short sellers – their rationale, whether justified or not.

In spite of the stock price mayhem, Japanese companies have not been sitting on their hands. Just before month-end, the media reported that Toyota would buy out the 48% of Daihatsu's shares that they did not already own and turn it into a wholly owned, unlisted subsidiary. Daihatsu's shares leapt to reflect the 0.26:1 share swap terms, and have since fallen in step with Toyota from their February 1 high. With sales of $250bn equal to 16 times that of Daihatsu, the acquisition will not make much difference to Toyota's consolidated results, but it is a way of adding to its expertise and reach in emerging economies, including Indonesia and China. The same newspaper article reported that Toyota was also in talks with Suzuki Motors for a tie-up which would be based on Suzuki's dominant position in the Indian car market. The report was immediately denied by both companies but it is likely to represent Toyota's wishes, if not those of Suzuki. Further consolidation in the auto assembly world would be logical.

There was also an announcement by Nippon Steel that it would be entering talks with affiliate Nisshin Steel to buy it out. Unlike Toyota and Daihatsu, Nippon Steel only has a minority stake of 8% in Nisshin, but Nisshin has always been regarded as part of the Nippon Steel group. While it would be a surprise if any alternative buyer emerged to block this, it would be a welcome change to force Nippon Steel to sharpen its pencil and fight for control. There must be more consolidation in the over-crowded arc furnace steel sector and a successful takeover of Nisshin would likely spur more action.

The Sharp saga moved closer to an end with the board agreeing to restart talks from occasional suitor Hon Hai of Taiwan. Most seemed to believe it was inevitable that the Japanese government-backed Innovation Network Corporation of Japan (INCJ) would gain control of Sharp even with a lower bid than that which Hon Hai was offering, but in a welcome show of good governance, Sharp's board has decided they should look to their shareholders' – and perhaps the company's – best interests and enter legitimate discussions with Hon Hai. With Toshiba also needing to reduce its debt, there is a growing feeling that whoever buys Sharp will look to separate the company's LCD panel business from their whitegoods division and combine the latter business with that of Toshiba's as both are sub-scale on a stand- alone basis. Without some focused and dynamic management - more likely if there were to be an MBO – we would not be rushing to invest in the new company.

We watched the market fall in January with dismay. February is only ten days old, but dismay is not the right way to describe our feelings so far this month. We have seen a desperate and violent unwinding of short Yen-long Nikkei (itself leveraged or not) positions over the past few weeks with heavy volumes traded. Brokers have seen their order books reach near record highs, but it would be a foolish broker to want to see it continue in this way for long.

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Recent 3 month Fund Exposure

% of NAV in	Nov 15	Dec 15	Jan 16
Long Stock Positions	90.56	90.61	91.13
Short Stock Positions	-13.39	-9.13	-9.47
Index Futures	-20.36	-20.49	-20.84
Index Options	-	-	-
Net Exposure	56.81	60.99	60.82

Optimal FUND MANAGEMENT

Should you wish to make an enquiry about the Optimal Japan Trust, please see our website www.optimalasia.com or contact us by email at optimal@optimalasia.com.

Position Concentration

	Top 5	Top 10
Longs	31.08%	50.31%
Shorts	-9.47%	-
Total no. of positions	34	

Top Five Positions

- Sumitomo Mitsui Financial Group Inc
- Mitsubishi Estate Co Ltd
- Mitsubishi UFJ Financial Group Inc
- Japan Airlines Co Ltd
- Nomura Holdings Inc

Winners

- Nikkei Index Futures (short)
- I.H.I. Corp (short)
- Japan Airlines Co Ltd
- Sun Frontier Fudousan Co Ltd
- Takeda Pharmaceutical Co Ltd (short)

Losers

- Mitsubishi UFJ Financial Group Inc
- Sumitomo Mitsui Financial Group Inc
- Fanuc Corporation
- Hitachi Ltd
- DMG Mori Co Ltd

Sector Exposure *as at 29 January 2016*

	Longs	Shorts	Net
Consumer Discretionary	19.50%	-	19.50%
Consumer Non-Discretionary	-	-2.63%	-2.63%
Energy	-	-	-
Financials	34.88%	-	34.88%
Futures	-	-20.84%	-20.84%
Health Care	-	-5.56%	-5.56%
Industrials	32.47%	-1.28%	31.19%
Information Technology	4.28%	-	4.28%
Materials	-	-	-
Telecommunications	-	-	-

Performance Contribution	Longs	Shorts	Futures	Other	FX Forwards	Total
January 2016	-8.40%	0.50%	1.54%	1.61%	-2.07%	-6.82%

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Historical Returns – Distribution Reinvested

Optimal Japan Trust Net Monthly Returns in AUD %

Annual Distributions

Year to Jun 00 *A$1.4158*	***Year to Jun 01*** *A$0.8989*	***Year to Jun 02*** *A$0.8983*
Year to Jun 04 *A$0.4713*	***Year to Jun 05*** *A$1.4218*	***Year to Jun 06*** *A$1.2446*
Year to Jun 07 *A$2.4179*	***Year to Jun 14*** *A$2.8013*	***Year to Jun 15*** *A$0.2631*

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
Series 1 (Inception August 2002)													
2016	-6.82												-6.82
2015	-3.51	6.35	-0.72	3.61	3.41	-2.69	1.03	-6.01	-7.96	9.34	-0.53	-2.30	-1.37
2014	-5.91	-2.71	0.37	-1.68	3.12	4.40	0.27	-1.02	1.90	-0.08	2.37	1.32	1.92
2013	6.42	0.75	3.82	12.97	-3.76	2.58	1.72	-2.82	8.21	-2.62	1.03	1.57	32.71
2012	1.16	4.87	1.46	-2.87	-4.99	2.53	-1.80	-1.06	1.17	0.39	1.73	6.05	8.41
2011	3.38	2.12	-3.46	-0.54	0.90	0.09	-0.36	-3.94	-0.74	-0.09	-2.54	-0.29	-5.57
2010	1.95	-1.53	5.74	2.76	-5.91	-3.24	0.49	-1.96	2.89	0.97	1.34	3.89	7.03
2009	-1.74	-2.15	1.91	0.47	0.84	-0.46	0.28	2.59	-4.87	-0.66	-5.15	3.02	-6.14
2008	-6.67	2.21	-0.67	6.20	1.34	-5.91	-0.83	-5.34	-0.09	-0.44	-6.38	3.22	-13.41
2007	1.99	0.55	-1.03	1.35	3.45	2.28	-1.01	-6.98	1.88	0.35	-6.70	-4.69	-8.88
2006	1.82	0.43	3.86	0.35	-4.05	0.18	-0.79	1.43	0.13	2.10	0.77	2.49	8.85
2005	2.74	2.02	0.07	-0.14	0.99	1.47	2.01	3.68	6.81	1.36	2.41	4.38	31.38
2004	-0.33	1.24	7.11	0.15	-1.14	3.93	-2.22	4.01	0.23	-1.21	1.30	1.51	15.15
2003	1.80	1.98	0.41	-0.10	2.55	3.48	1.54	5.20	3.86	3.55	-1.67	3.06	28.63
2002									1.68	-4.38	-3.66	-0.42	-6.73
Initial Series (Inception December 1999)													
2016	-6.83												-6.83
2015	-3.52	7.22	-1.04	4.71	3.35	-2.69	1.33	-6.28	-7.96	9.35	-0.54	-2.30	0.13
2014	-5.74	-2.71	0.35	-1.66	3.10	4.44	0.17	-0.96	1.86	-0.08	2.46	1.24	2.07
2013	6.42	0.71	3.86	12.97	-3.76	2.51	1.77	-2.81	7.91	-2.42	1.11	1.36	32.43
2012	1.10	4.89	1.47	-2.89	-4.99	2.49	-1.71	-1.10	1.11	0.37	1.73	6.09	8.33
2011	3.37	2.09	-3.44	-0.51	0.85	0.17	-0.42	-3.90	-0.79	-0.09	-2.49	-0.27	-5.53
2010	1.94	-1.54	5.81	2.70	-5.94	-3.25	0.47	-1.86	2.84	1.01	1.36	3.86	7.03
2009	-1.74	-2.21	1.90	0.53	0.79	-0.44	0.26	2.54	-4.79	-0.72	-5.15	3.05	-6.16
2008	-6.62	2.17	-0.71	6.19	1.42	-5.97	-0.78	-5.37	-0.08	-0.42	-6.38	3.23	-13.38
2007	1.96	0.58	-0.99	1.35	3.47	2.23	-1.02	-6.99	1.85	0.40	-6.68	-4.73	-8.90
2006	1.82	0.42	3.79	0.34	-4.04	0.24	-0.77	1.57	0.13	2.72	0.99	2.62	10.04
2005	2.83	2.05	0.00	-0.14	1.04	1.37	2.63	4.15	6.71	1.31	2.39	4.30	32.45
2004	-0.33	1.22	7.01	0.23	-1.20	3.95	-2.34	4.03	0.82	-1.55	1.65	1.92	16.12
2003	1.80	1.98	0.41	-0.20	2.65	3.97	1.91	5.90	3.81	3.58	-1.73	3.02	30.43
2002	1.10	1.47	2.07	-0.26	7.13	-2.92	-1.59	-1.39	2.04	-4.47	-3.65	-0.44	-1.42
2001	-2.34	3.13	1.36	8.47	-2.14	3.96	-3.09	1.49	-3.58	1.77	-3.89	-5.46	-1.22
2000	-0.32	12.76	8.99	-1.53	2.45	11.82	-9.05	4.53	-0.37	0.90	-0.18	-3.86	26.75
1999												0.58	0.58

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