

Monthly Performance % - as at 28 February 2018

	NAV	February	YTD	Strategy AUM
Offshore Feeder	US\$18.876	-2.68%	-0.19%	US\$51M
<i>Topix Return is in USD unhedged using WM London 4pm close</i>		-1.52%	2.71%	

We took some holidays in early February – joining the multitude of foreign visitors to Japan’s ski fields - and decided to take a month’s leave from writing our monthly letter to investors. Our final letter for 2017 – which we wrote in early January - had focused on the break in the link between the Yen/\$ rate and the Japanese equity market and in doing so, we evidently angered the market’s Gods. From a level of Y113/\$ on January 8th, the Yen then rose to 105/\$ by the end of February and contrary to our thesis, the Topix index pulled back by 10% from 1900 (23 January) to the low 1700s. We would suggest that it is not all Yen related, as other developed markets also fell and the decline year-to-date in Topix is in line with the indices of the UK and Europe. The dollar (trade weighted) has been weak again in 2018 so far – continuing the trend that has been in place since late 2016 – but in spite of this, there has been no evidence of Japanese corporate profits being suppressed by the stronger Yen, so far.

We met a lot of companies in Japan last week while attending a large conference put on each year by one of the Japanese brokers. Not one company talked about any negatives from the stronger Yen, though of course profits are affected to various degrees at different currency levels. The surprise is how much less sensitive to exchange rates overall Japanese corporate profits have become when a decade or so ago, there would be a weekly exercise to tweak profit forecasts based on that week’s change in the FX rate. It is evident from meetings that a far more important factor is overall demand and global economic activity, as Japan’s corporations – large and middling – have added offshore manufacturing bases whereas they once relied overwhelmingly on exports for overseas sales.

Although their crystal balls have never been any clearer than anyone else’s, evidence of the positive outlook currently held by Japanese companies can be seen in the increased private sector capex which contributed to the upward revision to the December quarter’s GDP number. The first estimate of Q4 GDP was for annualized q/q growth of 0.4% but this has been raised to 1.6% and takes estimates for the full FY17 (ending March 2018) GDP growth to 1.8% y/y. Although the consensus calls for GDP growth to fall in FY18 and FY19, the new estimates are higher than previously made, and the pattern of recent years has been for estimates to be raised from very low

levels as the year goes by. Private consumption is forecast to accelerate in FY18 - presumably in the lead up to the rise in consumption tax from 8-10% scheduled for October 2018 – but the growth rates in capex are far higher at 3.5% for 2017 and then 2.4% in FY2018. These aggregate numbers do not surprise us from the meetings we have held in the past six months as most companies have given express targets for increased capex and in many cases, M&A too. Although hard to quantify, it is clear that the growth in capex is due in some part to the shortage of available labour in some sectors of the economy. This shortage is not likely to be alleviated in the coming years.

February’s market was rough for a number of the sectors that had done particularly well in the latter half of last year. As an example, the oil refining sector which had been up 49% over the six months to the end of January was off more than 7% in February and other strong performers up to early 2018 were also weak in February with shippers, non-ferrous metals and tires all cases in point.

In our portfolio, SMC (machinery) was our biggest detractor, closely followed by Mitsui OSK (shipping), Hazama Ando (construction) and Mitsubishi UFJ (banks) – each one costing us between 60-75 bps in performance. On the positive side, Tokai Carbon and Horiba returned 50-60 bps for the month and have been positive over a longer period.

Our portfolio trades on a PER for the coming year of just over 11x and with an RoE of 13%. Companies continue to be too cautious about their balance sheets and have excess equity but total shareholder returns are well over 50% in an increasing number of cases when you add the value of buy-backs to dividends paid. After many years of global economic expansion – albeit one which has been tepid and geographically patchy – it is right to have some doubts about how long this can continue for, but the strong sense we have from our discussions with Japanese companies is that shareholders will receive an increasing share of the business in the form of dividends, buy-backs and possibly buy-outs. It is a margin of safety that gives us confidence in our optimistic outlook for Japan.

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Recent 3 month Fund Exposure

% of NAV in	Dec 17	Jan 18	Feb 18
Long Stock Positions	91.03	93.39	95.41
Index Futures	-	-	-
Net Exposure	91.03	93.39	95.41

Optimal FUND MANAGEMENT

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

Position Concentration

	Top 5	Top 10
Longs	29.36%	50.20%
Total no. of positions	28	

Top Five Positions

Mitsubishi UFJ Financial Group Inc
Hitachi Ltd
Horiba Ltd
Mitsui OSK Lines Ltd
Kasai Kogyo Co Ltd

Winners

Tokai Carbon Co Ltd
Horiba Ltd
Daido Metal Co Ltd
Pressance Corp
Nishimoto Co Ltd

Losers

SMC Corp
Mitsui OSK Lines Ltd
Hazama Ando Corp
Mitsubishi UFJ Financial Group Inc
Kasai Kogyo Co Ltd

Sector Exposure as at 28 February 2018

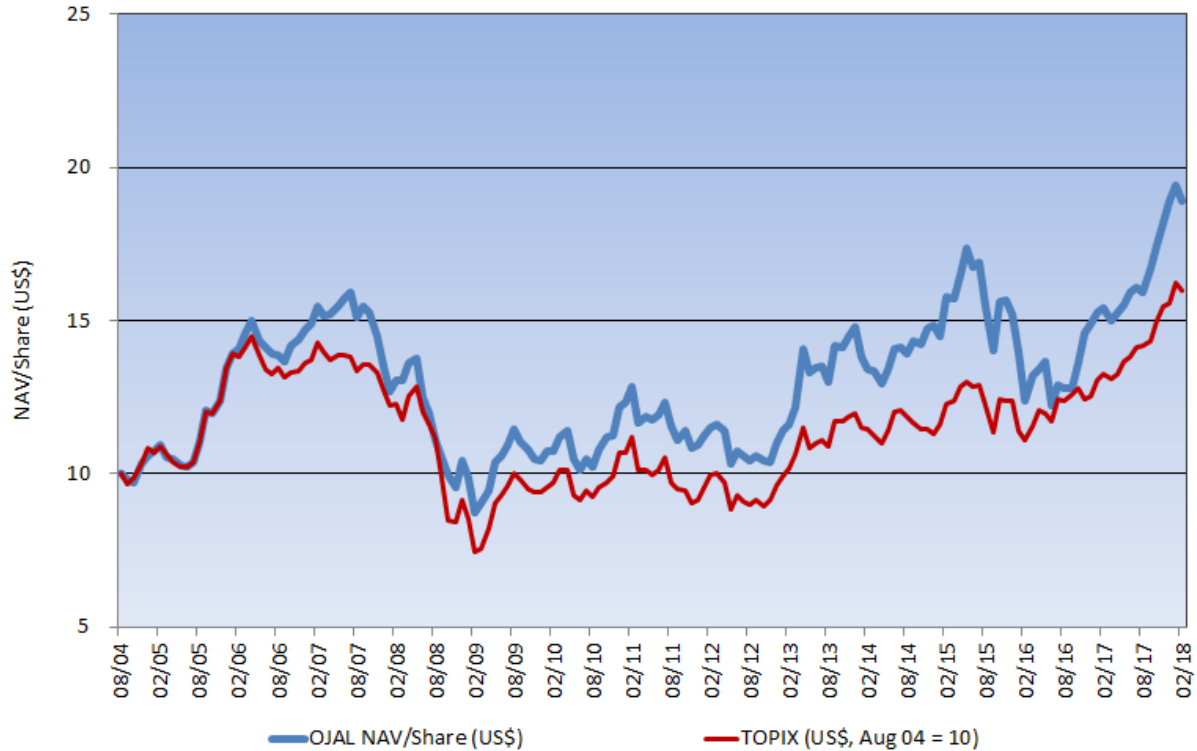
	Longs
Consumer Discretionary	26.93%
Consumer Non-Discretionary	4.29%
Energy	3.13%
Financials	14.46%
Health Care	-
Industrials	15.46%
Information Technology	14.02%
Materials	13.95%
Telecommunications	3.17%

Performance Contribution	Longs	Futures	FX Forwards	Other	Total
February 2018	-3.81%	-	-0.83%	1.96%	-2.68%

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Portfolio Performance as of 28 February 2018



Historical Returns- Optimal Japan Absolute Long Fund Monthly Returns in USD (before Performance Fees) %

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	Topix [*] YTD
(Inception September 2004)														
2018	2.56	-2.68											-0.19	2.71
2017	2.13	1.08	-2.46	1.55	1.61	2.76	0.95	-0.82	4.63	4.67	4.19	3.96	26.81	23.92
2016	-8.33	-11.28	6.75	1.57	1.82	-10.75	5.75	-0.86	-0.09	6.68	6.84	2.36	-2.06	1.23
2015	-2.45	8.82	-0.37	4.95	5.27	-3.54	0.70	-8.52	-9.08	11.21	0.39	-2.82	2.41	9.57
2014	-6.55	-3.03	-0.52	-3.07	3.71	4.69	0.57	-1.38	2.91	-0.65	3.38	0.96	0.40	-5.25
2013	4.19	1.40	5.18	15.67	-5.74	1.13	0.45	-3.56	8.91	-0.35	2.62	2.14	35.00	24.60
2012	2.84	2.31	1.04	-1.81	-9.47	3.97	-1.30	-1.79	1.73	-1.42	-0.57	5.68	0.37	5.01
2011	1.31	3.89	-9.20	1.72	-0.51	1.02	3.69	-6.40	-3.98	2.70	-4.91	0.83	-10.34	-14.55
2010	2.58	0.19	4.19	1.88	-8.25	-3.15	3.36	-2.39	5.77	3.79	0.36	8.26	16.65	13.67
2009	-5.28	-11.56	3.78	4.75	9.49	2.12	3.11	4.76	-3.58	-2.26	-2.78	-0.38	0.38	2.85
2008	-6.00	2.60	0.15	4.21	1.40	-9.57	-3.85	-7.26	-5.49	-5.14	-4.01	8.78	-22.95	-28.24
2007	1.50	3.69	-1.88	0.33	1.71	1.49	1.27	-4.97	2.18	-1.04	-5.37	-6.57	-7.97	-6.37
2006	3.57	1.22	3.55	2.74	-4.40	-1.32	-1.55	-0.29	-1.51	3.73	1.48	1.94	9.14	0.94
2005	1.61	2.05	-3.83	-0.47	-1.81	-0.58	1.17	6.66	9.32	-0.75	3.25	8.64	27.25	24.59
2004									-1.60	-1.32	6.18	2.52	5.70	8.16

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