

Prospect Japan Fund

Bloomberg Yen / USD	PJF LN 86.24	NAV Performance (USD) %				
			December	YTD	1 Year	3 Year
NAV (USD)	1.01	Prospect Japan Fund	2.02	20.24	20.24	32.89
Price (USD)	0.86	Topix Small Index	4.66	8.76	8.76	27.62
Premium/ Discount %	-14.34%					

Prospect Japan Fund inception date is 20 December 1994. Above performance of the Fund is net of fees and expenses and includes reinvestment of dividends and capital gains. Topix Small Cap Index (TPXSM) performance cited above is the total return including the reinvestment of net dividends into the index denominated in US Dollars (Source: Bloomberg). One cannot invest directly in an index. TPXSM is a capitalization - weighted index designed to measure the performance of the stocks listed on the First Section of the Tokyo Stock Exchange, excluding the TOPIX 500 stocks and non-eligible stocks.

The NAV is published in the 'Other Offshore Funds' column of the Financial Times. The NAV and Price are located on Bloomberg page PJF LN. The NAV and Indicated Prices are also listed on Bloomberg page LCFR and Reuters page LCFR07.

The Fund gained 2.02% during the month of December, underperforming the Topix Small Index' +4.66% performance. The Fund has strongly outperformed in 2012, gaining 20.24% versus the Topix Small Index' 8.76% increase. The end of year cash position was 14%.

Positive performance came from Katakura Industries (3001) and Tri-Stage (2178). Katakura Industries, a shopping mall operator engaged in the manufacture and sale of textiles, pharmaceuticals and auto parts, saw its share price rise sharply following the mid-month elections, reaching a 13-month high. Tri-Stage Inc, a marketing consultant service provider, saw its share price rise during the first half of the month, ahead of 3Q results announcement and the acquisition of customer relationships management company Mail Customer Center Co.

Weakness in the Fund came from Ace Koeki (8749), a commodity futures trader, which declined for most of the month ahead of 3Q end.

Japan has entered a technical recession after maintaining an annualized 3.5% GDP decline for Q3, its 3rd recession since the GFC. Sluggish exports and dampened domestic demand have dragged on the economy. Industrial production declined year-on-year for the 6th consecutive month in November, falling 5.8% and cementing the case for enhanced stimulus efforts supported by the incoming Abe administration.

Reflation expectations fueled by the landslide election of the Liberal Democratic Party to power after three years in the wilderness drove the yen to a 28-month low, and equities higher during the month. Former Prime Minister Shinzo Abe returned to power on a platform to launch a full-scale war on Japan's entrenched deflation, weakening the currency and achieve 3% nominal GDP growth via short-term stimulus spending on public works and economic growth centered legislation.

At months end, the yen was trading at 86.1 yen to the dollar, overshooting Bloomberg's top rated analysts' estimates of 82 by June 2013. On 14 December the quarterly Tankan survey of large manufactures showed an average forecast of 78.3 through March 2013.

The 16 December election gained the LDP and its coalition partner New Komeito 68% of the lower house seats, establishing a super majority capable of pushing through much of the new administration's lofty goals. The coalition came out swinging, calling for an approximately JPY 10 trillion supplementary budget centered on public works. Key to Abe's vision is closer ties between the government and the Bank of Japan, pressuring the BOJ to further expand its efforts on the monetary stimulus by publically pushing for an unlimited monetary easing and the adoption of a 2% inflation target, as opposed to the current 1% "goal". Abe has gone so far as to consider revising the law governing the BOJ if it does not meet expectations. The development of policies for economic growth will fall to a new economic revitalization council.

Unsurprisingly, the Bank of Japan expanded its asset purchase program by JPY 10 trillion at its 20 December meeting, increasing allocations for JGBs and short-dated T-Bills by JPY 5 trillion each. The BoJ also announced that it would review raising its 1% inflation "goal" to a more concrete 2% inflation "target", as demanded by incoming PM Abe, at its January policy board meeting. More aggressive BoJ action can be expected with the appointment of a new governor from April 2013, and there is also the possibility of additional fiscal stimulus when the 2013 budget is drafted.

Miki Shoji reported that average office vacancy in Tokyo's Central Business District crept up 2 bps month-on-month to 8.76% in November. The increase is the first following four consecutive months of lower declines.

REIT

In USD, the TSEREIT index saw a total return of +0.89% month-on-month, trailing the Nikkei 225's +5.62% month-on-month performance. J-REITs performed strongly during the month, following the strong re-election of Shinzo Abe's LDP to power on promises of increased fiscal and monetary easing. The index reached a 23-month high, on improved sentiment and strong supply-demand conditions, despite the large IPO of GLP J-REIT (3281).

The Bank of Japan refrained from J-REIT unit purchases for a second month in December. At the end of the year, the total amount of J-REIT units purchased is JPY 111.1 billion (85.5% of total allotment).

Leading logistics facility developer and manager, Prologis Inc. announced 12 December board approval of J-REIT sponsorship. The planned J-REIT is to list with a portfolio of 12 A-class properties, with AUM of JPY 173.4 billion. The properties will be concentrated in the Tokyo and Osaka areas, with an average age of 3.4 years and total floor space of about 940,000 sqm. The Nikkei newspaper reports a Prologis J-REIT could list as soon as January 2013.

The Nikkei newspaper reported on 25 December, that Hulic (3003) has plans to list a J-REIT by 2014. The company is targeting a portfolio of over JPY 100 billion at listing, growing to JPY 300 billion in 3 to 5 years. The portfolio would consist of Hulic owned condominiums, nursing facilities and office buildings.

The Financial Services Agency working group concluded its 13th and final meeting with a final report on suggested revisions to the Investment Trust Act. The changes will be drafted and voted on by the incoming Diet, with expected implementation in 2013. Changes to regulations effecting J-REITs are as follows:

- 1) Lifting certain bans on overseas acquisition of real estate
- 2) Diversification of fund procurement channels, including rights offerings, unit buy backs, and reduction of capital without compensation. The issue of convertible bond issuance was discussed, but shelved for the time being.

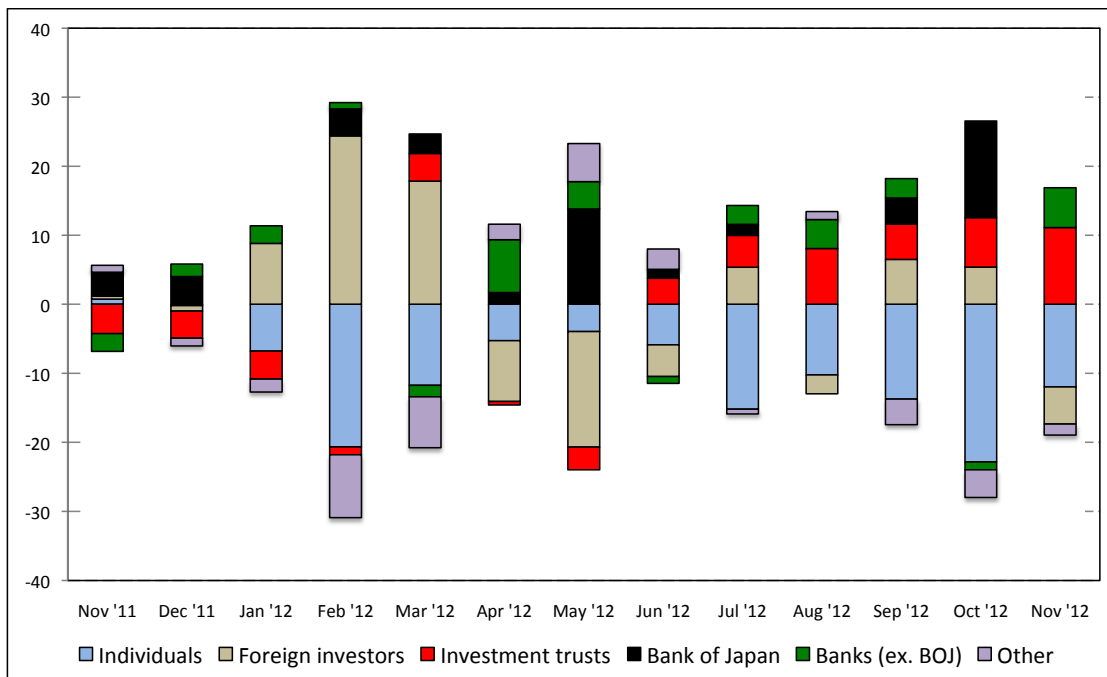
3) Establishing rules to strengthen corporate governance, specifically in regards to transactions with related entities and preserving unit-holder right to pursue injunction of new unit issues.

There was a total JPY 9.6 billion in property acquisitions announced during the month, along with JPY 5.6 billion in sales.

The TSEREIT index performed +25.95% during the year, versus the Nikkei 225 index's 12.22% gain.

Note: As of 31st December, 2012, of the Fund, Tri-Stage Inc (2178) is 10.29%, Katakura Industries (3001) is 9.71%, and Ace Koeki (8749) is 0.88%. Hulic (3003) and GLP J-REIT (3281) are not holdings of the Fund.

Tokyo Stock Exchange Market Data (Net Buyers/Sellers of J-REITs)



Sector Weightings

Advertising	10.3
Apparel	9.7
Beverages	4.6
Building Materials	2.0
Diversified Financial Services	6.3
Engineering & Construction	12.7
Internet	3.3
Investment Companies	3.6
Machinery-Diversified	0.1
Media	0.5
Real Estate	0.2
REITs	7.8
Retail	9.5
Storage/Warehousing	10.0
Total**	80.8
No of Positions	19

Top 10 Holdings

Symbol	Security	% of Total Assets
1921	TOMOE CORP	10.9
2178	TRI-STAGE INC	10.3
9304	SHIBUSAWA WAREHOUSE CO LTD/THE	10.0
3001	KATAKURA INDUSTRIES CO LTD	9.7
8205	SHAKLEE GLOBAL GROUP INC	8.0
8963	INVINCIBLE INVESTMENT CORP (REIT)	7.8
gktaihei	GODO KAISHA TAIHEIYO JISHO #1 BOND	5.4
2533	OENON HOLDINGS INC	4.6
3528	GRO-BELS CO LTD	3.6
2389	OPT INC	3.3

Percentage weightings are Prospect Asset Management's internal calculations and have not been reconciled by the administrator.
 **Results of calculations as presented may not be exact due to rounding and precision of stored values.

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The Prospect Japan Fund "Company" is a closed-end investment company incorporated in Guernsey and listed on the London Stock Exchange. The Company's investment objective is to achieve long-term capital appreciation from a portfolio of securities primarily of smaller Japanese companies listed or traded on Japanese Stock Markets.

There are risks involved with investing, including possible loss of principal. In addition to the normal risks associated with investing, narrowly focused investments, investments in smaller companies, illiquid investments and investments in a single country typically exhibit higher volatility. International investments may involve risk of capital loss from unfavorable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations.

Fund price and index performance calculations are obtained from Bloomberg and are as of the end of the month. NAV performance calculations are provided by PAMI and are un-audited. As of August 2003, the benchmark index changed from TSE2 to Topix Small since its characteristics with respect to average market capitalization more closely resemble the investment strategy pursued by the portfolio. The investment return and principal value of an investment will fluctuate so that an investor's shares when redeemed may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. Additional information regarding policies for calculation and reporting returns is available upon request.

The Board of the Prospect Japan Fund decided that the PJF should become a member of the AIC (The Association of Investment Companies) in 2005. The AIC only accepts valuations where the underlying assets are valued on a 'Fair' basis, which in the case of PJF, means on a bid basis (per the AIC). Upon the Prospect Japan Fund's Board approval, the Fund's administrator Northern Trust made a change to the pricing methodology in February 2006, whereby underlying assets in the Fund are valued using the 'last bid price.' Consequently, the Fund's Net Asset Value and performance from February 2006 reflects the change in this pricing methodology. In addition, in newsletters from February to September 2006, as a result of the new pricing methodology, Prospect had been calculating a performance based on an un-rounded Net Asset Value. In October 2006, Prospect made a decision to calculate performance based on a Net Asset Value rounded to the nearest hundredth. Therefore, the monthly performance from February to September was modified to reflect this change. The performance from October 2006 and going forward will incorporate this change.

Prospect Asset Management Inc. is registered as an investment adviser under the United States Investment Advisers Act of 1940, as amended, with Securities and Exchange Commission number 801-47749. The company specializes in investment in Japanese equities and real estate and seeks investments offering what PAMI considers above average earnings while trading at reasonable valuations.