

## Prospect Japan Fund

Bloomberg Yen / USD	PJF LN 105.33	NAV Performance (USD) %				
			December	YTD	1 Year	3 Year
NAV (USD)	1.29	Prospect Japan Fund	0.00	27.72	27.72	44.94
Price (USD)	1.05	Topix Small Index	0.78	21.10	21.10	31.79
Premium/ Discount %	-18.68%					

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.

Fund performance was flat during the month, versus the Topix Small Index' 0.78% gain. The Fund has solidly outperformed during the year, gaining 27.72% versus the index' 21.10% increase.

Strong performance came from Tri-Stage Inc. (2178) and Heiwa Real Estate REIT (8966). Tri-Stage, a marketing consultant service provider, saw sharp gains following the announcement of 3Q results, which remained ahead of full-year guidance. Heiwa Real Estate REIT, a diversified REIT, gained strongly towards year end in line with the J-REIT index.

Weakness came from Katakura Industries (3001) and Endo Lighting (6932). Katakura Industries, a shopping mall operator engaged in the manufacture and sale of textiles, pharmaceuticals and auto parts, retreated during the month, surrendering much of its relative outperformance ytd following disappointing 3Q results. Endo Lighting, maker of LED light fixtures, continued its decline following its downward revision to full year earnings forecasts due to a slowdown in light fixture replacement demand and inventory write-offs.

The last month of the year saw Japanese equities end at annual highs, as the Yen and equities responded to news out of the US Federal Open Market Committee of a USD 10 billion tapering of extraordinary asset purchases, with further incremental reduction of stimulus forthcoming. The Yen ended the year at 5 year low of 105.26 which helped the Nikkei rally strongly, finishing up +30.50% in USD terms for the year. The outlook for Japanese equities remains strong, despite the historic 2013 rally, with PE ratios remaining much unchanged due to strong earnings growth.

The Tokyo Stock Exchange reports that foreign investors have set a record for investment in Japanese equities, with a total inflow of JPY 12.9 trillion (net buying of JPY 2.3 trillion) in the eleven months through November.

GDP growth in the 3<sup>rd</sup> quarter was slower than initially estimated, at an annualized 1.1% (vs. initial 1.9% estimate). The figure marks a decline from the previous quarter's 3.6% GDP growth. Consumer spending contributed strongly to the expansion, while business spending

lagged, remaining unchanged from Q2. Business confidence rose to a six-year high according to the Bank of Japan quarterly Tankan survey.

Despite geopolitical headwinds, Japan Tourism Agency reports that the nation will probably welcome its 10 millionth visitor of the year during the month. The previous annual record was 8.6 million recorded in 2010. Chinese visitors to Japan increased 96% year-on-year to 101,900 last month, in spite of bilateral tensions in the East China Sea.

The ruling LDP party submitted a bill legalizing casinos to parliament during the month. Japan has the potential to be the world's second largest gambling market, with Union Gaming Group seeing possible annual revenue of USD 10 billion. The bill will be voted on during the next legislative session starting in January.

Miki Shoji reported that vacancy rates in Tokyo's Central Business District continued their downward trend in November, falling 0.04 ppt to 7.52% in November. This marks its lowest reading since June 2009.

Other major cities also saw improvements, with vacancy rates declining by 0.03 ppt to 9.85% in Osaka, and Nagoya declining 0.31 ppt to 9.76% in Nagoya.

### REIT

In USD, the TSEREIT index saw a total return of 1.09% month-on-month, underperforming the Nikkei 225's 1.48% month-on-month gain. The TSEREIT index has gained 15.44% year-to-date, versus the Nikkei 225's +30.50% performance.

The Bank of Japan purchased JPY 500 million in J-REIT units during the month. The total amount of units purchased to date now stands at JPY 141 billion, JPY 1 billion over the JPY 140 billion originally allotted for through 2013 end. The annual target for 2014 direct purchases is JPY 30 billion.

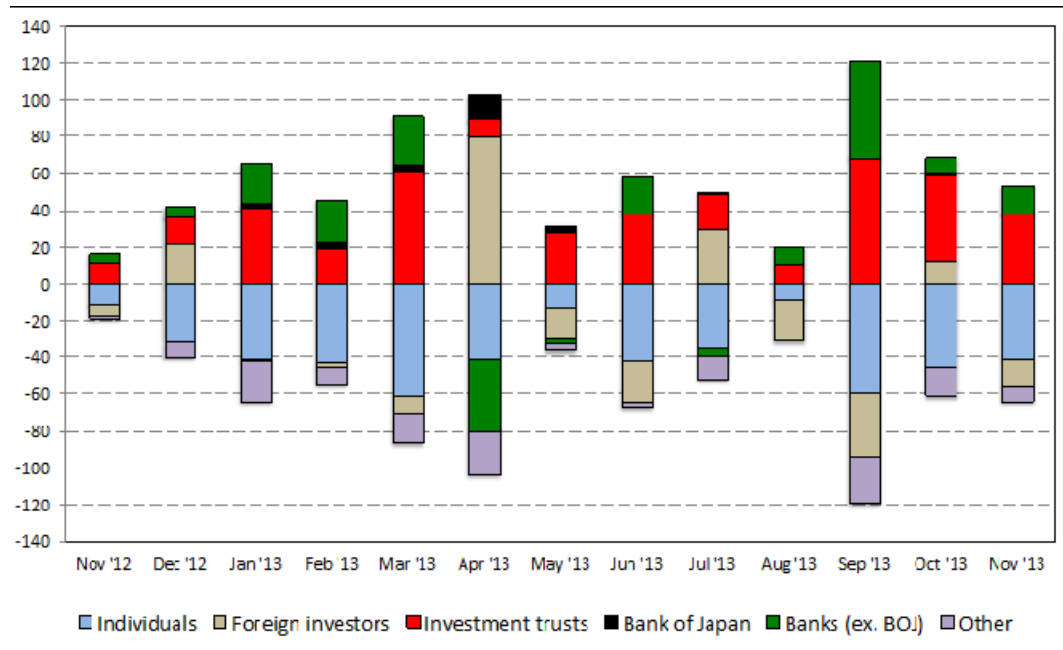
Invincible Investment (8963) announced a private placement of 224,887 new shares (16.7% dilution), expected to raise about JPY 3.0 billion. The proceeds will be used

along with JPY 20.4 billion in new borrowing to repay JPY 22.7 billion in high interest loans. The deal will reduce average interest rates on JPY 41.3 billion of borrowing to 1.936% (from 3.657%). Forecasts for the next fiscal period (June 2014) are for a 132% period-on-period increase in DPU to JPY 464.

There was a total JPY 18.5 billion in property acquisitions announced during the month, along with JPY 5.1 billion in dispositions.

*Note: As of 31 December 2013, of the Fund, Tri-Stage Inc (2178) is 7.69%, and Katakura Industries (3001) is 8.49%, Endo Lighting (6932) is 2.49%, Invincible Investment (8963) is 0.58%, and Heiwa Real Estate REIT (8966) is 4.31%.*

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



**Sector Weightings**

Advertising	7.7
Auto Manufacturers	4.1
Banks	1.9
Building Materials	2.5
Distribution/Wholesale	1.1
Diversified Financial Services	7.2
Engineering & Construction	5.6
Machinery-Diversified	1.2
Real Estate	16.8
REITs	18.8
Retail	7.3
Storage/Warehousing	4.8
Transportation	1.7
Total**	80.8
No of Positions	33

**Top 10 Holdings**

Symbol	Security	% of Total Assets
3001	KATAKURA INDUSTRIES CO LTD	8.5
2178	TRI-STAGE INC	7.7
3227	MID (REIT)	7.0
8205	SHAKLEE GLOBAL GROUP INC	6.2
8986	JAPAN RENTAL HOUSING (REIT)	5.9
1921	TOMOE CORP	5.4
3528CB01	GRO-BELS #1 cb 2% 2018	4.8
8966	HEIWA REAL ESTATE REIT (REIT)	4.3
gktaihei	GODO KAISHA TAIHEIYO JISHO #1 BOND	4.2
7404	SHOWA AIRCRAFT INDUSTRY CO LTD	4.1

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.