

## Prospect Japan Fund

Bloomberg Yen / USD	PJF LN 98.84	NAV Performance (USD) %				
			June	YTD	1 Year	3 Year
NAV (USD)	1.15	Prospect Japan Fund	-	13.86	19.79	41.98
Price (USD)	0.94	Topix Small Index	-0.91	9.20	12.99	34.69
Premium/ Discount %	-17.69%					

*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' 0.91% decline. Year-to-date the Fund has outperformed, gaining 13.86% versus the Topix Small Index' 9.2% increase.

Positive performance came from Toyo Engineering Works (6443) and Kenedix Residential Investment (3278). Toyo Engineering Works, a freezer and air-conditioner manufacturer and servicer, rose to its highest level since 1997 on news that its largest shareholder Mitsubishi Heavy Industries (7011) will seek to acquire the company at a 123% premium to last traded price. Kenedix Residential Investment, a residential J-REIT, recovered along with the rest of the J-REIT market as long-term benchmark bond yield volatility subsided.

Weakness in the Fund came from Katakura Industries (3001) and Gro-Bels (3528). Katakura Industries, a shopping mall operator engaged in the manufacture and sale of textiles, pharmaceuticals and auto parts, continued to retreat after rising to a four year high in April month on investor focus on companies with strong real estate holdings. Katakura holds JPY 99.2 billion in rental real estate assets with implied unrealized capital gains of JPY 77 billion, and recovered strongly towards the end of June. Gro-Bels, a property developer continued to retreat from near recent highs, following the release of full-year results that showed weak parent level earnings.

The Nikkei 225 index briefly entered bear market territory on 13 June, declining 20.4% by month's end from its peak of 15,627 on 22 May before rebounding to end June down 0.71% mom. External factors loomed large on Japanese performance for most of the month, amid a lack of strong domestic catalysts. The timing of an eventual US stimulus withdrawal, and Chinese money market volatility chief among them.

1Q GDP growth has revised to an annualized 4.1% (from initial forecast of 3.5%), and the current account surplus for April surprised on the upside at JPY 750 billion vs. the estimated JPY 350 billion. Japanese exports rose 10% yoy in May, more than the 6.4% yoy rise expected.

The Abe cabinet approved measures that aim to remove regulator barriers to private enterprise and promote cor-

porate investments through tax and regulatory reform. The policy changes are expected to go into effect this fall, in an effort to avoid political headwinds before the July upper house elections.

The Japanese Health, Labor and Welfare Ministry announced that the Government Pension Investment Fund (GPIF) would lower its allocation of Japanese bonds to 60% from 67%, while raising the allocation of Japanese stocks to 12% from 11% and foreign stocks to 12% from 9%, foreign bonds to 11% from 8%. The GPIF has JPY 111.9 trillion in assets under management, the largest public pension fund in the world.

The Bank of Japan left its policy unchanged following its two-day policy meeting this month. Expectations were for action to stem the volatility in bond markets by extending bank loan maturities and extending allocation for J-REIT purchases, which ended the month at 98.4% of the total 2013 purchase target. BoJ Governor Kuroda has stated his desire to avoid incremental moves in response to market volatility, while affirming that the bank sees improvements in the underlying economy. The Bank did offer some stability by adjusting to more frequent, but smaller bond purchases.

Miki Shoji reported that vacancy in the Tokyo Central Business District fell by 0.21 ppts to 8.33% last month, the lowest level since January 2010, with no large new supply coming online, and low new vacancies. Demand for new condominiums also remained strong, with contract ratio maintained at a high 78.1% in May, despite higher supply (+49.2% yoy).

### REIT

In USD, the TSEREIT index saw a total return of +4.09% month-on-month, outperforming the Nikkei 225's 0.92% month-on-month rise. J-REITs gained for the first time in three months, as benchmark government bond volatility subsided. The TSEREIT index has gained 10.50% year-to-date, versus the Nikkei 225's +15.09% performance.

The Bank of Japan purchased J-REIT units eight times during the month, worth JPY 900 billion. The total amount of J-REIT units purchased is JPY 137.8 billion (98.4% of

the JPY 140 billion allotted through 2013 end). While the BOJ left the J-REIT allocation amount unchanged after this month's policy board meeting, subsequent statements by Governor Kuroda made the point that JPY 140 is a projection and not an upper limit, suggesting that the BoJ is willing to continue support beyond the remaining JPY 1.3 billion left of the stated 2013 allocation.

Hoshino Resorts Inc. (private) announced the planned IPO of Hoshino Resort REIT (3287), a lodging J-REIT with planned AUM of JPY 15 billion at listing, making it the smallest listed J-REIT. The IPO is expected to raise JPY 10.0 billion.

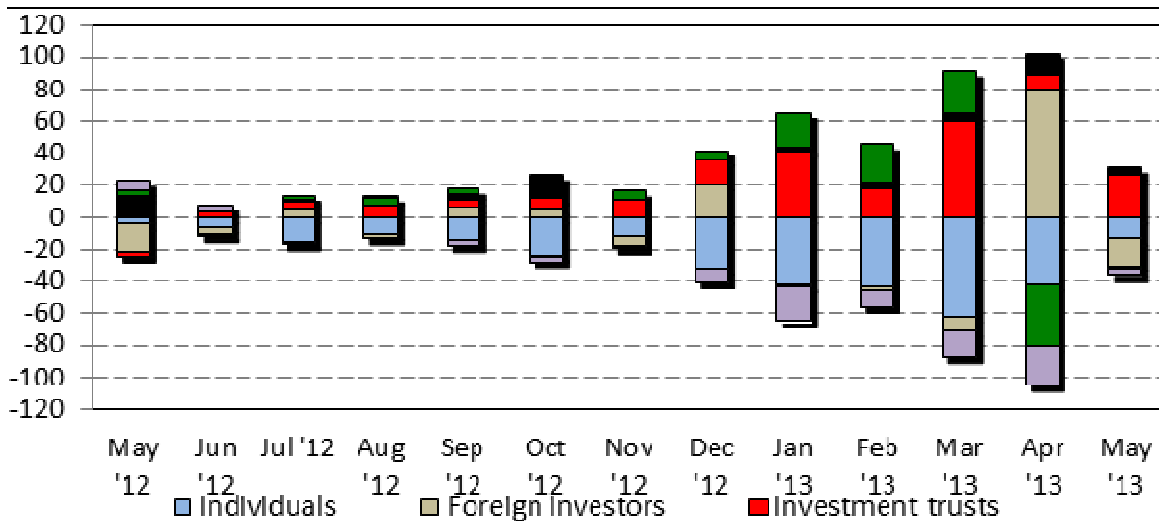
Nomura Real Estate Office Fund (8959) announced its first secondary issuance of new shares since 2008 during the month. The J-REIT will issue 67,430 (22.1% dilution), for an expected total of JPY 26 billion. The proceeds will be used to purchase three Tokyo office properties and repay debt.

United Urban Investment (8960) announced its second new share issuance of the year. The J-REIT will issue a total of 74,750 new shares (3.2% dilution), raising an expected JPY 8.5 billion to be used for the purchase of two new properties.

There was a total JPY 49.8 billion in property acquisitions announced during the month, and dispositions of JPY 597 million.

*Note: As of 30<sup>th</sup> June, of the Fund, Toyo Engineering Works (6443) is 10.10%, Kenedix Residential Investment (3278) is 4.59%, Katakura Industries (3001) is 6.08%, and Gro-Bels (3528) is 3.32%. Hoshino Resort REIT (3287), Mitsubishi Heavy Industries (7011), Nomura Real Estate Office Fund (8959), and United Urban Investment (8960) are not holdings of the Fund.*

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



(JPY billion)

## Sector Weightings

Advertising	7.1
Apparel	6.1
Auto Manufacturers	1.4
Banks	0.3
Building Materials	12.7
Distribution/Wholesale	1.3
Diversified Financial Services	7.5
Engineering & Construction	10.7
Entertainment	0.1
Food	0.1
Internet	1.6
Investment Companies	3.3
Machinery-Diversified	0.0
Real Estate	10.4
REITs	14.4
Retail	14.8
Storage/Warehousing	2.3
Textiles	0.4
Transportation	1.5
Total**	95.9
No of Positions	41

## Top 10 Holdings

Symbol	Security	% of Total Assets
8205	SHAKLEE GLOBAL GROUP INC	12.7
1921	TOMOE CORP	10.1
6443	TOYO ENGINEERING WORKS LTD	10.1
8833	TOHO REAL ESTATE CO LTD	8.8
2178	TRI-STAGE INC	7.1
3227	MID (REIT)	6.7
3001	KATAKURA INDUSTRIES CO LTD	6.1
gktaihei	GODO KAISHA TAIHEIYO JISHO #1 BOND	4.7
3278	KENEDIX RESIDENTIAL INV CORP (REIT)	4.6
3528	GRO-BELS CO LTD	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.