Prospect Asset Management

The Prospect Japan Fund Limited

Monthly Review

Bloomberg	PJF LN
Yen / USD	100.93
NAV (USD)	1.41
Price (USD)	1.00
Premium/ Discount %	-28.86

NAV Performance (USD) %	September	YTD	1 Year	3 Year
The Prospect Japan Fund Limited	2.92	2.92	15.57	5.22
MSCI Japan Small Cap Index	5.51	10.06	19.64	26.68

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 Prospect Japan Fund Limited inception date is 20 December 1994. The above performance of the Fund is net of fees and expenses and includes reinvestment of dividends and capital gains. (Source: Prospect Asset Management, Inc.) Although the Company is not managed to a benchmark, it measures its performance against the MSCI Japan Small Cap Index (Total Return) for comparison purposes only. The MSCI Developed Markets Small Cap Indices offer an exhaustive representation of this size segment by targeting companies that are in the Investable Market Index but not in the Standard Index in a particular developed market. The indices include Value and Growth style indices and industry indices based on the Global Industry Classification Standard (GICS®). (Source: Bloomberg)

The Fund gained 2.9% (USD) during the month, underperforming the MSCI Japan Small Cap index's 5.5% MoM USD gain.

Strength during the month came from holdings in Nagano Bank (8521), Fukushima Bank (8562) and Tri-Stage Inc. (2178). Nagano Bank and Fukushima Bank are regional banks based respectively in Nagano and Fukushima prefectures. Both banks performed well during the month, supported by the Bank of Japan's (BoJ) decision to forego a further push into negative interest rates. Tri-Stage Inc., a marketing consultant service provider, saw strong gains following an upward revision to H1 forecasts, citing better than expected revenue and profits in major segments.

While the Fund has started the process of converting the Stock Acquisition Rights ("SARs") it holds in Prospect Co., Ltd. (3528), no SARs were converted during the month.

Revised GDP for Q2 came in at +0.7% YoY, above the +0.2% initial figure and meeting original forecasts, due to upward revisions to private sector inventory (contributed 0.1% to GDP, vs preliminary 0% contribution) and better than originally reported business spending (-0.1% vs -0.4% QoQ preliminary reading).

August exports declined 9.6% YoY, underperforming consensus estimates for a 4.7% YoY decline, following the previous month's -14.0% performance. Exports have seen 11 consecutive months of YoY declines. Imports improved to -17.3% YoY, leaving a trade deficit of JPY 18.7 billion, well below the forecast surplus of JPY 191.0 billion.

Labor cash earnings for July improved to +1.4% YoY, beating consensus estimates of +0.4%, and slightly better than last month's +1.3% YoY reading. The bounce was facilitated by a 4.2% YoY growth in bonuses, while contract wages rose 0.3% YoY. Real cash earnings came in +2.0% YoY.

Overall Household Spending declined for the sixth consecutive month in August, falling 4.6% YoY, well below consensus estimates of -2.1%, and sharply below the previous month's -0.5% performance.

National Core CPI (excluding fresh food) for the month of August was unchanged at -0.5% YoY, the sixth consecutive month of YoY declines.

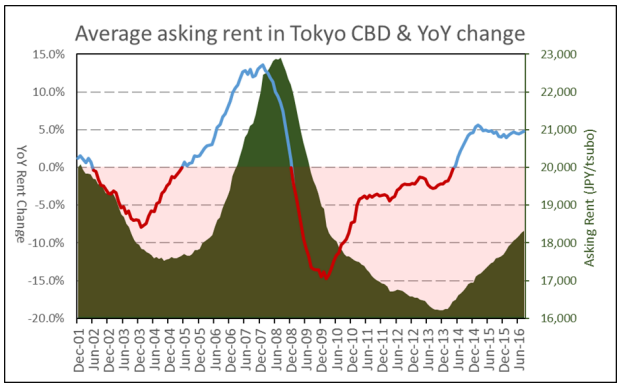
Faced with concerns regarding the limitations of monetary easing with increasingly evident side effects on financial sector profits, and limited success in achieving its 2% inflation target, the Bank of Japan adopted a new "QQE with Yield Curve Control" framework following the September board meeting. The BoJ left its controversial negative interest rate policy unchanged, while shifting the target of policy to the yield curve, and away from fixed increases to the monetary base.

Major adjustments include the elimination of the JPY 80 trillion annual increase in monetary base, allowing the BoJ to be flexible in its purchases depending on needed adjustments to the yield curve. The central bank's stated intention is to buy JGBs in line with the current pace, but eliminated the target for average maturity on JGB purchases. In practice, this could allow for defacto tightening without the need for an official policy change, should yields fall below the target range of "around zero".

The BoJ also announced an "inflation-overshooting commitment", stating that extraordinary policy will continue until inflation is stable above the 2% target. The ETF purchase target remained stable at 5.7 trillion, though 2.7 trillion was allotted for ETFs that track the broader TOPIX index.

Miki Shoji reported that vacancy rates in Tokyo's Central Business District (CBD) declined 13 basis points (bps) to 3.9% in July, reaching an 8-year low. Year-on-year, the vacancy rate has fallen 95 bps.

Average office rents in the CBD rose 4.6% YoY, a slight rise from last month's 4.5% increase. Rent levels are now 12.7% above the December 2013 lows, while remaining well below the highs seen in the last cycle with vacancies at similar levels.



1 tsubo = 3.306 sqm

While the Fund does not currently hold any J-REITs, they serve as a bellwether for the overall Japanese real estate market, and the BoJ's commitment to asset reflation via direct purchase of investment units. During the month, the BoJ purchased a total of JPY 4.8 billion in J-REIT units. This brings total purchases to date to JPY 336.3 billion, 73% of its stated JPY 90 billion annual purchase allocation.

Note: As of 30 September 2016, of the Fund, Nagano Bank (8521) is 4.6%, Fukushima Bank (8562) is 23.1%, Tri-Stage Inc (2178) is 5.5%, Tohoku Bank (8349) is 0.8% and Prospect Co. Ltd is 2.1% (not including the SARs).

(Sources: Bloomberg, Nomura, Nikkei, Miki Shoji, Bank of Japan)

Sector Weightings

Banks	54.2
Storage/Warehousing	12.0
Retail	9.2
Real Estate	8.7
Advertising	5.5
Engineering & Construction	4.4
Machinery-Diversified	2.2
Diversified Financial Services	0
Transportation	0
REITs	0
Total*	96.1
No of Positions	14

Top 10 Holdings

Symbol	Security	% of Total Assets
8563	DAITO BANK LTD/THE	25.7
8562	FUKUSHIMA BANK LTD/THE	23.1
9313	MARUHACHI WAREHOUSE CO LTD	9.8
8205	SHAKLEE GLOBAL GROUP INC	9.2
2178	TRI-STAGE INC	5.5
8521	NAGANO BANK LTD/THE	4.6
3001	KATAKURA INDUSTRIES CO LTD	4.5
1921	TOMOE CORP	4.4
3528	PROSPECT CO LTD	4.3
7404	SHOWA AIRCRAFT INDUSTRY CO LTD	2.2

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.

Important Legal Information – Please Read

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The Prospect Japan Fund Limited "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.

NAV performance calculations are provided by PAMI and are un-audited. Fund price and index performance calculations are obtained from Bloomberg and are as of the end of the month. Although the Company is not managed to a benchmark, it measures its performance against the MSCI Japan Small Cap Index (Total Return) for comparison purposes only. 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 Limited 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 Limited'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.