

# The Prospect Japan Fund Limited

Monthly Review

Bloomberg	PJF LN	NAV Performance (USD) %	June	YTD	1 Year	3 Year
Yen / USD	112.05	The Prospect Japan Fund Limited	-0.81	-1.61	-11.59	-12.23
NAV (USD)	1.22	MSCI Japan Small Cap Index	0.95	13.86	20.10	33.75
Price (USD)	1.27	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.				
Premium/ Discount %	3.80					

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)

As announced on 31 May 2017, terms have been agreed on the recommended all-share offer for the Fund by Prospect Co., Ltd ("Offer"). The Offer will be implemented by way of a scheme of arrangement, further details are set out in the scheme document which is posted on the Fund's website.

The Fund retreated 0.81% (USD) during the month, underperforming the MSCI Japan Small Cap index's 0.95% MoM USD gain.

Weakness during the month came from holdings in Prospect Co., Ltd (3528) and Fukushima Bank (8562). Prospect Co., Ltd. shares retreated following announcement of the offer for the entire issued capital of Prospect Japan Fund (PJF LN) and the large accompanying share dilution. Fukushima Bank, a regional bank based in Fukushima prefecture, traded down following last month's FY 2017 earnings announcement showing large profit declines due to tightening loan and investment income yields.

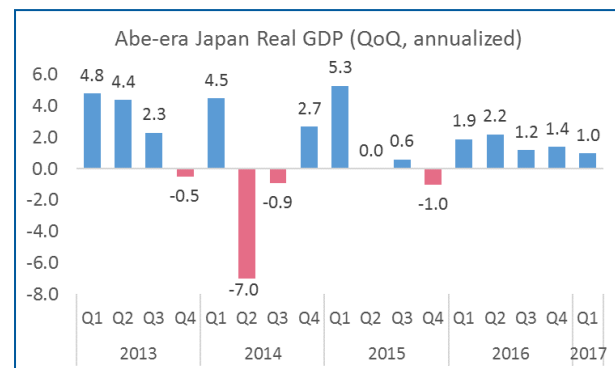
Strength during the month came from holdings in Shaklee Global Group (8205) and Maruhachi Warehouse (9313). Shares in Shaklee Global Group, a seller of nutrition and personal care products, rebounded after touching a 4-year low earlier in the month. Maruhachi Warehouse, a warehousing and logistics company, gained ahead of Q2 results due for the release in early July.

In December 2015, the Fund acquired 1,440 Stock Acquisition Rights ("SARs") at a total cost of JPY 288 million. Each SAR gives the right to acquire 100,000 ordinary shares in Prospect Co., Ltd at a price of JPY 54 per share. The SARs are exercisable until 20 December 2020. The SARs have been held at cost in the NAV reports since December 2015 and are not revalued. For information purposes only, if the SARs were to be 'fair valued' using the Black-Scholes-Merton model, in line with the annual financial statements, there would be an uplift of US\$6,715,982.45 (31 December 2016 annual accounts: US\$7,684,136) from the NAV based on retaining the SARs at cost for the same date, the exercise price remains unchanged. A total of 90 SARs have been converted leaving 1,350 at 31 December 2016. None have been converted in 2017.

June ended with Prime Minister Shinzo Abe in a weakened position, as approval ratings dipped as low as 36% in some polls, due to cronyism scandals involving alleged favors to close associates in opening schools in a special economic zone. The

decline in support prompted the PM to announce that he is considering a cabinet reshuffle, and raised speculation that he may be forced to postpone calling an election this year.

Final Q1 GDP was revised down to an annualized +1.0%, underperforming initial estimates of +2.2%, and well below the consensus estimates of +2.4% growth. This marks five



consecutive quarters of expansion, the longest run of quarter-on-quarter growth since 2006. Underperformance was driven by contribution from inventory investment being revised down from +0.1ppt in the preliminary GDP estimates to -0.1ppt, and a downward revision to private consumption (+0.3% QoQ, vs +0.4% QoQ preliminary reading).

Corporate profits gained 26.6% YoY in the three months through March 2017, the strongest quarterly gain since Q4 2013. Capital Spending rose 4.5% YoY during the same period, outperforming consensus estimates for a 4.0% YoY gain.

The labour market remains tight, with unemployment for May rising slightly from a 20-year low of 2.8% to 3.1%, and the jobs-to-applicant ratio inched up to 1.49x. Real cash earnings were unchanged YoY in April, after declining 0.8% YoY last month, while overall household spending declined 0.1% YoY in May, outperforming the consensus estimate of -0.7% YoY, and marking the 15th consecutive month of YoY declines.

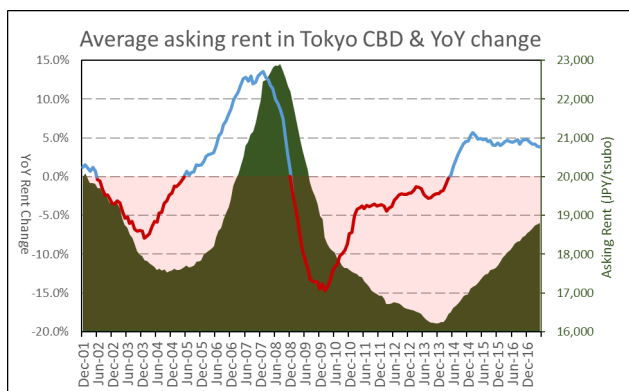
National Core CPI (excluding fresh food) for the month of May ticked up to 0.4% YoY, matching consensus estimates. This marks the fifth consecutive month of price gains, though inflation remains far removed from the Bank of Japan's (BoJ) 2% target.

May exports rose 14.9% YoY, below consensus estimates for an 16.0% YoY increase. This marks a sixth consecutive month of export growth. Imports rose 17.8% YoY, above the consensus estimates for a 14.5% YoY increase. Japan reported a May trade deficit of JPY 203.4 billion, underperforming consensus estimate of JPY 43.3 billion surplus.

The BoJ left its core policy unchanged during the month, while announcing a scheduled technical adjustment to its negative interest rate policy (NIRP), increasing the proportion of current account funds that will be considered a part of the “macro add-on balance” not subject to negative policy rates. The benchmark ratio was set at 20% (up from 17%) for the June through August 2017 period. This marks the sixth consecutive increase since NIRP was announced in February 2016. The BoJ estimates the “policy rate balance” (subject to negative rates) for the period will range from JPY 10 to 20 trillion, unchanged from the last three-month period. The next benchmark ratio period (September to November 2017) will be announced on 11 September 2017.

Miki Shoji reported that vacancy rates in Tokyo’s central business district (CBD) rose 2 basis points (bps) to 3.41% in May. Year-on-year, the vacancy rate has fallen 64 bps. The higher vacancy rate reflected supply overhang for new buildings, as existing building vacancy fell to 2.99%, the first sub-3% reading since April 2008.

Miki Shoji reports that average office rents in the CBD rose 3.8% YoY, the 37<sup>th</sup> consecutive monthly gain, though the pace of gains have now slowed for two consecutive months. Rent levels are now 16.0% above the December 2013 lows, while remaining 17.9% below 2008 highs when vacancies were 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 9.6 billion in J-REIT units. This brings total purchases to date to JPY 405.9 billion.

Note: As of 30 June 2017, of the Fund, Prospect Co. Ltd (3528) is 3.6% (not including the SARs), Fukushima Bank (8562) is 23.4%, Shaklee Global Group (8205) is 9.8% and Maruhachi Warehouse (9313) is 9.9%.

(Sources: Bloomberg, Miki Shoji, Bank of Japan, Mainichi)

## Sector Weightings

Banks	52.9
Storage/Warehousing	10.0
Retail	9.8
Real Estate	5.7
Engineering & Construction	0.2
REITs	0
Total*	78.5
No of Positions	9

## Top 10 Holdings

Symbol	Security	% of Total Assets
8563	DAITO BANK LTD/THE	26.1
8562	FUKUSHIMA BANK LTD/THE	24.4
9313	MARUHACHI WAREHOUSE CO LTD	10.0
8205	SHAKLEE GLOBAL GROUP INC	9.8
3528	PROSPECT CO LTD	5.7
8521	NAGANO BANK LTD/THE	2.4
1921	TOMOE CORP	0.2

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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This information is for use by investment professionals only. Past performance is no indication of future results. This document does not constitute an offer of shares of The Prospect Japan Fund Limited nor the solicitation of an offer to buy such shares. This document should not be forwarded or distributed to any other person except with the prior written consent of Prospect Asset Management Inc (PAMI).

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.