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THE ABSOLUTE FUND

Monthly Report – July 31st 2002

Fund Performance

Share Class (Principal series)	NAV	July 2002		2002 Year to Date		Since Inception†	
		Fund (%)	FT World (%)*	Fund (%)	FT World(%)*	Fund (%)	FT World (%)*
Class A – US$	US$102.32	(0.78)	(8.36)	+1.05	(16.00)	+2.32	(7.87)
Class B - £	£103.24	(0.59)	(10.59)	+2.25	(21.75)	+3.24	(13.33)
Class C - €	€102.40	(0.64)	(7.69)	+1.67	(23.72)	+2.40	(14.43)

**The FT World Share Index in the currency of the respective share class – Source: FT/Bloomberg* *†1st October 2001*

We didn't think that conditions in financial markets could get much more challenging than they were in June but we were wrong. July served up a toxic cocktail of plunging equity and corporate bond markets, coupled with unprecedented volatility. As investors and regular readers of this report know, we regard any performance number for the Absolute Fund which is preceded by a minus sign as unsatisfactory and we are therefore disappointed to report declines of 0.78%, 0.59% and 0.64% in the prices of the US$, £ and € shares classes respectively for the month of July. The relatively better performance of the sterling and euro share classes is entirely due to the differentials in interest rates which are captured through our systematic hedging of all currency exposure within the Absolute Fund.

As the comparative numbers above reveal, the performance of the Absolute Fund was clearly much better than that of broad equity markets in which investors continued to sustain heavy losses. We attach greater importance, however, to our performance in absolute terms and compared with our peers. Falls of 1.35% and 1.04% in the CSFB Hedge Fund Index and Hedge Fund Research ("HFR") Fund of Hedge Funds Index show just how difficult it was to preserve capital in July. At least we can draw some consolation from the fact that performance since the beginning of the year is positive and broadly in line with cash deposits.

For the Absolute Fund's equity hedge fund managers the problem in July wasn't so much the fact that equity markets were falling but that selling was indiscriminate. Indeed, shares of better quality companies often fell by more than those of their weaker brethren as traditional investors scrambled to take profits wherever they could still find them. In this respect, the kind of in-depth fundamental research which gives most of our equity hedge fund managers their 'edge' proved to be a disadvantage rather than an asset. Corporate bond markets also remained in disarray as credit spreads (the incremental rate of interest a borrower has to pay over and above that paid by a 'safe' borrower such as the US government) continued to widen in response to the growing list of corporate accounting scandals and general fears about levels of corporate indebtedness. Again, investors seemed unwilling to differentiate between companies which are sound credit risks and those which are not and this impacted on the debt-related strategies represented within the Absolute Fund including convertible bond arbitrage and distressed and high yield. Finally, stock market volatility exploded in July to reach levels higher than in September last year and during 1998's Long-Term Capital Management financial crisis. Although the FT World Share Index fell by 'only' 8% in July in local currency terms it was down by as much as 16% at its nadir. The risk management techniques which most of the Absolute Fund's underlying managers utilise are extremely difficult to operate in these circumstances.

Not surprisingly, short bias funds occupied two of the slots on our 'Best 3 Funds' list in July. However, a European equity hedge fund, Fund ELS7, was our most successful investment with a gain of 5.9%, an extraordinary result bearing in mind that the fund was at no time more than 10% net short during the month. For the second successive month, the 'Worst 3 Funds' list was headed by Fund USLS2, which we gave the required 60 days notice to redeem at the end of June. The appearance on the same list of Fund USLS5, one of our most profitable investments so far this year, is testament to the extreme market conditions.

Biggest 5 Holdings as at 31st July 2002

Name of Fund	%	Strategy	July (%)	Year to Date (%)
MS3	3.5	Multi-strategy	(0.6)	2.2
DHY2	3.5	Distressed Securities	(1.8)	0.9
CBA4	3.3	Convertible Bond Arbitrage	(1.2)	5.5
CBA5	3.2	Convertible Bond & Merger Arbitrage	(0.7)	2.2
ED2	2.9	Event Driven	0.1	1.9

Best 3 Funds in July

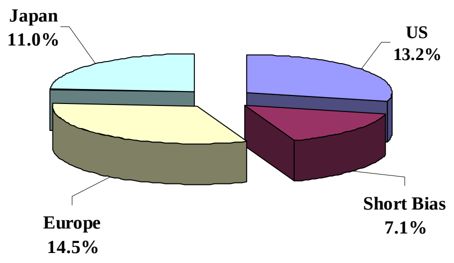
Name of Fund	Strategy	July	YTD
ELS7	European L/S	5.9	9.0
USSB3	Short Bias	5.4	10.3
USSB1	Short Bias	4.5	3.7

Worst 3 Funds in July

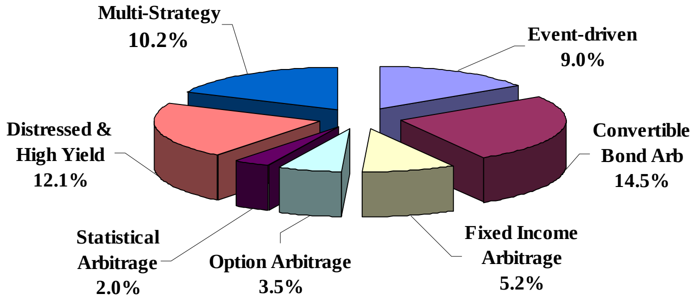
Name of Fund	Strategy	July	YTD
USLS2	US Equity L/S	(9.9)	(20.5)
USLS5	US Equity L/S	(4.9)	4.3
OA1	Option Arbitrage	(4.3)	(5.0)

Asset Allocation by Strategy (as at 31st July 2002)

Equity Long/Short (45.7%)



Arbitrage & Other (56.4%)



Outlook

In the last two months we have been fighting a bruising and almost successful battle just to preserve capital and we wish that we could offer the prospect of an imminent uplift in performance. However, the month of August is usually characterised by thin trading volumes in financial markets which can lead to exaggerated and sometimes strange movements in share and bond prices and exchange rates. Our instinct and experience therefore tells us that August is likely to be a dull month for the Absolute Fund and this prognosis is so far being backed up by the weekly estimates of performance we receive from many of our underlying hedge fund managers.

As we have said before, rising stock and/or corporate bond markets are not a pre-requisite for the Absolute Fund to achieve the 1% monthly returns we aim to provide. The composition of the Absolute Fund is such that we should also be able to deliver steady returns during periods when market indices are range-bound or even trending downwards. All that we and the managers of our underlying funds need is for market participants to begin to discriminate once again between companies with good and bad prospects and cheap and expensive shares and bonds. The irrational and indiscriminate behaviour of financial markets over the last few months, not in terms of the falls in market indices (which may be wholly justified) but with respect to the prices of individual securities, has left a host of glaring anomalies which we are confident the Absolute Fund's underlying managers will be able to harvest. This should lead to a series of monthly returns of 1% or more. With four months of the year remaining after August, we are still hopeful that the Absolute Fund will provide a return in 2002 which, even if not in double figures, will still compare very favourably with cash deposits and, almost certainly, equity markets.

For what it is worth, we remain cautious about prospective returns for traditional investors in most equity markets and find it hard to resist comparing the price graphs of the US and Japanese stock markets with a 10-year time shift. In our opinion, the bubbles of the US consumer spending and US (and UK?) house prices are still to burst.

Fortunately, and in contrast, our confidence and conviction in the Absolute Fund's asset allocation and in our fund selection grows ever stronger. In July, we initiated new investments in Fund ED4 (event-driven), Fund USLS10 (US equity long/short) and Fund ELS9 (European equity long/short) and added to the Absolute Fund's investment in Fund JLS2 (Japanese equity long/short). At the end of August, the Absolute Fund's exposure to convertible bond arbitrage will fall to our target of 10% and our disappointing investments in Funds USLS2, USSB4 (see last month's report) and SA1 (statistical arbitrage) will be gone.

As always, we welcome your comments, suggestions and questions

Charles Hovenden & Christopher Aldous – 21 August 2002

Manager's Track Record & Summary Statistics

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
1999	0.83	1.07	0.96	2.60	1.43	0.74	1.61	0.37	0.81	0.70	2.46	0.57	15.05
2000	1.36	3.21	1.87	(0.03)	1.01	1.63	0.98	0.80	0.83	0.17	(0.28)	0.58	12.77
2001	0.87	0.41	0.36	0.38	0.62	(0.32)	(0.10)	0.68	(0.19)	0.39	0.24	0.63	4.02
2002	0.49	(0.01)	0.82	0.65	0.41	(0.52)	(0.78)						1.05

Annual Rate of Return	9.05	Sharpe Ratio (@ 5% risk free)	1.46	Biggest Monthly Loss	(0.78)
Standard Deviation	2.77	Correlation with FT World Index (Local)	0.42	Biggest Peak-to-Trough Drawdown	(1.30)

NB: The monthly returns in the shaded portion of the 'Manager's Track Record' table are those of a portfolio previously managed by the Investment Manager of the Absolute Fund. Together with other almost identical portfolios, it was the forerunner of the Absolute Fund in terms of both investment strategy and procedures and its investments have been absorbed into the Absolute Fund. Returns prior to October 2001 have been adjusted to reflect the Absolute Fund's scale of fees. Figures from October 2001 onwards are for the Class A (Principal series) shares of the Absolute Fund.

General Information

Size of Fund:	US$57.8m	**Investment Manager:**	Absolute Fund Management Ltd. 33, St. James's Square London SW1Y 4JS Telephone: +44 (0) 20 7661 9342 Website: www.absolutefund.co.uk **Contact: Christopher Aldous**
No. of Holdings:	46		
Share Classes:	US$, £, €		
Basic Fee:	1%		
Incentive Fee:	15% of gains between 6% and 24% p.a.		
High Water Mark:	Yes	**Administrator:**	International Fund Managers (Ireland) Ltd. IFSC House International Financial Services Centre Dublin 1 Telephone: +353 1 670 0660 **Contact: Andrew Martin**
Dealing:	Monthly (35 days notice for redemptions)		
Min. Investment:	US$100,000		
Fund Domicile:	Cayman Islands		
Listing:	Irish Stock Exchange		
Price Information:	Financial Times under The Absolute Fund Ltd.		

Risk Warning

AFM is regulated by the FSA

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www.absolutefund.co.uk