

Share Class (Principal series)	NAV	May 2004		2004 Year to Date		Since Inception [†]	
		Fund (%)	FT World (%)*	Fund (%)	FT World (%)*	Fund (%)	FT World (%)*
Class A – US\$	US\$111.23	(0.74)	+0.91	+1.90	+1.88	+11.23	+21.08
Class B - £	£116.45	(0.50)	(2.40)	+2.89	(0.53)	+16.45	(2.95)
Class C - €	€113.31	(0.67)	(0.95)	+2.29	+5.21	+13.31	(9.70)

*The FT World Share Index in the currency of the respective share class – Source: FT/Bloomberg

†1st October 2001

Financial markets have a tiresome knack of keeping investors humble and so it was perhaps typical that the ecstasy of April (when the Absolute Fund's returns ranked in the top few percentiles of the global fund of hedge fund universe) would be followed by the agony in May of the second biggest monthly loss in our 5 ½ year track record. As all of the Fund's investors know, we absolutely hate losing money in any circumstances and the fact that May's performance was superior to the main benchmark HFR Fund of Hedge Funds Index (-0.97%) and substantially better than that achieved by some of the most celebrated names in the fund of hedge funds business provides only limited consolation.

If there is such a thing as a 'Perfect Storm' for our strategy then we possibly encountered it in May. The month began with the announcement of a second consecutive month of strong growth in employment in the US, prompting fears that a rise in interest rates was imminent. Whilst everyone surely knew that it is becoming increasingly hard for the Federal Reserve to justify keeping rates at just 1%, the reaction in financial markets was violent: equity markets worldwide fell sharply (the Japanese TOPIX Index was down by 11% mid-month), bond yields spiked higher and the dollar strengthened. In the equity long/short half of the Absolute Fund's portfolio, the insurance provided by our allocation to short bias funds worked well and largely offset the losses sustained by our long-biased managers. However, short bias profits were dissipated in the second half of the month as confidence and markets recovered, whilst the reduction in net exposure which many of our long-biased managers had implemented through their risk management controls restricted their participation in the rally. Frustratingly, therefore, we lost money in both long-bias and short-bias sub-strategies in May. Our allocation to Japanese funds, having contributed 0.43% to returns in April and 0.81% in March, cost us 0.34% in performance in May.

Whilst occasional monthly losses are probably inevitable in the equity half of the portfolio due to its higher return and risk profile, losing 0.40% in the arbitrage half of the portfolio in May was a most unusual and unwelcome experience. Most arbitrage strategies involve bonds of one form or another and are therefore exposed to interest rate- and credit-risk which our managers hedge as they see fit. However, the whiff of higher interest rates prompted conventional investors to pull billions of dollars from corporate bond funds. This led to indiscriminate selling and dislocations in credit markets against which it was impossible to hedge effectively. In summary, we made money in only 2 out of 9 sub-strategies and just 15 out of 48 underlying funds in May. These are sorry statistics which we neither hope nor expect will be repeated for some considerable time.

Biggest 5 Holdings as at 31st May 2004

Name of Fund	%	Strategy	May (%)	Year to Date (%)
JLS6	3.1	Japanese Equity Long/Short	(0.2)	+13.4
ED4	3.0	Event-Driven	(0.4)	+2.2
USLS12	2.9	US Equity Long/Short	+1.1	+6.8
FICA6	2.9	Credit Arbitrage	(1.2)	+2.2
DHY7	2.8	Distresses Securities	+0.3	+4.1

Best 3 Funds in May

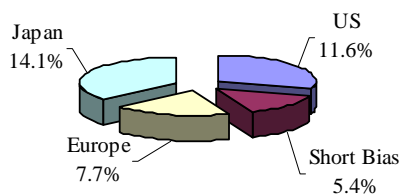
Name of Fund	Strategy	May	YTD
USSB2	Short Bias Equity	+3.3	+0.8
MS4	Multi-Strategy	+1.5	+3.6
ED5	Event-Driven	+1.4	+7.0

Worst 3 Funds in May

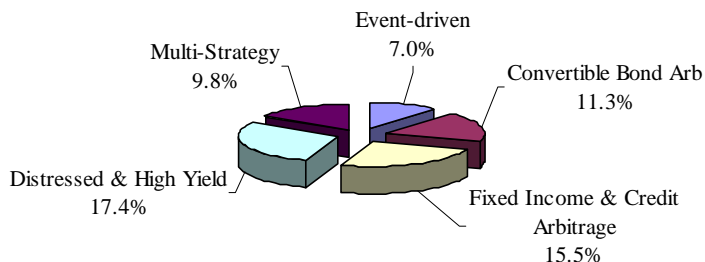
Name of Fund	Strategy	May	YTD
JLS3	Japanese Equity L/S	(12.5)	(12.9)
JLS5	Japanese Equity L/S	(4.3)	+12.5
CBA9	Convertible Arbitrage	(4.0)	+1.7

Asset Allocation by Strategy (as at 31st May 2004)

Equity Long/ Short (38.8%)



Arbitrage & Other (60.9%)



Outlook

Although we often emphasise our focus on preserving capital at all times and preach the power of compounding small positive returns, it is simply unrealistic to expect the Absolute Fund never to have 'down' months. We haven't discovered the secret of eternal profits and we never will. May's loss of 0.74%, whilst disappointing to us both professionally and personally, can hardly be described as disastrous in absolute terms. The circumstances were exceptional and we are not going to react by making wholesale changes to the Absolute Fund's composition.

We have, however, re-examined the Absolute Fund's portfolio to check that it does not contain risks which we had hitherto not fully recognised. We have often written about net market exposure as a source of risk in relation to equity long/short funds but it applies equally to bond-based strategies. After last year's bumper returns from corporate bonds, it is our opinion that credit spreads (the difference between corporate and US government bond yields) are more likely to widen than contract further in the year ahead. We were therefore particularly keen to make sure that the Absolute Fund was not overtly net long of credit risk. However, having spoken with many of our credit-oriented managers and viewed their portfolios and risk management data, we are satisfied that this is not the case. Time after time, we discovered that losses in May could be attributed principally to dislocations in capital structures of specific companies. For this reason, we are confident that May's losses are mostly anomalous and are likely to be recovered in the months ahead.

We were visiting Japan during the second week of May when the market plunged and were well aware of the pain that this had caused for several of our managers. We had, in fact, already halved the sizes of the investments in both JLS3 and JLS5 at the end of March because of concerns about rising levels of net market exposure and volatility of returns. Without this timely and prophetic change, performance in May would have been about 0.25% worse. JLS3's loss of more than 12% would usually trigger the sale of the rest of the Absolute Fund's investment (due to our internal 6% stop-loss limit). However, much stricter exposure limits have now belatedly been introduced which should prevent a repeat of May's shocker. In addition, we still judge JLS3's investment team to be outstanding stock-pickers (as they demonstrated in 2003) and we are mindful that capacity in the best funds is a serious challenge in Japan. For these reasons, we have decided to be pragmatic and retain the Fund's half unit of investment. The 6% stop-loss limit, however, has now become non-discretionary.

As always, we thank the Fund's investors for their trust and welcome any comments, questions and suggestions.

Charles Hovenden & Christopher Aldous

23rd June 2004

Manager's Track Record & Summary Statistics (for Class A US\$ shares)

	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)	(0.04)	(1.07)	(0.42)	0.18	0.83	0.53
2003	0.67	0.30	(0.01)	0.46	0.61	0.60	0.36	0.86	0.84	1.41	0.10	0.82	7.24
2004	1.00	0.26	0.87	0.51	(0.74)								1.90
Annual Rate of Return	7.54	Sharpe Ratio (@ 5% risk free)						0.98	Biggest Monthly Loss				(1.07)
Standard Deviation	2.59	Correlation with FT World Index (Local)						0.33	Biggest Peak-to-Trough Drawdown				(2.80)

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\$87.8m	Investment Manager:	Absolute Fund Management Ltd. 4, Arlington Street London SW1A 1RA Telephone: +44 (0) 20 7307 0000 Website: www.absolutefund.co.uk Contact: Christopher Aldous
No. of Holdings:	48	Administrator:	International Fund Managers (Ireland) Ltd. IFSC House International Financial Services Centre Dublin 1 Telephone: +353 1 670 0660 Contact: Andrew Martin
Share Classes:	US\$, £, €		
Basic Fee:	1%		
Incentive Fee:	15% of gains between 6% and 24% p.a.		
High Water Mark:	Yes		
Dealing:	Monthly (with 35 days notice for redemptions)		
Min. Investment:	US\$100,000		
Fund Domicile:	Cayman Islands		
Listing:	Irish Stock Exchange		

Price Information

	Financial Times	Bloomberg	SEDOL	ISIN
Class A (US\$)	under The Absolute Fund Ltd	ABSFNDA KY <Equity>	3093568	TBC
Class B (£)	“	ABSFNDB KY <Equity>	3093591	TBC
Class C (€)	“	ABSFNDC KY <Equity>	3093610	TBC

Risk Warning

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