Kimura Dreamvisor Newsletter Summary 27th November 2006

Chances of a rate hike by BOJ before year's end are 20 % at most; US FF rates cannot decrease so easily.

Do not believe media's market explanation

Today's market opening was down due to Yen strength and US stocks fall. However due to the fact main indexes had already renewed lows sell orders were few and buyers on dip took confidence. Future short sellers buying back in a hurry could also have caused this but anyway at 9:30 am market had recovered to previous day's high. US $ kept steady above 115 Yen level therefore large exporters previously sold were bought back and finally we ended at 22d November level.

Technically speaking a so-called 'Micro bottom' typical pattern formed, characterized by ups and downs in a narrow range near bottom zone. TOPIX broke its 25th of September but Nikkei 225 did not signalling recovery. By calculating TOPIX price range since April high: TOPIX lost 344,72 points up to June low, TOPIX rose 233,02 points up to October's high regaining 2/3 of loss. From October's high to current low TOPIX lost 145,65 points which is golden ratio 61,8 % at 1528 level therefore TOPIX recovered strongly. From a chartist angle it looks difficult to break such level.

If you believe in what medias say foreign investors turned negative for Japanese stocks since autumn but that is totally misleading. Misunderstanding inducement through media's mislead and readers misread piled up. Some hedge funds did sell, however most global asset managers have not changed Japan weighting putting aside slight position squaring, money flow remains steady.

When professional investors take action, reasons have nothing to do with television or newspapers reporting something like 'market reacted this way because there were such news today'. Professionals managing own positions forestall information, interpret it then act like a chess player discounting his opponent next move.

In addition medias usually publish articles after the actual fact came out to sell it to third parties. It's important but not newsworthy. News thrown to the general public usually belongs to old news category for professionals. Readers and viewers take investment action after looking at such type of news. When stock popularity goes up based on medias articles professionals are already selling. There is a huge value gap between news available to anyone and news made out real time statistical data compilation. In the latter case information flows are swiftly delivered to seasoned professionals from well-informed persons, most of the time this is discounted in advance by market.

BOJ intends to further increase rates but market's the expert.

Recent Yen strength is based neither on both US economic slowdown signs and EU next rate rise nor to mention expected BOJ rate increase. However even if BOJ does increase rates it will be +0,25 % at most and by next year, meanwhile US FF rates will remain steady at that level for the next six months or so then eventually cut once or twice by 0,25 %.

During last BOJ quarterly press conference Fukui stated that current monetary economic policy was driven by abnormal economic situation like deflation, financial crisis etc. but he repeated that should the economic situation normalize then rates would be hiked. Considering current earnings improvement, employment progression it is just a matter of time for Japanese rates to increase. In that sense a rate hike during next BOJ meeting the 19th of December cannot be totally excluded. But leading indicators such as individual's consumption, industrial production and leading advance indicators like machinery orders weakened since September end. I believe Japanese government has to somewhat revise down its forecasts.

Current economic cycle is the longest post-war but growth rate between previous Izanagi and current cycle was a pale 2 %. Most of the growth was due to Asian economies expansion, excluding special factors pure domestic led growth has been rather weak. Putting aside domestic led demand weakness there are no other positive domestic factors in sight. US economy is now clearly slowing and this will have important negative impact on housing demand therefore globally one cannot have too positive views on consumption.

Stock prices steady pace is maintained alongside earnings, if domestic consumption starts to jump then BOJ will tighten, no doubt. However recent market weakness set doubt on this scenario and unless machinery orders (announced next month) or Tankan advance indicators show resilience then forget about rate increase this year. I believe odds are only 20 % for a rate increase this year. A lot of market participants expect US rate cuts next calendar year but this is not as easy as it looks. First employment figures are still on the rise, hourly salary is increasing at 4 % whis is above prices increase. Further savings rate is still negative; from the excess demand point of view rates are still too low.

US current deficit high level and negative savings rate lead to believe that rates are still too low. Unless those two indicators show substantial improvement there are no reasons to lower rates. Any improvement will take time, US rate cut would signal hard slowdown, which is not exactly what Japanese equities investors want to see anyway.