

## Kimura Dreamvisor Newsletter Summary 4<sup>th</sup> October 2006

NY Dow new historic high give us a hint.

World excess money is progressing, it will spread to Japan.

NY Dow registered a new absolute historic high first time for the past 6 years and 9 months. Oil price went down which is negative for natural resources development related equities but raw fuel expenses decrease and this has a positive impact on individual's consumption therefore buy orders went ahead. It seems the market consensus is heading toward US economy soft landing.

Housing starts decreased but thanks to oil price decline individual's consumption effect is limited. Rates have stabilized and loan defaulting should also be limited.

Advanced ISM index declined to 52.9 but as the index kept above 50 economy is still in an expansionary phase. Generally production goes down 3 months after it has broken under 50 level, then Japanese economy is impacted. This still looks far ahead.

Following oil gold also declined; money flows which fed commodities markets suddenly went directionless. This said there are resistances to buy 10 years TB yielding only 4.6 %, by default, stocks was bought. I think we can explain US bullish sentiment this way.

Putting aside energy related equities fall, after 10:00 am market tone was rather bullish. However approaching September's high buy orders ceased but market was later dragged by the Korean stock market which rebounded despite the North Korea nuclear test trial announcement. This looks a play of words but the 4<sup>th</sup> of October was named 'the investment day'. Up to last year this very day's special feature was to close in positive territory every year, today ended in failure. Downside for small caps index (-1.80%) and mid caps index (-1.47%) was more severe than large caps index (-0.61%), someone probably launched sell baskets on TOPIX.

This said I do not believe the Japanese market will weaken. Providing US market does not loose its momentum then Yen should remain weak on the basis of US Japan rates differential. Based on the low yield spread it is unconceivable to reduce equities

position.

With a bit of luck there will be numerous companies revising upward earnings and dividends at interim stage, in addition to guard against unwelcome M&A stocks buy backs should increase. With baby boomers retirement rush by the end of the year fund management needs will be noticed again.

US stocks are note relatively high. Provided current bullish tone continues global investors have no specific reason to lower US stocks weighting. Globally funds scale is still expanding and out of half new funds to be invested in equities 10 % are dedicated to the Japanese market. Foreigners expected buying amount for October December period should be at par with years 2003 and 2004 at 2 trillion yen (2005 stand out with 4 trillion yen net buying). This falls in the quasi sure category.

Excessive consideration for the national assembly's factions will prove current cabinet Achilles' heel.

I looked at national assembly questions session, the new cabinet (or rather post Koizumi LDP) looks like a 'glasswork'. New cabinet's policy course does not seem to be more than wishful thinking. Showing a face able to win in the house of councilor's election was a prerequisite for the new prime minister. By reflex he opposed consumption tax problem debate and to gain maximum popular support he totally bypassed pension and revenue source structure debate. It is a well known fact that Abe's strong point is not economy and he had to avoid by all means digging his own grave by entering the debate. For such reasons Abe used catch phrases like 'high nominal growth rate', 'new challenges', 'financial spending brake'.

However tough Chief Secretary Nakagawa Hidenao speaks, that won't give a chance to raise the offense considering he is raising a misplaced logic.

Increase nominal growth rate and curb public expenses altogether is nonsense in terms of political target, turn it upside down if you want that's unfeasible. According to text books you need an expansionary fiscal policy to increase nominal growth rate. Thanks to recent economic growth, tax revenues expanded but leniency increased too. Should nominal growth rate expand then tax revenues will grow therefore to sustain it is no problem to forego the consumption tax controversy is a type of white lie.

'A society meeting new challenges' catchphrase also looks suspicious. In case of failure

the government has to shoulder the incumbent debts. Can living unconditionally under public assistance be allowed? People who started a new business and failed, took Debt and staged a comeback are only those filing the three following conditions: one's nature is above average, debt scale is small compared to age and employment status is good.

IT industry seems to fit in such conditions however I do not believe it goes that smoothly for other industries. The government cannot guarantee economy ascent. If government does not take ample financing measures the 'let's challenge it!' philosophy is merely irresponsibility.

I feel that consumption tax ever-postponement is dangerous. Consumption tax is just taxes and pensions redistributed part. Nakagawa chief secretary is actively repeating that increasing value added tax will reduce economic growth rate. It is clear that increasing VAT rate implies a slowdown the following year but there is no data sustaining those countries with high value added tax rate registered lower than average growth rate. Please see the link for main OECD countries consumption tax rate <http://www.mof.go.jp/jouhou/syuzei/siryoku/102.htm>.

By not making clear allowances and revenue source for social security and pension the government will increase the number of people who do not use money despite having enough reserves. I feel a lot of old and middle age persons would appreciate consumption tax rate to be openly raised in order to protect revenue source.