Foreign Investors totally sidelined for now.

But shareholder's activism continues to make inroads in Japan. Market supported by individual's high yield stocks purchase in September.

According to the last Merrill Lynch September survey of world fund managers the number of respondents overweighting Japan has fallen since June from 60% to less than 40 %. More interesting, Hedge Funds who actively invested in Japanese stocks in late 2005 have been doing poorly respective to Japanese indexes (according to Singapore Eureka Hedge Fund database). There is an informal 'Tokyo Hedge Fund Club' launched in June 2005 where Tokyo based Hedge Fund analyst/researchers teams gather once a year. Although more than 200 participants attended June 2006 session, this time not a single fund manager himself could be spotted! The fizzle has gone. In fact most foreign investors shall stay sidelined until Koizumi successor can demonstrate his willingness to continue the reforms. Some foreign asset managers also argue that Japan now trading at 19 times 2007 earnings is not undervalued anymore on a worldwide basis (US stocks trade at 15 times 07 forecasted earnings, Europe at 12-13 times 07 earnings). But I believe this logic bypasses current Japanese cycle's dynamics. For now the market is supported by Japanese individuals in anticipation of high dividend payout ratio. High dividend payout ratio stocks are performing better than the overall market. Most companies closing accounts by march have to announce mid year earnings by September and pay half year dividends (half year dividends shall be paid the 25th of September for current fiscal year). The recent downtrend in long term rates (despite BOJ ZIRP end) makes high yield equities the more attractive for onshore investment trusts. By the end of august net amount invested by onshore investment trusts in such stocks has tripled at 1 trillion 249 billion Yen.

Underlying trend goes unchanged in Japan.

The Japanese Pension Fund association manages 12 trillion yen private companies' pension money (out of which 4 trillion Yen invested in Japanese equities with 30 % managed in house). JPF has totally revamped its organization in 2005 and is stepping up its shareholder activism campaign. As a comparison US CALPERS manages in house 50 % of its 20 trillion Yen entrusted pension money. By 2009 JPF plans to raise its specialist staff by 1.6 x in order to increase in house managed money to 70 % of its entrusted assets. Assets under management have doubled since 2001.Baby Boomers retirement is expected to increase payout.

According to the equities fund management division head Mr. Yamamoto Takashi (Nikkei Financial Daily 14th September) JPF is embarking on Shareholder activism *stage 2* by clearly opposing to the renewal of administrators mandate, should the company register three fiscal years losses in a row (US investors would be much less complacent I believe). Nevertheless such stance shows the underlying trend for management style. JPF oppositions to the management decisions at shareholder's assembly were as high as 40 % in 2003, for 2006 it went down to 22 % which shows things are changing.

Now what to buy?

'Comprehensive strengths' has not paid off for Japanese large electrical conglomerates. The Nikkei 20th September reported that the market has not highly valued the 8 large comprehensive electrical/electronic giants since 1996, although the gap is widening between (6752) matsushita and the seven others integrated electrical makers in Japan. (See template below). The disparity is clearly explained by the capacity to focus on a core industrial activity.

	Sales*	Net earnings*	Mkt. cap At 09/19/06 close	1996 Mkt cap.
Matsushita	89,500	1,900	60,713	39,900
Sony	82,300	1,300	49,399	28,428
Melco	37,000	1,200	21,214	14,814
Sharp	30,000	1,000	23,380	18,574
Toshiba	66,000	900	25,623	23,434
Fujitsu	52,000	800	19,189	19,886
NEC	49,000	500	13,658	21,683
Hitachi	97,400	- 550	22,835	35,984

Unit: 100 million Yen

- : loss

*Figures are March 2007 forecasts.

Considering current (6752) Matsushita streamlining strategy I believe long term upward momentum remains strong.

I would also pay special attention to the announcement made by (4901) Fuji Photo Film (stock already jumped in anticipation) CEO Komori Shigetaka: Fuji Photo is going to adopt the holding structure by 1st of October 06 revamping totally its management system. He also announced that for March 2007 ordinary profit would reach 200 billion Yen and forecasted that by March 2009 consolidated sales would reach 3 trillion 150 billion Yen and ordinary profit 250 billion Yen. To increase group corporate governance synergy between the different affiliates shall be strengthened, production and logistics subsidiaries will be merged. Group subsidiaries like Sankyo chemicals and Fujinon will be totally incorporated (please see my *Newsletter dated 29th of august*), CSR (consolidated Cash Management System) will be introduced to increase group overall profitability. Komori Shigeta also announced that by 2010 the company planned to increase by 60 % sales in LCD panel's filters and optical disks in anticipation of slower growth for digital cameras. Fuji is also planning to increase 'information solutions' industrial division contribution to 45 % of total sales. Fuji Photo already ranks high within listed Japanese equities top foreign holders which explain the outlined strategy.

Finally I would invite all buy side professionals in search of potentially forward looking investment ideas in Japan to read *Kimura Dreamvisor Newsletter 19th of September* second part：China's economy 'Achilles' heel' subject. Indeed Environment protection related technology stocks weighting is high in Japanese market. Such companies would directly benefit from China's acute problems. Kurita water (6370) is an example among others.