

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

JAPAN SMALLER CAPITALIZATION FUND INC

Form N-CSR

November 03, 2004

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED MANAGEMENT

INVESTMENT COMPANIES

Investment Company Act file number: 811-05992

JAPAN SMALLER CAPITALIZATION FUND, INC.

2 World Financial Center, Building B, New York, N.Y. 10281

Nomura Asset Management U.S.A. Inc.

2 World Financial Center, Building B, New York, N.Y. 10281

Registrant's telephone number, including area code: (800) 833-0018

Date of fiscal year end: February 28, 2005

Date of reporting period: August 31, 2004

ITEM 1. REPORT TO SHAREHOLDERS

JAPAN SMALLER CAPITALIZATION FUND, INC.

To Our Shareholders:

October 26, 2004

We present the Semi-Annual Report of Japan Smaller Capitalization Fund, Inc. (the "Fund") for the six months ended August 31, 2004.

The Net Asset Value per share ("NAV") of the Fund increased by 12.9% during the six months. The closing market price of the Fund on August 31, 2004, on the New York Stock Exchange was \$11.59, representing a premium of 9.2% to the NAV of \$10.61. The net assets of the Fund amounted to \$168,076,352 on August 31, 2004.

The TOPIX, consisting of all companies listed on the Tokyo Stock Exchange (the "TSE") First Section, increased by 4.6% and the Nikkei Average Index (a price-weighted index of 225 leading stocks on the TSE) increased by 0.6%, in United States ("U.S.") dollar terms, during the six months ended August 31, 2004. The Nikkei JASDAQ Average Index (the "OTC Index"), a price-weighted index of the quotations of the OTC registered stocks, and the Index of the Japan Securities Dealers Association Quotation System (the "JASDAQ Index"), a capitalization-weighted index of all OTC stocks, increased by 20.0% and 22.7%, respectively, in U.S. dollar terms, during the same period. The Japanese yen (the "Yen") appreciated by 0.2% against the U.S. dollar during the six months.

Performance

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

The Fund underperformed the OTC Index by 7.1 percentage points during the six months ended August 31, 2004. Exposure to the semiconductor, liquid crystal display and digital consumer electronics products companies, such as Dainippon Screen Mfg., T&K Toka and Chiyoda Integre detracted from the relative performance. These stocks under-performed due to the uncertain outlook for supply-demand conditions in the semiconductor and liquid crystal display businesses, and a cautious outlook for sales of digital consumer electronics products. In addition, the underperformance was mainly attributable to the Fund's holdings such as Toysrus-Japan and Nichii Gakkan, which announced the downward revision on their outlook for this fiscal year. The Fund underperformed the JASDAQ Index by 9.8 percentage points during the same period.

The NAV of the Fund increased by 0.1% for the quarter ended August 31, 2004. During the same period, the Nikkei Average Index and the JASDAQ Index each decreased by 0.1% and 1.2%, respectively, in U.S. dollar terms. The OTC Index and the TOPIX increased by 0.1% and 0.4%, respectively. The Yen appreciated by 1.3% during the same period. The Fund outper-

formed the OTC Index by 0.1 percentage points and outperformed the JASDAQ Index by 1.3 percentage points.

The Portfolio

The Fund's equity exposure decreased from 98.5% at February 29, 2004 to 97.5% at August 31, 2004. The Fund was diversified into 114 issues, of which 61 issues were TSE First Section stocks, 11 were TSE Second Section stocks, 36 were JASDAQ stocks and 6 were other smaller capitalization stocks, comprising 53.5%, 9.9%, 27.9% and 6.2%, respectively, of net assets on August 31, 2004.

Market Review

The OTC Index gained 19.7% in local currency terms for the six months ended August 31, 2004. The OTC Index outperformed the broad Japanese stock market TOPIX index, which slightly appreciated by 4.3%.

In March, the Japanese overall market extended its rally and outperformed the U.S. and European markets. Some events had a negative impact globally, such as the terrorist attacks in Spain and the Hamas leader's assassination in Israel. However, favorable domestic macroeconomic data and expectations of an end to deflation outweighed the negative news and supported the view that the Japanese economy could be on course for a steady expansion.

In April, the broad TOPIX Index extended its rally through the beginning of April based on strong Tankan survey results. However, the stock market began to consolidate again by the month end. Stock prices stumbled following the release of strong employment data in the U.S. that raised concerns of an eventual interest rate increase from the Federal Reserve. The market also responded to fears that the Chinese authorities might tighten policy in an attempt to rein in the country's overheating economy. Meanwhile, the OTC Index continued to extend their rally during the month and outperform the TOPIX Index by considerable margin because of its lower sensitivity to many of the troubles that had overshadowed the main market, such as monetary policy in the U.S. and the economic slowdown in China.

In the Japanese stock market, consolidation took hold until mid-May based on concerns about the possible impact of an eventual interest rate increase

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

from the Federal Reserve. Apprehension over rising oil prices and the regional impact of austerity measures to rein in the growth of China's economy also undermined investor sentiment. Nevertheless, the Japanese over all stock market was able to make up for the early losses toward the end of June, helped by favorable macro economic figures. The rising U.S. stock market and the easing of crude oil prices provided further support for the Japanese overall market.

In July, the OTC Index declined, erasing most of the gains earned in June as a result of profit-taking activity following a sharp rise in share prices since the beginning of this year. Although a favorable set of Tankan survey results was issued right at the beginning of the month, the market failed to react to the positive news. Instead, the Japanese stock market succumbed

to the negative impact of a return to rising oil prices, the decline in the U.S. stock market that followed the negative June employment data results, and the weak earnings results issued by some consumer electronics companies.

In August, the OTC Index mostly traded in parallel with the broad Japanese stock market. The Japanese stock market extended its decline through to the middle of the month amid very low summer trading volume. Discouraging April-June real GDP data (the preliminary estimates) for Japan pushed the Tokyo market lower. Meanwhile, disappointing figures for U.S. real GDP and employment, plus soaring oil prices, together overshadowed the U.S. stock market and also damaged investor sentiment in Japan. Pessimism started to evaporate later in August and the Japanese stock market climbed higher for ten consecutive trading days partly as a result of bargain hunting activity, but helped by a pause in the oil price rally and a recovery in U.S. stock prices. The Japanese stock market eventually regained most of the earlier losses.

Outlook and Strategy

Several factors that are now influencing Japanese stocks and the economy are together likely to keep the market range-bound for the time being. From a broad macro viewpoint, a more cautious consensus outlook has been emerging in relation to the global economy. Although the Fund forecasts a smaller increase in U.S. interest rates this year than the market consensus, this is mainly because the Fund is less optimistic about the growth prospects in the U.S. Although the Fund expects the American economy to resume its recovery next year, the expected slowdown will impede export growth for Japanese companies for now.

Oil prices may now be less of a threat to the Japanese economy. In relation to Japan's GDP, a \$10 increase in the price of crude oil would result in an increase in oil import costs equivalent to only 50 basis points of Japan's GDP growth. Furthermore, given that the recent surge in oil prices has been driven by speculative activity, the Fund expects them to ease towards the year-end, with the benchmark crude oil price likely to edge back below \$40 per barrel. Such a reversal would benefit the global economy and further aid the expected recovery.

However, the Fund has made no changes to GDP growth forecasts for Japan for this year and next year of 3.5% and 1.6% respectively. The slowdown in export growth as the U.S. economy struggles to regain momentum will have an impact on capital expenditure and therefore domestic demand too. Although capital spending is closely correlated with export growth, one encouraging sign is the capital coefficient (capital stock/real GDP), which is now

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

declining and suggests that the long-standing issue of overcapacity is now being resolved. Fiscal policy on the other hand is unambiguously negative for domestic demand. The rolling back of tax breaks introduced in the late 1990s and recent increases in social insurance premiums will undermine the household spending component of domestic demand over the coming months.

With so many conflicting influences, it is unlikely to see any valuation expansion for now. Given the prospect that the 10% earnings

growth expectation for this fiscal year has already been priced into the stock market, we need to see further positive developments in terms of corporate profits.

The Fund believes the current stock price consolidation will eventually uncover considerable value from a long-term investment perspective. Therefore, the Fund intends to maintain focus on long-term investment opportunities, namely the strategy remains focused on identifying and selecting oversold stocks.

We appreciate your continuing support of your Fund.

Sincerely,

Yasushi Suzuki
President

NEW PRINCIPAL INVESTMENT STRATEGY

The Fund's Shareholders approved a new Principal Investment Strategy whereby the Fund, under normal circumstances, will invest at least 80% of its total assets in smaller capitalization Japanese equity securities traded on the Tokyo, Osaka and Nagoya Stock Exchanges. JASDAQ, Mothers, Hercules, Centrex, and other indices or markets determined by Nomura Asset Management U.S.A., Inc. to be appropriate indices or markets for smaller capitalization companies in Japan ("Smaller Capitalization Companies").

A description of the policies and procedures that the Fund uses to determine how to vote proxies relating to portfolio securities is available (1) without charge, upon request, by calling toll-free 1-800-833-0018; and (2) on the Securities and Exchange Commission's web site at <http://www.sec.gov>. Information about how the Fund voted proxies relating to securities held in the Fund's portfolio during the most recent 12-month period ended June 30 is available (1) without charge, upon request, by calling toll-free 1-800-833-0018; and (2) on the Securities and Exchange Commission's web site at <http://www.sec.gov>.

SHAREHOLDERS ACCOUNT INFORMATION

Shareholders whose accounts are held in their own name may contact the Fund's transfer agent, Equiserve Trust Company, N.A. at (800) 426-5523 for information concerning their accounts.

INTERNET WEBSITE

NAM-U.S.A. has established an Internet website which highlights its history, investment philosophy and process and products, which includes the Fund. The Internet web address is www.nomura.com. We invite you to view the

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Internet website.

JAPAN SMALLER CAPITALIZATION FUND, INC.

FUND HIGHLIGHTS--AUGUST 31, 2004

(Unaudited)

KEY STATISTICS

Net Assets.....	\$168,076,3
Net Asset Value per Share.....	\$10.
Closing NYSE Market Price.....	\$11.
Percentage Change in Net Asset Value per Share*+.....	12.
Percentage Change in NYSE Market Price*+.....	7.

MARKET INDICES

Percentage change in market indices:*

	YEN ---
TOPIX.....	4.3%
Nikkei Average.....	0.4%
JASDAQ.....	22.4%
OTC.....	19.7%
*From March 1, 2004 through August 31, 2004. +Reflects the percentage change in share price.	

ASSET ALLOCATION

Japanese Equities

TSE First Section Stocks.....	53.5
TSE Second Section Stocks.....	9.9
JASDAQ Stocks.....	27.9
Other Smaller Capitalization Stocks.....	6.2
Cash and Cash Equivalents.....	2.3

Total Investments.....	99.8
Other Assets less Liabilities, Net.....	0.2

Net Assets.....	100.0
=====	

INDUSTRY DIVERSIFICATION

	% of Net Assets -----	
Services	15.1	Banks and Finance.....
Miscellaneous Manufacturing.....	12.0	Electric.....
Automotive Equipment and Parts.....	10.4	Wholesale.....

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Chemicals and Pharmaceuticals.....	8.3	Textiles and Apparel.....
Electronics.....	7.9	Machinery and Machine Tools...
Retail.....	7.6	Iron and Steel.....
Information and Software.....	6.7	Restaurants.....
Food Manufacturing.....	5.2	Real Estate and Warehouse....
		Telecommunications.....

TEN LARGEST EQUITY HOLDINGS BY MARKET VALUE

Security

C. Uyemura & Co., Ltd.....
Arisawa Manufacturing Co., Ltd.....
Yamato Kogyo Co., Ltd.....
Musashi Seimitsu Industry Co., Ltd.....
Nissin Healthcare Food Service Co., Ltd.....
Meganesuper Co., Ltd.....
Yusen Air & Sea Service Co., Ltd.....
Nova Corporation.....
United Arrows Limited.....
Nippon Cable Systems Inc.....

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS

AUGUST 31, 2004

(Unaudited)

	Shares	Cost
	-----	----
EQUITY SECURITIES		
Automotive Equipment and Parts		
Calsonic Kansei Corporation.....	85,000	\$ 603,78
Radiators, mufflers and air conditioning systems		
Futaba Industrial Co., Ltd.....	129,800	2,214,97
Mufflers and exhaust manifolds		
Musashi Seimitsu Industry Co., Ltd.....	70,100	1,309,41
Ball joints, camshafts and gears		
Nippon Cable Systems Inc.....	186,300	1,693,75
Control cables		
Nippon Piston Ring Co., Ltd.....	537,000	1,030,11
Internal combustion engine parts		
Nissin Kogyo Co., Ltd.....	68,000	1,519,76
Brake systems		

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Nittan Valve Co., Ltd.....	296,000	1,873,25
Engine valves		
Toyoda Boshoku Corporation.....	121,200	2,219,29
Air filters, oil filters, bumpers and interior materials		
U-Shin, Ltd.....	142,000	1,006,76
Door locks		-----
Total Automotive Equipment and Parts.....		13,471,11

Banks and Finance

The Bank of Fukuoka, Ltd.....	196,000	991,483
Deposits, loans and exchange transactions		
The Hiroshima Bank, Ltd.....	256,000	1,127,041
General banking services		
The Hyakugo Bank, Ltd.....	129,000	714,364
General banking services		
Okasan Holdings, Inc.....	221,000	1,455,508
Financial services		
Ricoh Leasing Co., Ltd.....	99,600	2,268,366
Credit sales and leasing		
Sanyo Shinpan Finance Co., Ltd.....	34,700	1,898,164
Consumer financing		-----
Total Banks and Finance.....		8,454,926

Chemicals and Pharmaceuticals

Arisawa Manufacturing Co., Ltd.....	101,800	2,280,644
Glassfibers and insulating resins		
C. Uyemura & Co., Ltd.....	143,000	2,365,695
Chemicals		
Mandom Corporation.....	69,000	962,431
Cosmetic products		

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS--Continued

AUGUST 31, 2004

(Unaudited)

Shares Cost

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

	-----	-----
Matsumoto Yushi-Seiyaku Co., Ltd.....	11,500	\$ 215
Analgesic anti-inflammatory agents		
Shizuokagas Co., Ltd.....	366,000	1,024
Natural gas supplier		
T & K Toka Co., Ltd.....	90,400	1,456
Ink for printing		
Towa Pharmaceutical Co., Ltd.....	26,200	537
Generic drugs		-----
Total Chemicals and Pharmaceuticals.....		8,842

Electric		
Citizen Electronics Co., Ltd.....	41,800	1,275
Electric parts		
Eneserve Corporation.....	44,400	1,008
Electric generation system for supermarkets		
Mirai Industry Co., Ltd.....	261,000	2,586
Plastic molded electric materials		-----
Total Electric.....		4,870

Electronics		
Chiyoda Integre Co., Ltd.....	98,520	913
Electronic components		
Cosel Co., Ltd.....	76,500	1,986
Electrical machinery		
Dainippon Screen Mfg. Co., Ltd.....	338,000	1,499
Electronic components		
Fuji Electric Industry Co., Ltd.....	44,200	465
Electronic parts		
Fukuda Denshi Co.....	39,000	961
Medical electronic equipment		
Kuroda Electric Co., Ltd.....	60,700	738
Materials and components		
Mimasu Semiconductor Industry Co., Ltd.....	113,800	1,802
Semiconductor materials		
Sumisho Electronics Co., Ltd.....	71,200	923
Office systems		
Toshiba Tec Corp.....	236,000	961
Electronic equipment manufacturing		-----
Total Electronics.....		10,252

Food Manufacturing		
Arcs Co., Ltd.....	123,480	1,215
Supermarket chain		
Ariake Japan Co., Ltd.....	39,083	739
Natural seasonings		

See notes to financial statements

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS--Continued

AUGUST 31, 2004

(Unaudited)

	Shares -----	Cost -----
Kakiyasu Honten Co., Ltd.....	80,600	\$ 674
Processed meat products, fresh meats, and side dishes		
Nippon Flour Mills Co., Ltd.....	272,000	1,240
Flour and grain		
Ozeki Co., Ltd.....	24,000	1,132
Supermarket chain		
Plenus Co., Ltd.....	71,560	1,779
Japanese lunch-boxes		
Q'sai Co., Ltd.....	125,000	522
Frozen and processed foods and juice drinks		-----
Total Food Manufacturing.....		7,305

Information and Software		
Argo Graphics Inc.....	72,000	896
Computer aided design software		
Daiwabo Information System Co., Ltd.....	99,000	1,277
Develops and sells personal computers and softwares		
Index Corporation.....	216	75
Cellular phone, internet content		
Jastec Co., Ltd.....	6,800	90
Business application software		
Konami Computer Entertainment Tokyo, Inc.....	82,900	870
Video games software		
NEC Mobilling, Ltd.....	72,400	2,077
Software for mobile telecommunication systems		
Netmarks, Inc.....	145	806
Designing, developing and building network systems		
Net One Systems Co., Ltd.....	436	1,673
Designs, installs, maintains, and sells computer network systems		
Trend Micro Inc.....	19,500	1,488
Computer software, anti-virus server		
Works Applications Co., Ltd.+.....	280	529
Software development		-----
Total Information and Software.....		9,788

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Iron and Steel

Nisshin Steel Co., Ltd.....	520,000	1,092,3
Steel producers		
Yamato Kogyo Co., Ltd.....	252,000	3,361,0
Steel producers		-----
Total Iron and Steel.....		4,453,3

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS--Continued

AUGUST 31, 2004

(Unaudited)

	Shares	Cost
	-----	----
Machinery and Machine Tools		
Nihon Ceratec Co., Ltd.....	141	\$ 673,3
Ceramics for semiconductors		
Shinkawa Ltd.....	6,400	125,5
Bonders and semiconductors		
THK Co., Ltd.....	117,400	3,342,2
Linear motion systems for industrial machines		
Tsubaki Nakashima Co., Ltd.....	85,500	1,092,8
Bearing balls, blowers and precision ball screws		
Yamazen Corporation.....	412,000	1,259,7
Machinery and tools		-----
Total Machinery and Machine Tools.....		6,493,6

Miscellaneous Manufacturing		
Central Glass Co., Ltd.....	297,000	1,565,5
Glass products		
Dynic Corporation +.....	379,000	1,210,4
Bookbinding cloth		
Fuji Seal, Inc.....	2,050	36,7
Packing materials		
Fujimi Inc.....	6,400	110,6
Polishing materials for silicone wafers		
JSP Corporation.....	125,000	1,832,3

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Polystyrene products		
Kansai Paint Co., Ltd.....	170,000	1,071,8
Manufactures and sells a wide range of paints		
Kitagawa Industries Co., Ltd.....	26,400	380,3
Metal products and fasteners		
Mani, Inc.....	79,800	1,378,3
Medical goods and equipment		
Mizuno Corporation.....	184,000	670,6
Sporting goods		
Nichiha Corporation.....	134,600	1,209,8
Ceramic exterior walls and fiber boards		
Nippon Kodoshi Corp.....	188,000	2,839,3
Paper for electric insulation		
Onkyo Corp.....	64,000	284,0
Multi-media products		
Riso Kagaku Corporation.....	38,600	1,486,5
Printing and copying machines		
Sanei-International Co., Ltd.....	35,000	1,299,2
Fashion apparel		
Secom Techno Service Co., Ltd.....	44,000	1,176,9
Security systems, provides maintenance service		

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS--Continued

AUGUST 31, 2004

(Unaudited)

	Shares -----	Cost ----
SK Kaken Co., Ltd.....	54,500	\$ 1,291,3
Paints		
Suruga Co., Ltd.....	1,500	22,8
Daily necessities, novelties and promotional items		-----
Total Miscellaneous Manufacturing.....		17,867,2

Real Estate and Warehouse		
Leopalace21 Corporation.....	89,000	865,6
Builds, repairs, sells, leases and manages real estate properties		
Recrm Research Co., Ltd.....	625	806,2
Building management		-----
Total Real Estate and Warehouse.....		1,671,8

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Restaurants

Saint Marc Co., Ltd.....	66,100	2,137,3
Restaurants and bakery shop chain		
Y's Table Corporation +.....	150	653,9
Operates a variety of restaurants		
Total Restaurants.....		2,791,3

Retail

Art Vivant Co.,Ltd.....	98,000	783,6
Arts and crafts		
Askul Corporation.....	28,400	1,419,2
Catalog shopping		
Cawachi Limited.....	44,800	1,241,8
Drug store chain		
Edion Corporation.....	54,200	276,5
Consumer electronics		
Kitamura Co., Ltd.....	102,000	805,4
Consumer electronics		
Meganesuper Co., Ltd.....	152,300	2,597,2
Eye glasses chain		
Nitori Co., Ltd.....	6,360	182,9
Home furnishings		
USS Co., Ltd.....	20,890	484,0
Automobile auction		
Village Vanguard Co., Ltd.+.....	107	874,8
Books, cd's, videos and office supplies		
Xebio Co., Ltd.....	31,400	892,2
Sporting goods		
Total Retail.....		9,558,0

Services

Alps Logistics Co., Ltd.....	89,000	625,4
Transportation		

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS--Continued

AUGUST 31, 2003

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

(Unaudited)

	Shares -----	Cost -----
Daiwa Logistics Co., Ltd.....	26,000	\$ 198,8
Transports housing materials and building steel frames		
Fullcast Co., Ltd.....	728	608,3
Human resources		
Hitachi Transport System, Ltd.....	98,000	739,4
Freight truck and marine transportation		
Nissin Healthcare Food Service Co., Ltd.....	161,100	1,976,4
Nursing home caterer		
Nova Corporation.....	255,000	1,184,7
Language instruction courses		
Okinawa Cellular Telephone Company.....	177	1,627,6
Cellular and car phone services		
Pasona Inc.....	167	166,1
Human resources		
Sumisho Auto Leasing Corporation.....	38,400	1,448,9
Auto leasing and maintenance		
TKC Corporation.....	21,000	356,1
Consulting services		
Toei Animation Co., Ltd.....	28,300	1,447,0
Animated cartoon movies production		
Tohokushinsha Film Corporation.....	79,800	1,254,7
Produces tv programs, movies and commercial films		
Tokyo Individualized Educational Institute, Inc.....	111,600	1,529,8
Individual guidance system for elementary to high school students		
Toppan Forms Co., Ltd.....	105,200	1,113,8
Commercial printing		
Tow Co., Ltd.....	217,700	1,355,0
Entertainment		
Yusen Air & Sea Service Co., Ltd.....	80,600	2,465,5
Domestic and international air freight forwarding		
Total Services.....		18,098,4

Telecommunications		
Forval Corporation.....	140,200	1,624,0
Telecommunication equipment		

Textiles and Apparel		
United Arrows Limited.....	114,600	1,132,8
Casual clothes		
Workman Co., Ltd.....	68,000	1,229,1
Uniforms		
World Co., Ltd.....	27,200	890,2
Apparel manufacturers		

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Total Textiles and Apparel..... 3,252,1

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

SCHEDULE OF INVESTMENTS--Continued

AUGUST 31, 2004

(Unaudited)

	Shares	Cost
	-----	----
Wholesale		
ArcLand Sakamoto Co., Ltd.....	76,400	\$ 855,2
Home appliances		
Kato Sangyo Co., Ltd.....	146,000	1,099,1
Processed foods		
Paltac Corporation.....	50,000	419,8
Cosmetics, toiletries, and other consumer goods		
Toba, Inc.....	21,500	203,1
Trading company for control systems		
Toshin Denki Co., Ltd.....	62,600	789,8
Lighting equipment and electrical engineering materials		-----
Total Wholesale.....		3,367,2

TOTAL INVESTMENTS IN EQUITY SECURITIES.....		132,162,5

INVESTMENTS IN FOREIGN CURRENCY	Principal Amount	

Hong Kong Shanghai Bank-Tokyo		
Non-interest bearing account.....	JPY421,313,144	\$ 3,849,5

TOTAL INVESTMENTS IN FOREIGN CURRENCY.....		3,849,5

TOTAL INVESTMENTS.....		136,012,1

OTHER ASSETS LESS LIABILITIES, NET.....		332,1

NET ASSETS.....		\$136,334,3
		=====

+Non-income producing security

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Portfolio securities and foreign currency holdings were translated
at the following exchange rate as of August 31, 2004.

Japanese Yen JPY (Y) 108.985 = \$1.00

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

STATEMENT OF ASSETS AND LIABILITIES

AUGUST 31, 2004

(Unaudited)

ASSETS:

Investments in securities, at market value (cost--\$132,162,576)	\$16
Investments in foreign currency, at market value (cost--\$3,849,554)	
Receivable for investments sold	
Receivable for dividends and interest, net of withholding taxes	
Prepaid expenses	
Cash or cash equivalent	
Total Assets	17

LIABILITIES:

Payable for investments purchased	
Accrued management fee	
Other accrued expenses	
Total Liabilities	

NET ASSETS:

Capital stock (par value of 15,846,384 shares of capital stock outstanding, authorized 100,000,000, par value \$0.10 each)	16
Paid-in capital	(3)
Accumulated net realized loss on investments and foreign currency transactions	3
Unrealized net appreciation on investments and foreign exchange	
Accumulated net investment loss	
Net Assets	\$16

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Net asset value per share.....

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

STATEMENT OF OPERATIONS

FOR THE SIX MONTHS ENDED AUGUST 31, 2004

(Unaudited)

INCOME:

Dividend income (less \$74,173 withholding taxes).....	\$,024,029
Interest income.....	4,380

Total Income.....	\$1,028,409

EXPENSES:

Management fee.....	845,958
Legal fees.....	93,298
Custodian fees.....	77,775
Directors' fees and expenses.....	47,300
Auditing and tax reporting fees.....	32,166
Shareholder reports.....	23,181
Registration fees.....	16,734
Annual meeting expenses.....	15,873
Transfer agency fees.....	11,950
Miscellaneous.....	4,968
Insurance.....	3,261

Total Expenses.....	1,172,464

INVESTMENT LOSS--NET.....	(144,055)

REALIZED AND UNREALIZED GAIN/(LOSS) ON INVESTMENTS AND FOREIGN CURRENCY:

Realized gain/(loss) on investments and foreign currency transactions:	
Net realized gain on investments.....	2
Net realized gain on foreign exchange.....	3

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Net realized gain/(loss) on investments and foreign exchange.....	6
Change in net unrealized appreciation/(depreciation) on translation of foreign currency and other assets and liabilities denominated in foreign currency.....	(3) 15
Change in net unrealized appreciation on investments.....	---
Net realized and unrealized gain on investments and foreign exchange.....	19
NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS.....	\$19
	==

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

STATEMENT OF CHANGES IN NET ASSETS

	For the Six Months Ended August 31, 2004 (Unaudited) -----	For the Year Ended February 29, -----
FROM INVESTMENT ACTIVITIES:		
Net investment income/(loss)	\$ (144,055)	\$ (499,221)
Net realized gain/(loss) on investments	2,954,654	(5,808,231)
Net realized gain/(loss) on foreign exchange.....	3,476,040	(1,558,350)
Change in net unrealized appreciation/(depreciation) on investments and foreign exchange	12,777,836	65,948,080
	-----	-----
Increase in net assets derived from operations	19,064,475	58,082,278
	-----	-----
NET ASSETS:		
Beginning of period.....	149,011,877	90,929,599
	-----	-----
End of period	\$168,076,352	\$149,011,877
	=====	=====

See notes to financial statements

JAPAN SMALLER CAPITALIZATION FUND, INC.

NOTES TO FINANCIAL STATEMENTS (Unaudited)

1. Significant Accounting Policies

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

Japan Smaller Capitalization Fund, Inc. (the "Fund") is registered under the Investment Company Act of 1940 as a non-diversified, closed-end management investment company. The Fund was incorporated in Maryland on January 25, 1990 and investment operations commenced on March 21, 1990. The Fund issued to its shareholders of record as of the close of business on October 25, 1999 nontransferable Rights to subscribe for up to an aggregate of 3,804,940 shares of Common Stock of the Fund at a rate of one share of Common Stock for three Rights held ("Primary Subscription"). The Fund had the ability to increase the number of shares subscribed for in this offering by up to 25% of the Primary Subscription, or an additional 951,235 shares, to honor record date shareholder requests to purchase more shares. During November 1999, the Fund issued a total of 4,458,565 shares of Common Stock on exercise of such Rights at the subscription price of \$11.99 per share, compared to a net asset value per share of \$16.20 and a market value per share of \$12.6875. Additionally, a sales load of 3.75% was charged to each share issued. Right offering costs of approximately \$546,000 and the sales load were charged directly against the proceeds of the Rights Offering. The following is a summary of significant accounting policies followed by the Fund.

(a) Valuation of Securities--Investments traded in the over-the-counter market are valued at the last reported sales price as of the close of business on the day the securities are being valued or, if none is available, at the mean of the bid and offer price at the close of business on such day or, if none is available, the last reported sales price. Portfolio securities which are traded on stock exchanges are valued at the last sales price on the principal market on which securities are traded or lacking any sales, at the last available bid price. Short-term debt securities which mature in 60 days or less are valued at amortized cost if their original maturity at the date of purchase was 60 days or less, or by amortizing their value on the 61st day prior to maturity if their term to maturity at the date of purchase exceeded 60 days. Securities and other assets for which market quotations are not readily available are valued at fair value as determined in good faith by or under the direction of the Board of Directors of the Fund.

(b) Foreign Currency Transactions -- Transactions denominated in Japanese yen are recorded in the Fund's records at the current prevailing rate at the time of the transaction. Asset and liability accounts that are denominated in Yen are adjusted to reflect the current exchange rate at the end of the period. Transaction gains or losses resulting from changes in the exchange rate during the reporting period or upon settlement of foreign currency transactions are included in operations for the current period.

The net assets of the Fund are presented at the exchange rate and market values at the end of the period. The Fund does not isolate that portion of the change in unrealized appreciation (depreciation) included in the statement of operations arising as a result of changes in Yen rates at August 31, 2004 on investments and other assets and liabilities. Net realized foreign exchange gains or losses includes gains or losses arising from sales of portfolio securities, sales and maturities of short-term securities, currency gains or losses realized between the trade and settlement dates on securities transactions, the difference between the amounts of dividends, interest, and foreign withholding taxes recorded on the Fund's books, and the U.S. dollar equivalent of the amounts actually received or paid.

(c) Security Transactions, Investment Income and Distributions to Shareholders--Security transactions are accounted for on the trade date. Dividend income and distributions are recorded on the exdividend date and interest income is recorded on the accrual basis. Realized gains and losses on the sale of investments are calculated on the identified cost basis.

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

JAPAN SMALLER CAPITALIZATION FUND, INC.

NOTES TO FINANCIAL STATEMENTS (Unaudited)--Continued

Distributions from net investment income and net realized gains are determined in accordance with Federal income tax regulations, which may differ from generally accepted accounting principles. To the extent these "book/tax" differences are permanent in nature (i.e., that they result from other than timing of recognition--"temporary"), such accounts are reclassified within the capital accounts based on their Federal tax-basis treatment; temporary differences do not require reclassification. Dividends and distributions which exceed net realized gains for financial reporting purposes, but not for tax purposes, are reported as distributions in excess of net realized gains.

(d) Income Taxes -- A provision for United States income taxes has not been made since it is the intention of the Fund to qualify as a regulated investment company under the Internal Revenue Code and to distribute within the allowable time limit all taxable income to its shareholders.

Under Japanese tax laws, a withholding tax is imposed on dividends at a rate of 7% and on interest at a rate of 10% and such withholding taxes are reflected as a reduction of the related revenue. There is no withholding tax on realized gains.

(e) Capital Account Reclassification -- For the yearended February 29, 2004, the Fund's accumulated net realized loss was increased by \$853 and paid in capital was decreased by \$498,368, with an offsetting decrease in accumulated net investment loss of \$499,221. This adjustment was primarily the result of the reclassification of foreign currency gains and reclassification of the net operating loss.

(f) Use of Estimates in Financial Statement Preparation -- The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from these estimates.

(g) Concentration of Risk -- A significant portion of the Fund's net assets consists of Japanese securities which involve certain considerations and risks not typically associated with investments in the United States. In addition to the smaller size, and greater volatility of the market, there is often substantially less publicly available information about Japanese issuers than there is about U.S. issuers. Future economic and political developments in Japan could adversely affect the value of securities in which the Fund is invested. Further, the Fund may be exposed to currency devaluation and other exchange rate fluctuations.

(h) Indemnifications--Under the Fund's organizational documents its officers and directors are indemnified against certain liabilities arising from the performance of their duties to the Fund. Additionally, in the normal course of business, the Fund enters into contracts that contain a variety of representations which provide general indemnifications. The Fund's maximum exposure under these agreements is unknown as this would involve future claims that may be made against the Fund that have not yet occurred. However, based on experience, the Fund expects the risk of loss to be remote.

2. Management Agreement and Transactions With Affiliated Persons

Nomura Asset Management U.S.A. Inc. (the "Manager") acts as the manager

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

of the Fund pursuant to a management agreement. Under the agreement, the Manager provides all office space, facilities and personnel necessary to perform its duties. Pursuant to such management agreement, the Manager has retained its parent company, Nomura Asset Management Co., Ltd. (the "Investment Adviser"), to act as investment adviser for the Fund.

As compensation for its services to the Fund, the Manager receives a monthly fee at the annual rate of

JAPAN SMALLER CAPITALIZATION FUND, INC.

NOTES TO FINANCIAL STATEMENTS (Unaudited)--Continued

1.10% of the value of the Fund's average weekly net assets not in excess of \$50 million, 1.00% of the Fund's average weekly net assets in excess of \$50 million but not exceeding \$100 million, .90% of the Fund's average weekly net assets in excess of \$100 million but not in excess of \$175 million and .80% of the Fund's average weekly net assets in excess of \$175 million. For services performed under the Investment Advisory Agreement, the Investment Adviser receives a monthly fee from the Manager at the annual rate of .50% of the Fund's average weekly net assets not in excess of \$50 million, .45% of the Fund's average weekly net assets in excess of \$50 million but not in excess of \$100 million, .40% of the Fund's average weekly net assets in excess of \$100 million but not in excess of \$175 million and .35% of the Fund's average weekly net assets in excess of \$175 million. Under the Management Agreement, the Fund accrued fees to the Manager of \$845,958 for the six months ended August 31, 2004. Under the Investment Advisory Agreement, the Manager informed the Fund that the Investment Adviser earned fees of \$380,441 for the six months ended August 31, 2004. At August 31, 2004, the fee payable to the Manager, by the Fund, was \$133,202.

Certain Officers and/or Directors of the Fund are officers and/or directors of the Manager. Nomura Holdings, Inc. (the Manager's indirect parent) and affiliates earned \$0 in commissions on the execution of portfolio security transactions for the six months ended August 31, 2004. The Fund pays each Director not affiliated with the Manager an annual fee of \$10,000 plus \$1,000 per meeting attended, together with such Director's actual expenses related to attendance at meetings. Such fees and expenses for unaffiliated Directors aggregated \$47,300 for the six months ended August 31, 2004.

3. Purchases and Sales of Investments

Purchases and sales of investments, exclusive of investments in foreign currencies and short-term securities, for the six months ended August 31, 2004 were \$65,979,018 and \$68,024,784, respectively.

As of August 31, 2004, net unrealized appreciation on investments exclusive of investments in foreign currency and short-term securities for Federal income tax purposes was \$31,725,656 of which \$37,976,524 related to appreciated securities and \$6,250,868 related to depreciated securities. The aggregate cost of investments, exclusive of investments in foreign currencies and short-term securities of \$3,849,554 at August 31, 2004 for Federal income tax purposes was \$132,162,576. The Fund has a capital loss carryforward as of February 29, 2004 of approximately \$38,594,0665 of which \$22,683,799 expires February 28, 2010, \$6,143,866 expires February 28, 2011 and \$9,766,401 expires February 29, 2012.

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

JAPAN SMALLER CAPITALIZATION FUND, INC.

NOTES TO FINANCIAL STATEMENTS--Continued

FINANCIAL HIGHLIGHTS

Selected per share data and ratios for a share of common stock outstanding throughout the period.

			For the Year Ended	
	For the Six Months ended August 31, 2004 (Unaudited)	February 29, 2004	February 2003	February 2002
Net asset value, beginning of period.....	\$9.40	\$5.74	\$5.86	\$7.10
Rights offering costs*.....	--	--	--	--
Net investment loss @.....	(0.01)	(0.03)	(0.05)	(0.07)
Net realized and unrealized gain (loss) on investments and foreign currency.....	1.22	3.69	(0.07)	(1.10)
Total from investment operations.....	1.21	3.66	(0.12)	(1.17)
Distributions to shareholders from:				
Net realized capital gains.....	--	--	--	(0.01)
Net investment income.....	--	--	--	--
Total distributions.....	0.00	0.00	(0.00)	(0.01)
Decrease in net asset value due to shares issued through rights offering*.....	--	--	--	--
Net asset value, end of period.....	\$10.61	\$9.40	\$5.74	\$5.93
Market value, end of period.....	\$11.59	\$10.79	\$6.38	\$5.93
Total investment return+.....	7.4%	69.1%	15.4%	(18.1%)
Ratio to average net assets/supplemental data:				
Net assets, end of period (in 000).....	\$168,076	\$149,012	\$90,930	\$92,800
Operating expenses.....	1.37%+	1.47%	1.63%	1.50%
Net investment loss.....	(0.17%)+	(0.41%)	(0.75%)	(0.80%)
Portfolio turnover.....	40%	28%	28%	30%

+Based on market value per share, adjusted for reinvestment of income dividends and long term capital gain distributions, and capital share transactions. Total return does not reflect sales commissions.

*Decrease is due to rights offering (see note 1).

@Based on average shares outstanding.

+Annualized.

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

BOARD OF DIRECTORS

William G. Barker, Jr.
William K. Grollman
Yasushi Suzuki
Chor Weng Tan
Arthur R. Taylor
John F. Wallace

OFFICERS

Yasushi Suzuki, President
Kiyoharu Ikeda, Vice President
Kenneth L. Munt, Vice President
Rita Chopra-Brathwaite, Treasurer
Neil A. Daniele, Secretary

MANAGER

Nomura Asset Management U.S.A. Inc.
2 World Financial Center, Building B
New York, New York 10281
Internet Address
www.nomura.com

INVESTMENT ADVISER

Nomura Asset Management Co., Ltd.
1-12-1-Chome Nihonbashi, Chuo-ku,
Tokyo 103-8260, Japan

DIVIDEND PAYING AGENT, TRANSFER AGENT AND REGISTRAR

Equiserve Trust Company, N.A.
P.O. Box 43011
Providence, RI 02940-3011

CUSTODIAN

Brown Brothers Harriman & Co.
40 Water Street
Boston, Massachusetts 02109

COUNSEL

Sidley Austin Brown & Wood LLP
787 Seventh Avenue
New York, New York 10019

INDEPENDENT ACCOUNTANTS

PricewaterhouseCoopers LLP
300 Madison Avenue
New York, New York 10017

JAPAN SMALLER CAPITALIZATION FUND, INC.
2 WORLD FINANCIAL CENTER, BUILDING B,
NEW YORK, NEW YORK 10281

This Report, including the Financial Statements, is transmitted to the Shareholders of Japan Smaller Capitalization Fund, Inc. for their information. This is not a prospectus, circular or representation intended for use in the purchase of shares of the Fund or any securities mentioned in the Report.

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

The accompanying Financial Statements, including the Schedule of Investments, have not been examined by the Fund's independent accountants, PricewaterhouseCoopers LLP, and accordingly, they express no opinion thereon.

=====

JAPAN
Smaller Capitalization
Fund, Inc.

SEMI-ANNUAL REPORT

AUGUST 31, 2004

=====

ITEM 2. CODE OF ETHICS

Not Applicable to this semi-annual report

ITEM 3. AUDIT COMMITTEE FINANCIAL EXPERT

Not Applicable to this semi-annual report

ITEM 4. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Not Applicable to this semi-annual report

ITEM 5. AUDIT COMMITTEE OF LISTED REGISTRANTS

Not Applicable to this semi-annual report

ITEM 6. SCHEDULE OF INVESTMENTS

Not Applicable

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

ITEM 7. DISCLOSURE OF PROXY VOTING POLICIES AND PROCEDURES FOR CLOSED-END MANAGEMENT INVESTMENT COMPANIES

Not Applicable to this semi-annual report

ITEM 8. PURCHASES OF EQUITY SECURITIES BY CLOSED-END MANAGEMENT INVESTMENT COMPANY AND AFFILIATED PURCHASERS

Not Applicable

ITEM 9. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not Applicable

ITEM 10. CONTROLS AND PROCEDURES

- (a) The Registrant's Principal Executive Officer and Principal Financial Officer have evaluated the Registrant's disclosure controls and procedures within 90 days of the filing of this report and have concluded that they are effective in providing reasonable assurance that the information required to be disclosed by the Registrant in its reports or statements filed under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission.
- (b) There were no changes in the Registrant's internal control over financial reporting that occurred during the Registrant's last fiscal half-year (the Registrant's second fiscal half-year in the case of an annual report) that have materially affected, or are reasonably likely to materially affect, the Registrant's internal control over financial reporting.

ITEM 11. EXHIBITS

- (a) (1) Not Applicable to this semi-annual report
- (a) (2) Certifications of Principal Executive Officer and Principal Financial Officer pursuant to Rule 30a-2 under the Investment Company Act of 1940 are attached hereto as an exhibit.

- (a) (3) Not applicable.
- (b) Certifications pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 are furnished herewith as an exhibit.

Edgar Filing: JAPAN SMALLER CAPITALIZATION FUND INC - Form N-CSR

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Japan Smaller Capitalization Fund, Inc.

By: /s/ Yasushi Suzuki

Yasushi Suzuki, President
(Principal Executive Officer)

Date: November 3, 2004

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

By: /s/ Yasushi Suzuki

Yasushi Suzuki, President
(Principal Executive Officer)

Date: November 3, 2004

By: /s/ Neil A. Daniele

Neil A. Daniele, Assistant Treasurer
(Principal Financial Officer)

Date: November 3, 2004