

JAPAN EQUITY FUND INC
Form N-CSR
January 05, 2012

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 811-06142

THE JAPAN EQUITY FUND, INC.

(Exact name of registrant as specified in charter)

c/o Daiwa Securities Trust Company
One Evertrust Plaza, 9th Floor
Jersey City, New Jersey 07302-3051

(Address of principal executive offices) (Zip code)

c/o Daiwa Securities Trust Company
One Evertrust Plaza, 9th Floor
Jersey City, New Jersey 07302-3051

(Name and address of agent for service)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (201) 915-3054

DATE OF FISCAL YEAR END: October 31

DATE OF REPORTING PERIOD: October 31, 2011

Item 1. Reports to Stockholders.

The Japan Equity Fund, Inc.

General Information (unaudited)

The Fund

The Japan Equity Fund, Inc. (the "Fund") is a diversified, closed-end management investment company. The investment objective of the Fund is to outperform over the long term, on a total return basis (including appreciation and dividends), the Tokyo Stock Price Index ("TOPIX"), a composite market-capitalization weighted index of all common stocks listed on the First Section of the Tokyo Stock Exchange ("TSE"). The Fund seeks to achieve its investment objective by investing substantially all of its assets in equity securities of companies listed on the TSE or listed on the over-the-counter market in Japan or listed on other stock exchanges in Japan. Daiwa SB Investments (U.S.A.) Ltd. is the Fund's Investment Manager. Daiwa SB Investments Ltd. is the Fund's Investment Adviser. The Fund implements an "active" portfolio management policy, which is an approach that involves quantitative valuation of securities to identify an appropriate universe of securities from which to select investments, with judgmental analysis then applied to this universe to determine the actual investments to be made by the Fund.

Stockholder Information

The Fund's shares are listed on the New York Stock Exchange ("NYSE"). The Fund understands that its shares may trade periodically on certain exchanges other than the NYSE, but the Fund has not listed its shares on those other exchanges and does not encourage trading on those exchanges.

The Fund's NYSE trading symbol is "JEQ". The Fund's daily net asset value ("NAV") is available by visiting www.daiwast.com or calling (800) 933-3440 or (201) 915-3020. Also, the Fund's website includes press releases, a monthly market review and a list of the Fund's top ten industries and holdings. The Fund has also placed its Fund governance documents on its website under the section titled "Information", which includes the Fund's proxy voting policies and procedures, its code of ethics and its audit committee charter.

Inquiries

Inquiries concerning your registered share account should be directed to the American Stock Transfer & Trust Company (the "Plan Agent") at the number noted on the next page. All written inquiries should be directed to The Japan Equity Fund, Inc., c/o Daiwa Securities Trust Company, One Evertrust Plaza, 9th Floor, Jersey City, NJ 07302-3051.

Proxy Voting Policies and Procedures

A description of the policies and procedures that are used by the Fund's Manager to determine how to vote proxies relating to the Fund's portfolio securities is available (1) without charge, upon request, by calling collect (201) 915-3054; (2) by visiting www.daiwast.com; and (3) as an exhibit to the Fund's annual report on Form N-CSR which is available on the website of the Securities and Exchange Commission (the "Commission") at www.sec.gov. Information regarding how the Manager votes these proxies is now available by calling the same number and is available on the Commission's website. The Fund has filed with the Commission its report on Form N-PX covering

the Fund's proxy voting record for the 12-month period ended June 30, 2011.

Quarterly Portfolio of Investments

A Portfolio of Investments is filed with the Commission as of the end of the first and third quarters of each fiscal year on Form N-Q and is available on the Commission's website at www.sec.gov and the Fund's website at www.daiwast.com. Additionally, the Portfolio of Investments may be reviewed and copied at the Commission's Public Reference Room in Washington, D.C. Information on the operation of the Public Reference Room may be obtained by calling (800) SEC-0330. The quarterly Portfolio of Investments will be made available without charge, upon request, by calling (201) 915-3054.

Certifications

The Fund's principal executive officer has certified to the NYSE that, as of June 2, 2011, he was not aware of any violation by the Fund of applicable NYSE corporate governance listing standards. The Fund also has included the certifications of the Fund's principal executive officer and principal financial officer as required by Section 302 and Section 906 of the Sarbanes-Oxley Act of 2002 in the Fund's Form N-CSR filed with the Commission for the period of this report.

Dividend Reinvestment and Cash Purchase Plan

A Dividend Reinvestment and Cash Purchase Plan (the "Plan") is available to provide Stockholders with automatic reinvestment of dividends and capital gain distributions in additional Fund shares. The Plan also allows you to make optional annual cash investments in Fund shares through the Plan Agent. A brochure fully describing the Plan's terms and conditions is available on the Fund's website at www.daiwast.com and from the Plan Agent by calling (866) 669-9904 or by writing The Japan Equity Fund, Inc., c/o the American Stock Transfer & Trust Company, Operations Center, 6201 15th Avenue, Brooklyn, NY 11219

A brief summary of the material aspects of the Plan follows:

Who can participate in the Plan? If you wish to participate and your shares are held in your name, you may elect to become a direct participant in the Plan by completing and mailing the Enrollment Authorization form on the back cover of the Dividend Reinvestment and Cash Purchase Plan Brochure to the Plan Agent. However, if your shares are held in the name of a financial institution, you should instruct your financial institution to participate in the Plan on your behalf. If your financial institution is unable to participate in the Plan for you, you should request that your shares be registered in your name, so that you may elect to participate directly in the Plan.

May I withdraw from the Plan? If your shares are held in your name and you wish to receive all dividends and capital gain distributions in cash rather than in shares, you may withdraw from the Plan without penalty at any time by contacting the Plan Agent. If your shares are held in the name of a financial institution, you should be able to withdraw from the Plan without a penalty at any time by sending written notice to your financial institution. If you withdraw, you or your financial institution will receive a share certificate for all full shares or, if you wish, the Plan Agent will sell your shares and send you the proceeds, after the deduction of brokerage commissions. The Plan Agent will convert any fractional shares to cash at the then-current market price and send you a check for the proceeds.

How are the dividends and distributions reinvested? If the market price of the Fund's shares on the payment date should equal or exceed their net asset value per share, the Fund will issue new shares to you at the higher of net asset value or 95% of the then-current market price. If the market price is lower than the net asset value per share, the Fund will issue new shares to you at the market price. If the dividends or distributions are declared and payable as cash only, you will receive shares purchased for you by the Plan Agent on the NYSE or otherwise on the open market to the extent available.

What is the Cash Purchase feature? The Plan participants have the option of making semi-annual investments in Fund shares through the Plan Agent. You may invest any amount from \$100 to \$5,000 semi-annually. The Plan Agent will purchase shares for you on the NYSE or otherwise on the open market on or about February 15th and August 15th of each year. Plan participants should send voluntary cash payments to be received by the Plan Agent approximately ten days before the applicable purchase date. The Plan Agent will return any cash payments received more than thirty days prior to the purchase date. You may withdraw a voluntary cash payment by written notice, if the notice is received by the Plan Agent not less than two business days before the investment date.

Is there a cost to participate? There are no Plan charges or brokerage charges for shares issued directly by the Fund. However, each participant will pay a service fee of \$2.50 for each investment and a pro rata portion of brokerage commissions for shares purchased on the NYSE or on the open market by the Plan Agent.

What are the tax implications? The automatic reinvestment of dividends and distributions does not relieve you of any income tax which may be payable (or required to be withheld) on such dividends and distributions. In addition, the Plan Agent will reinvest dividends for foreign participants and for any participant subject to federal backup withholding after the deduction of the amounts required to be withheld.

Please note that, if you participate in the Plan through a brokerage account, you may not be able to continue as a participant if you transfer those shares to another broker. Contact your broker or financial institution or the Plan Agent to ascertain what is the best arrangement for you to participate in the Plan.

The Japan Equity Fund, Inc.

Shareholder Letter (unaudited)

December 8, 2011

Dear Shareholders:

It is our pleasure on behalf of the Board of Directors to present the Annual Report for The Japan Equity Fund, Inc. (the "Fund") for the year ended October 31, 2011.

Market Review (November 2010 – October 2011)

In the year ended October 2011, the TOPIX Index ("TOPIX") returned -3.66% in Japanese yen ("JPY") terms. The Tokyo market, as well as Japanese society, experienced an unprecedented event in March which was undoubtedly the biggest event in the term. Before the disaster, the Tokyo market enjoyed a moderate catch-up rally. From November to February, the U.S. dollar-Japanese yen exchange rate stabilized as the loose monetary policies by the Federal Reserve Bank, including Quantitative Easing 2 ("QE2") fell in line with market expectations. Japanese corporate earnings were steady while other countries were losing growth momentum. Indeed, the Tokyo market usually benefits from the combination of anaemic global markets—boosting the relative appeal of Japanese equities—and an ebb towards strong yen conditions. The TOPIX rallied more than 17% during the first four months. Analysts discussed the Arab Spring in countries such as Tunisia and Egypt as the important social and political issue in the world, rather than sovereign debt problems in European peripheral countries.

In March, the situation turned upside down. A huge earthquake hit the north-eastern area of Japan, including the Tokyo metropolitan area. The disaster paralyzed large cities, albeit temporarily. Tsunamis that followed the earthquake claimed twenty thousand lives in the coastal area of the Tohoku region. It also caused the emergency in the Fukushima Daiichi nuclear power plant. Business activities were naturally affected, particularly in the automobile industry with some key components factories, including microcontroller chips, being significantly damaged or not available for use due to radiation from the Fukushima plant. Automobile production slid 49% in March from the previous year, although the extent of the drop narrowed to 14% year-over-year ("y-o-y") in June. Starting this past April, many Japanese manufacturers began to make every effort to restore their disrupted supply chains.

The strong JPY trend, which had resumed after the March earthquake, prompted the G7 countries to unanimously intervene in the forex market. However, the Japanese yen, in spite of the occasional intervention by the Ministry of Finance, remained at record-high levels up until October.

From April through July, the Tokyo market moved sideways as market participants assessed the degree of recovery in the damaged production sites of Japanese companies. Most macro numbers across the globe were neither upbeat nor gloomy. Those in Japan were also returning to the path of recovery as the double digit declines in industrial production in March and April bounced back to positive growth in August.

In August, global markets went south as the US ISM Manufacturing Index suggested a slowdown and S&P lowered the credit rating of U.S. treasury bonds. In Europe, the sovereign debt crisis in Greece worsened and generated broad uncertainty in financial markets. As a result, Japanese stocks fell sharply, although the big drop was mitigated towards month-end on robust earnings announcements. In the following months, the Tokyo market moved sideways as its prices had approached record lows in the preceding months and thus had a limited likelihood of further downward moves.

A sector-based review of equity market developments shows that Rubber Products, Mining, and Construction sectors performed relatively well, while Electric Power & Gas and Marine Transportation were among the worst performers. Rubber product companies, namely tire makers, were favored compared to automobile makers that were adversely impacted by the March Earthquake. The problems facing nuclear power plants brought on a revision of energy policy, thus affecting electric power operators such as Tepco. Some mining companies, including Inpex, will benefit from increasing demand for liquefied natural gas—Inpex's main product—as a result of suspended activities in most nuclear power plants throughout Japan. Construction companies will benefit from reconstruction activities in areas damaged by the disaster. Shipping companies continue to struggle with industry-wide overcapacity.

Performance/Attribution Analysis

Table 1: NAV performance in comparison with the benchmark (TOPIX), U.S. Dollar ("USD") base

	Latest 12 Months (As of October 31, 2011) %
Japan Equity Fund (time weighted return)	-3.43(1)
Benchmark (TOPIX)	-1.97
Underperformance	-1.46

Table 2: Attribution analysis summary, JPY base

	Latest 12 Months (As of October 31, 2011) (%)
Portfolio (Equity Only)	-5.55
Benchmark (TOPIX)	-3.66
Underperformance	-1.89
Breakdown	
Sector Selection	1.20
Stock Selection	-3.08
Others	-0.01
Total	-1.89

¹Due to fluctuations in foreign exchange rates, this value may differ from the total investment return based on net asset value at beginning and end of year, assuming reinvestment of dividends, provided in the Financial Highlights section of the Fund's Annual Report.

The Japan Equity Fund, Inc.

Table 3: Portfolio return (equity portion of the Fund's portfolio) vs. Benchmark Return, USD base (monthly)

		Portfolio Return (A) (%)	Benchmark Return (B) (%)	Relative Return (A) - (B) (%)
2010	November	1.26	1.91	-0.65
	December	8.27	7.96	0.31
2011	January	0.39	0.47	-0.08
	February	4.70	5.06	-0.36
	March	-8.47	-10.19	1.72
	April	-1.22	-0.74	-0.48
	May	0.36	-0.11	0.47
	June	1.61	1.47	0.14
	July	2.25	2.74	-0.49
	August	-9.23	-7.09	-2.14
	September	-1.34	-1.11	-0.23
	October	-0.75	-1.04	0.29

Table 4: Attribution Analysis Breakdown, JPY base (Latest 12 Months) – (equity portion of Fund's portfolio)

	Port Weight (%)	Bench Weight (%)	Port Return (%)	Bench Return (%)	Sector Selection Effect (%)	Stock Selection Effect (%)
Fishery, Agriculture & Forestry	0.00	0.10	0.00	5.70	-0.01	0.00
Mining	0.00	0.62	0.00	23.38	-0.14	0.00
Construction	1.63	2.20	23.36	21.90	-0.10	0.02
Foods	1.85	3.14	2.06	12.59	-0.27	-0.11
T e x t i l e s &						
Apparel	0.07	0.94	6.60	4.47	-0.08	0.04
Pulp & Paper	0.20	0.38	4.16	3.43	0.01	-0.04
Chemicals	6.61	5.99	-7.71	0.55	0.02	-0.52
Pharmaceutical	3.61	4.61	3.99	1.09	-0.18	0.10
O i l & C o a l						
Products	1.91	0.90	0.72	5.62	0.03	-0.06
R u b b e r						
Products						