

Japan Smaller Capitalization Fund, Inc.

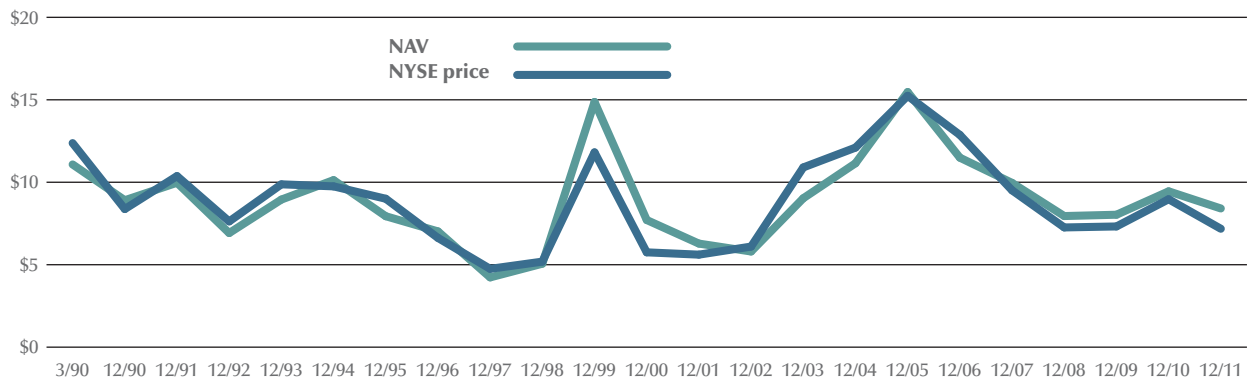
as of 12/31/11

Fund Objective

Japan Smaller Capitalization Fund, Inc. ("JOF" or the "Fund") Japan Smaller Capitalization Fund, Inc. ("JOF" or the "Fund") is a non-diversified, closed-end management investment company. The Fund's investment objective is to provide shareholders with long-term capital appreciation and to invest, under normal circumstances, at least 80% of its total assets in smaller capitalization Japanese equity securities traded on the Tokyo, Osaka, Nagoya, and JASDAQ Stock Exchanges, the Mothers, Hercules, Centrex markets, 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. Nomura Asset Management U.S.A. Inc. has served as the Fund's Manager since the Fund's inception in 1990. Nomura Asset Management Co., Ltd. has served as the Fund's Investment Adviser since the Fund's inception. The Manager and Investment Adviser are subsidiaries of Nomura Holdings, Inc. and affiliates of Nomura Securities Co., Ltd., Tokyo, Japan.

Net Asset Value Since Inception (March 22, 1990) vs. NYSE Closing Price



Fund Facts

• Net Assets:
\$238,325,469

• Net Asset Value:
\$8.41

• NYSE Close:
\$7.18

• Premium/Discount:
-14.60%

• NYSE Ticker Symbol:
JOF

• Equity Portfolio Holdings:
80

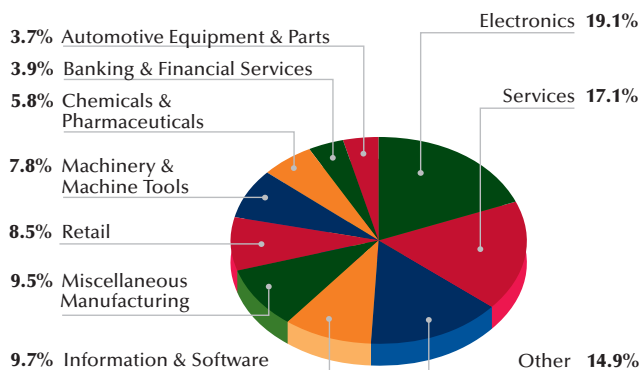
• CUSIP:
47109U104

• Inception Date:
3/22/90

• Automatic Reinvestment Option

Sector Weightings

As of 12/31/11. Sector weightings may vary over time.



Top Ten Holdings

As of 12/31/11. Holdings may vary over time.

Company	Percentage of Net Assets
Rakuten, Inc.	2.8%
Disco Corporation	2.8%
Aeon Credit Service Co., Ltd.	2.7%
Shinko Electric Industries Co., Ltd.	2.5%
Otsuka Corporation	2.5%
Message Co., Ltd.	2.5%
Park24 Co., Ltd.	2.3%
Musashi Seimitsu Industries Co., Ltd.	2.3%
Funai Electric Co., Ltd.	2.2%
MegaChips Corporation	2.2%

Performance Overview

Period ending 12/31/11.

	Calendar YTD ¹	1 Yr	3 Yr	5 Yr	10 Yr	Since Inception ¹
JOF NAV	-10.6%	-10.6%	2.6%	-5.4%	4.7%	0.5%
JOF NYSE Price	-19.6%	-19.6%	0.3%	-10.4%	4.2%	-0.5%
Benchmark Index	-2.0%	-2.0%	7.5%	-1.8%	7.5%	-0.7%
Nikkei JASDAQ Avg.	-0.9%	-0.9%	8.4%	-3.0%	5.8%	-0.8%

Past performance is not indicative of future results.

¹Inception date: March 22, 1990. ²Based on NAV price, adjusted for reinvestment of income dividends and capital gain distributions. ³Based on New York Stock Exchange's closing market price, adjusted for reinvestment of income dividends and capital gain distributions. JOF's performance does not represent sales commissions. ⁴Since inception to 8/31/04; Nikkei JASDAQ Average Index. 9/1/04 onwards: Russell/Nomura Small Cap Index. ⁵Nikkei JASDAQ Average Index in U.S. dollars.

Performance in excess of one year is annualized.

Sources: Nomura Asset Management U.S.A. Inc. and Bloomberg L.P.

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Japan Smaller Capitalization Fund, Inc.

Manager's Commentary

Japanese equities extended their losses, declining for a third consecutive quarter in the October-December period. The Tokyo Stock Price Index (TOPIX) eventually closed 3.7% lower in local currency terms for the fourth quarter of 2011, after fluctuating widely in reaction to some erratic shifts in investor risk tolerance. A series of positive economic indicators from the U.S. helped to mitigate some of the initial unease about global growth, while an agreement among European governments on measures to tackle the debt crisis also helped the Japanese market to rebound in November. The equity market sell-off resumed when speculators started to shift towards other financially vulnerable Euro zone states such as Italy and Spain, forcing their government bond yields up to unsustainable levels. Downward revisions to corporate earnings projections by Japanese companies that are suffering amid the protracted strength of the yen undermined market sentiment too, despite intervention by the Japanese authorities in the currency markets. An agreement among the main central banks to coordinate action to avert a liquidity crisis, together with solid economic numbers from the U.S., led to a rebound in the TOPIX in early December, but the market later became top-heavy toward the end of the quarter along with the yen's appreciation against both the U.S. dollar and the Euro.

Japanese economic indicators reflected the negative impact of the output disruption caused by the flooding in Thailand, faltering European demand and weaker domestic demand. Industrial production data was

unexpectedly weak, declining by 2.6% month-over-month (mom) as the flooding in Thailand temporarily disrupted output. In contrast, the survey of production forecasts suggested a solid recovery from the temporary decline in November, with a sustained rebound of +4.8% (mom) in December and +3.4% (mom) in January. European austerity measures and supply chain disruption were reflected in the trade figures too. Nominal exports in November posted a second consecutive monthly decline, decreasing by 4.5% year-over-year (yoy) after a 3.7% decline in October, as demand for major export product categories such as automobiles, electronics and machinery diminished. In the meantime, domestic demand has continued to stagnate. Real consumer spending in November declined for the ninth month in a row, shrinking by 3.2% (yoy). This unexpectedly large drop was partly attributed to the end of temporary policy measures, such as subsidies for the purchase of fuel efficient cars and home appliances. Also, the core Consumer Price Index in November continued to decline at a rate of -0.2% (yoy).

Many companies have reduced their earnings forecasts during the review period due to the strengthening yen and uncertainty about overseas economic conditions. In this context, performances were subdued across all sectors during the quarter. Softer equity markets and sovereign debt woes in the Euro zone particularly weighed on the Financials. In contrast, the defensive Communication sector was stable amid the market downturn.

Fund Information by Calendar Year¹

	JOF Performance ²	Benchmark Index ³	Nikkei JASDAQ Index ⁴	NAV At Period End	NYSE Closing Price At Period End	Income Dividend	Capital Gain Distributions	Net Assets (\$ millions)
1994 ⁵	-1.3%	—	22.7%	\$10.13	\$9.75	—	—	\$119.4
1995	-10.3%	—	-16.2%	\$7.94	\$9.00	—	—	\$94.3
1996	-23.9%	—	-10.6%	\$7.02	\$6.63	\$0.04	—	\$89.3
1997	-27.3%	—	-45.8%	\$4.23	\$4.75	\$0.08	—	\$48.2
1998	9.3%	—	0.5%	\$5.06	\$5.19	\$0.01	—	\$57.6
1999	127.7%	—	213.1%	\$14.88	\$11.83	—	—	\$235.6
2000	-45.1%	—	-51.1%	\$7.71	\$5.75	—	\$0.82	\$122.2
2001	-1.0%	—	-20.1%	\$6.28	\$5.61	—	\$0.08	\$99.6
2002	8.7%	—	-3.9%	\$5.80	\$6.10	—	—	\$92.0
2003	78.7%	—	58.2%	\$9.03	\$10.90	—	—	\$143.2
2004	11.0%	36.6%	28.0%	\$11.15	\$12.10	—	—	\$176.7
2005	26.0%	37.3%	34.9%	\$15.47	\$15.24	—	—	\$326.8
2006	-4.1%	-14.3%	-21.8%	\$11.49	\$12.87	\$0.41	\$1.25	\$243.3
2007	-26.1%	-10.5%	-13.2%	\$9.96	\$9.51	—	—	\$211.5
2008	-22.4%	-17.8%	-22.3%	\$7.95	\$7.26	—	—	\$169.0
2009	1.6%	6.1%	5.1%	\$8.03	\$7.32	\$0.0532	—	\$170.6
2010	23.6%	19.5%	22.4%	\$9.45	\$8.97	\$0.0796	—	\$200.8
2011	-10.6%	-2.0%	-0.9%	\$8.41	\$7.18	—	—	\$238.3

¹Sources: Nomura Asset Management U.S.A. Inc. and Bloomberg L.P. ²The Fund's inception date was March 22, 1990. ³Based on New York Stock Exchange's closing market price, adjusted for reinvestment of income dividends and capital gain

distributions. JOF's performance does not reflect sales commissions. ⁴Since inception to 8/31/04: Nikkei JASDAQ Average Index. 9/1/04 onwards: Russell/Nomura Small Cap Index. ⁵Nikkei JASDAQ Average index in U.S. dollars.

Additional Information

Comparisons between changes in the Fund's net asset value or market price per share and changes in the Fund's benchmark should be considered in light of the Fund's investment policy and objective, the characteristics and quality of the Fund's investments, the size of the Fund, and variations in the Japanese Yen/U.S. Dollar exchange rate.

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