JCGR Corporate Governance Survey 2006

－Final Report－

Takaaki Wakasugi (Tokyo University of Economics), Christina Ahmadjian (Hitotsubashi University)
Shusai Nagai (Ritsumeikan Asia Pacific University), Keiji Inoue (JCGR)
Kazuo Fukui (Fujitsu Research Institute)

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Japan Corporate Governance Research Institute (JCGR)
Corporate Governance Index Research Group

For questions regarding this survey, please contact: mailto:webmaster@JCGR.org

Summary and Recommendations

Outline of the Survey

The objective of corporate governance is to assure long-term corporate performance by establishing a system that makes management accountable for achieving corporate goals. A good corporate governance system leads to excellent corporate performance because it brings out superior management.

The framework of joint-stock company requires shareholders to take responsibility for the companies in the form of exercising their voting right. In the face of the business environment of the 21st century, with its intensifying global competition and rapid technological change, shareholders have made efforts to enhance the ability of the board of directors to monitor the management by electing independent directors at the shareholders' meeting in the past decade. Hence, a corporate governance system that separates execution by managers (management) and monitoring by the board of directors (governance) has been spreading around the world. Even in Japan, the Commercial Code was revised to allow firms beginning in April 2003 to either introduce a new corporate governance system, called the Board with Committees, or maintain the existing system of statutory corporate auditors. In May 2005, the Companies Act was newly established and took effect with the aim to strengthen corporate governance.

Since 2002, the Corporate Governance Index Group of the Japanese Corporate Governance Research Institute has conducted an annual survey of corporate governance of all firms listed on the First Section of the Tokyo Stock Exchange. This survey assesses how close a firm’s corporate governance adheres to this desirable state of separation between management and governance and reports the results for each firm in terms of the JCGIndex.

Between August and October 2006, we surveyed Tokyo Stock Exchange First Section Firms. While the number of the respondents had steadily increased before, it decreased to 312 firms (18.4% of the total) this year from 405 firms (24.6%) last year. Nonetheless, 70 firms responded to our survey for the first time, this year, reflecting a solid interest in corporate governance. This report covers 302 firms that had responded to the survey by the deadline (October 20). The results of our analyses of the relationship between the JCGIndex and performance were generally similar to results of previous years: high JCGIndex companies enjoy superior performance, as measured by higher ROA and ROE; however, unlike in the past results, low JCGIndex firms present higher return on common stock than high JCGIndex firms. This negative correlation is especially apparent this year.

We had assumed that analyzing the relationship between the past corporate performances and the present JCGIndex alone is sufficient. However, it turns out that several high JCGIndex firms have experienced poor performance; they started to reform the governance recently in the aftermath of the poor performance. For such companies, a negative correlation should be observed between the past performance and the JCGIndex. The existence of such high JCGIndex firms presumably has become apparent since last year. As we already expressed, corporate governance reform aims at improving future performance. Considering the fact that the corporate governance reform has just got started in Japan, that makes it reasonable to trace the relationship between the JCGIndex and performance after these firms start the governance reform. As of now, however, we are unable to conduct analysis from this perspective because the history of our survey is just four years and the size of the samples is too small. Now that we have five-year-data, we will be able to analyze the relationship between the JCGIndex and the future performance next time.

Anyway, the findings of the past JCGIndex surveys demonstrate that there is a positive correlation between the JCGIndex and corporate performance, implying that a corporate governance system that separates governance and management is the best model in today's business environment. We hope that the JCGIndex and the results of our analyses will be used by both investors and managers and will be useful in promoting continued corporate governance reform in Japan. We are very grateful to the companies that responded to this survey.

Since we started the survey, the environment surrounding the Japanese companies has been drastically changing: the new Companies Act, frequent takeover bids, etc. To address these changes, this time too, we modified questions, options, and proportions. Knowing that making changes every year is undesirable with regard to the survey's consistency, we strongly believe that handling with the perpetually changing environment is much more important. Therefore, a company's JCGIndex may increase or decrease by about 10 points. We would appreciate your understanding.

Seven Important Results

1. Response rate indicates a continued increase in interest in corporate governance

From August to October 2006, the Japan Corporate Governance Research Institute surveyed all firms listed on the First Section of the Tokyo Stock Exchange (1,696 firms as of July 13, 2006), and received responses from 312 firms. Survey questions were based on the "JCGR Corporate Governance Principles." The JCGIndex is based on these questions.

This is the fifth consecutive year that we have carried out the survey. In 2002, we received responses from 159 firms. In 2003, 201 firms responded, 129 for the first time. In 2004, 341 firms responded, 189 for the first time. In 2005, 405 firms responded, 112 for the first time. In 2006, 70 firms responded for the first time. Over the past five years, we have received responses from 660 firms. This report analyses the results for 302 firms that had responded to the survey by the deadline of October 20.

2. Characteristics of the responding firms: Large firms with high performance

Firms that responded to the survey tended to be very large. The average size of assets, sales, and number of employees of responding firms (averaged over 2001-2005) was more than twice the size of the average listed firm. ROA of responding firms was 5.74%, compared to 5.45% for all listed firms: ROE was 5.03% versus 3.26%. Like in the previous year, however, the return on common stock for responding firms was slightly lower than all listed firms (12.72% versus 12.74%).

3. Distribution of the JCGIndex: Increased average score but wide range

This year, the average JCGIndex for the 302 responding firms is 47.3 (standard deviation 14.1), compared to an average of 48.0 (standard deviation 12.9) for last year. We believe that this decrease in average is due to the changes made in the questions and proportions this year and does not imply a worsening corporate governance in Japan.

Now that matters concerning takeover bids are discussed from the viewpoint of interest of shareholders, it is fair to say that the state of corporate governance in Japan continues to advance. However, 47.3 points is lower than one half of the total of 100 possible points, and from this it can be concluded that the state of corporate governance in most Japanese firms is far from the ideal state of our governance model.

The range between the highest and lowest JCGIndex firms is quite large, as in the previous years. This year, the highest JCGIndex was 92 and the lowest was 18. Last year, the highest JCGIndex was 86 and the lowest 12. The standard deviation increased to 14.1 from the previous 12.9.

4. Average points by category: Governance reform is unbalanced

The JCGIndex is the sum of the points in 4 separate categories (Cg1, Cg2, Cg3, Cg4). Categories Ⅰ and Ⅱ are related to corporate governance system, and Ⅲ and Ⅳ are about corporate management system.

The following table reports the average points in each category for the 302 responding firms. In Categories III and IV, firms on average achieved over 50% of all possible points. The achievement rates for Categories I and II were far lower. In particular, average points for Category II, the structure and function of board of

directors, were particularly low, indicating that the separation of monitoring by the board of directors (governance) and execution by managers (management) has yet to spread widely.

For all of the four categories, the average points significantly changed from last year. We assume reasons of the changes to be as follows: The achievement rate for Category I fell from last year because changes in proportions were made to emphasize the difference between good governance and bad governance. The average for Category II increased because even companies adopting the system of statutory corporate auditors reinforced the function of monitoring the management by clarifying the nomination and compensation functions or accepting outside directors. The lower average point for Category III is due to the addition of questions on internal control and anti-takeover measures. The remarkable increase in the average of Category IV reflects the management's serious efforts to meet with the public demand for transparency.

These results suggest that in corporate governance reform, firms have focused on corporate restructuring, and have improved management systems and disclosure. In contrast, reform in the essence of governance, which is CEO accountability and board function, has not progressed as far.

Category	Mean/ allocated point	Achievement rate* (mean/allocated point)
I Corporate objectives and CEO responsibility	10.2/28	36.4% (42.9%)
II Structure and function of board of directors	8.7/25	34.8% (30.8%)
III Management system	15.1/27	55.9% (62.6%)
IV Transparency and communication with shareholders	13.3/20	66.5% (57.0%)

(note) results from last year's survey are in parentheses

5. Characteristics of high and low JCGIndex firms

To compare the characteristics of high and low JCGIndex firms and to examine the relationship between the JCGIndex and corporate performance, we constructed two groups: high and low JCGIndex firms. The high JCGIndex group consists of the 51 firms with a JCGIndex of 62 or more points (over one standard deviation above the mean) and the low JCGIndex group consists of the 54 firms with a JCGIndex of 33 or less (over one standard deviation below the mean).

(1) Characteristics of high and low JCGIndex firms: The percentage of foreign ownership is higher

The average percentage of shares held by foreigners in the high JCGIndex group is 30.3%, while the average for responding firms is 18.9%, and the average for low JCGIndex firms is even lower at 10.9%. Every year, our survey has illustrated that companies with good governance generally enjoy strong

performance. It is not certain whether good governance defines high foreign ownership or vice versa.

There is no statistically significant difference in the average age of the CEO between high JCGIndex firms (60.3) and low JCGIndex firms (60.0). In the previous survey, the average age for high JCGIndex firms was three years younger than the average for low JCGIndex firms.

(2) High JCGIndex firms are bigger

The total assets, sales, and number of employees are over 10 times greater in the high JCGIndex firms than the low JCGIndex firms.

(3) High JCGIndex firms are strong in all aspects of corporate governance

High JCGIndex firms have achieved high points in all four categories, indicating that a high JCGIndex cannot be achieved with high scores in only one or two categories. In Category I, high JCGIndex firms achieved on average 16.5 points (versus 5.4 points for low JCGIndex firms). In Category II, this was 16.4 versus 4.3, in Category III, 19.9 versus 10.0, and in Category IV, 17.6 versus 8.9. The JCGIndex captures the complete picture of a company's corporate governance capabilities and is not determined by single category.

6. JCGIndex and firm performance: A clear relationship

The objective of corporate governance is to assure excellent corporate performance. Is there really a relationship between corporate governance and corporate performance? In the 2006 JCGIndex survey, as well as in surveys for previous years, we found a close relationship between the two. However, just as last year, return on common stock was lower in the high JCGIndex firms than in the low JCGIndex firms.

(1) High JCGIndex firms enjoy superior performance on most dimensions

Based on 5-year averages, ROA (5.97% versus 5.63%) is higher in the high JCGIndex firms than in the low JCGIndex firms. However, this year, ROE (4.79% versus 5.48%) and return on common stock (10.42% versus 15.33%) were lower in the high JCGIndex firms than in the low JCGIndex firms. In the first three years, all of the three were higher in the high JCGIndex firms, but the trend has changed since last year. This reversal can be attributable to the fact that several companies that reformed the governance in the aftermath of the poor performance have now scored high JCGIndex, as we explained in the outline. Further analysis is required to verify this assumption.

(2) The rate of growth in employment is higher in the high JCGIndex firms

Based on the 3-year average (2003-2005) of growth of employment, high JCGIndex firms have a higher growth rate than low JCGIndex firms (4.57% versus 2.85%). While it is often said that in order to increase profits it is necessary to sacrifice employment, our result suggests that high JCGIndex companies are

establishing high performance without cutting costs through reducing employment.

7. Relationship between each category and performance: Strongest for structure and function of the board of directors and transparency and communication with shareholders

To determine whether or not there was a similar relationship between performance and each of the categories of the JCGIndex, we constructed high and low JCGIndex groups in each of the 4 categories, choosing the firms with points of one standard deviation above the mean or one standard deviation below the mean for each of the categories. In the surveys for previous years, the groups with high points in each category had higher performance (averaged over the past 5 years) than firms with low points. This year, however, we found no clear differences across categories in the relationship to performance. The generally positive relationship between the JCGIndex as a whole and performance explained above indicates that corporate governance is not a question of a single category, but rather, of all the categories taken together.

Conclusion: Corporate governance reform is key to the revival of the Japanese economy

The JCGR surveys over the past 5 years have demonstrated that corporate governance is strongly related to corporate performance. Although the response rate of the survey has not been high in any given year, we have received 1,418 responses for 660 distinct firms, and each year shows a similar relationship between JCGIndex and performance (although there are a few abnormalities). Based on this, we feel that it is appropriate to conclude that corporate governance reform is a necessary condition for Japanese firms to compete in the 21st century business environment. We hope that investors and managers will use the JCGIndex to promote corporate governance reform.

Investors are particularly important to governance reform. From the perspective of managers, there is not much incentive to promote corporate governance, as corporate governance reform makes them more accountable for corporate performance. For investors, on the other hand, corporate governance reform has a close relationship to the improvement of the performance of their investment, and therefore, they have a strong incentive to push for reform. This is especially true for institutional investors, who manage such a large share of investment capital today.

As investors become more aware of the importance of corporate governance reform, shareholder activism, including exercise of voting rights and establishment of governance funds, will increase. We hope that the JCGIndex will be used as an important weapon in these activities. For this reason, in 2004, we started to ask all responding companies to disclose their JCGIndex results. As part of the survey, we ask firms to give us permission to disclose their name if they were in the top 50% of the JCGIndex. Fortunately, most of the companies have answered “yes.” Thus, we have been able to report a list of the top 50% JCGIndex firms, as well as a list of all responding companies. We are very impressed by the courage of firms that permitted the disclosure of their names and are very grateful to them. We hope that firms and investors

will find many uses for the JCGIndex.

【Appendix】The top 52 JCGIndex firms and their JCGIndex results

Nomura Holdings, Inc. (*)	92	Toshiba Corp. (*)	86
Nikko Cordial Corp. (*)	84	Daiwa Securities Group Inc. (*)	83
Sumida Corp. (*)	81	Omron Corp.	80
Eisai Co., Ltd. (*)	79	Shinsei Bank, Ltd. (*)	79
Teijin Ltd.	78	Sony Corp. (*)	78
Meitec Corp.	77	Millea Holdings, Inc.	76
Asahi Glass Co., Ltd.	75	Mitsubishi Electric Corp. (*)	74
Anritsu Corp.	74	Konica Minolta Holdings, Inc. (*)	73
Aeon Co., Ltd. (*)	73	Resona Holdings, Inc. (*)	73
Hitachi, Ltd. (*)	72	Hitachi Information Systems, Ltd. (*)	71
Benesse Corp.	71	**********	71
Mitsui & Co., Ltd.	70	Ube Industries, Ltd.	70
Tokyo Gas Co., Ltd.	70	Santen Pharmaceutical Co., Ltd.	70
Asahi Breweries, Ltd.	69	Isetan Co. Ltd.	69
Terumo Corp.	68	Aisin Seiki Co., Ltd.	68
Marubeni Corp.	67	Orix Corp. (*)	67
**********	67	Fuji Seal International, Inc. (*)	66
Kao Corp.	66	Sojitz Corp.	66
Yamato Holdings Co., Ltd.	66	Parco Co., Ltd. (*)	66
Japan Airlines Corp.	65	**********	65
Tokyo Theatres Co., Inc.	64	Showa Denko K. K.	64
Nomura Research Institute, Ltd.	64	Yamaha Motor Co., Ltd.	64
TDK Corp.	63	Ricoh Co., Ltd.	62
Tokyo Electron Ltd.	62	Showa Shell Sekiyu K.K.	62
Yokogawa Electric Corp.	62	Hitachi Maxell, Ltd. (*)	62
The Fuji Fire and Marine Insurance Co., Ltd. (*)	62	Transcosmos Inc.	62

(note) (*) firms adopting board with committees

I. Outline of the survey and the survey results

1. An overview of the JCGIndex survey 2006

Between August and October 2006, the Japan Corporate Governance Research Institute (JCGR) sent its fifth annual survey to all Tokyo Stock Exchange First Section firms (1,696 firms as of July 13, 2006). We received responses from 312 firms. The names of these firms are listed in the Appendix. This report analyzes the responses from 302 firms that had responded to the survey by the deadline.

159 firms responded in 2002, 201 firms in 2003, 341 firms in 2004, and 405 firms in 2005. 590 firms responded in one or all of the four years. Of the 312 firms that responded to the survey in 2006, 70 firms responded for the first time. Over the five years that we have administered the survey, we have received 1,418 responses from a total of 660 firms.

2. The objective of the JCGIndex survey

The objective of the JCGIndex is to measure the current state of corporate governance in Japanese firms through indexation. We hope that the JCGIndex will help Japanese people to look at Japanese firms in a new light. Furthermore, we hope that the JCGIndex will help the foreign business community better understand the corporate governance situation in Japan. We believe that in the process of responding to the questions in the JCGIndex survey, Japanese companies will gain a deeper understanding of our corporate governance model and hope that the JCGIndex is helpful to Japanese firms in realizing the corporate governance that they desire.

3. About the JCGIndex

The objective of corporate governance is to give corporate executives a clear goal for corporate performance and to create a system by which they assume responsibility to reach those goals. For this reason, it is important to separate the execution of management (management) by executive officers from the monitoring of management (governance) by the board of directors, and to maintain transparency to shareholders and all stakeholders regarding the state of the corporation.

The JCGIndex is based on about 50 questions, derived from the “JCGR Corporate Governance Principles.” These questions were grouped under nine titles for the ease of respondents.:

1. governance from the perspective of shareholders
2. clear and measurable corporate goals
3. a system to assure the responsibility of CEO and top management team for realizing the goals
4. an independent board with capability to monitor and motivate management

5. systems for managerial decision-making and implementation to achieve performance targets
6. risk-management to fulfill compliance, internal control, and social responsibilities
7. accountability to shareholders
8. provision of appropriate information to shareholders through investor relations activities
9. maintenance of transparency through disclosure to all stakeholders

The answers to each question item are quantified, and distributed to one of the following four categories from the viewpoint of division of governance and management, and finally constitute a category score.

I. Corporate objectives and CEO responsibility
II. Structure and function of board of directors
III. Management system
IV. Transparency and communication with shareholders

The JCGIndex is the sum of the points in these four categories. If all points in all four categories are achieved, a firm receives a JCGIndex of 100. The fewer the points achieved, the closer the JCGIndex is to 0.

II. Characteristics of responding companies and the JCGIndex

1. A comparison of responding companies to all listed companies

The 312 responding companies represent 18.4% of the companies listed on the Tokyo Stock Exchange First Section. The table below presents comparisons of financials of responding companies and all listed companies, based on 5-year averages (2001-2005). The averages do not include companies that did not report financials in all five years.

Companies that responded to the JCGIndex survey were far larger than average in terms of total assets, sales, and number of employees. ROA, ROE, and return on common stock, which are not related to firm size, were larger for responding companies than for the average listed companies and their variance was smaller than that for all listed companies. The differences in these measures of size and performance for responding firms and all listed firms were significant in all cases. Here all figure are based on the consolidated financial statement.

5-year averages (consolidated)

total assets	No of firms	Mean	Minimum	Maximum	Standard deviation
All listed firms	1,400	406,791.39	1,425.80	23,147,631.40	1,293,543.53
responding firms	262	874,122.81	3,988.00	13,999,948.20	1,809,477.11

(million yen)

Sales	No of firms	Mean	Minimum	Maximum	Standard deviation
All listed firms	1,400	346,217.73	670.00	17,608,756.40	1,123,586.69
Responding firms	262	775,415.14	3,815.20	12,973,247.20	1,724,708.46

(million yen)

ROA	No of firms	Mean	Minimum	Maximum	Standard deviation
All listed firms	1,348	5.448	-15.10	32.03	4.25
Responding firms	256	5.738	-1.19	31.89	3.77

(%)

ROE	No of firms	Mean	Minimum	Maximum	Standard deviation
All listed firms	1,337	3.258	-464.18	67.35	17.93
Responding firms	253	5.029	-34.59	38.20	6.71

(%)

employees	No of firms	Mean	Minimum	Maximum	Standard deviation
All listed firms	1,399	6,990.88	16.60	316,957.80	20,791.99
Responding firms	262	15,155.61	86.40	316,957.80	32,243.04

(number of employees)

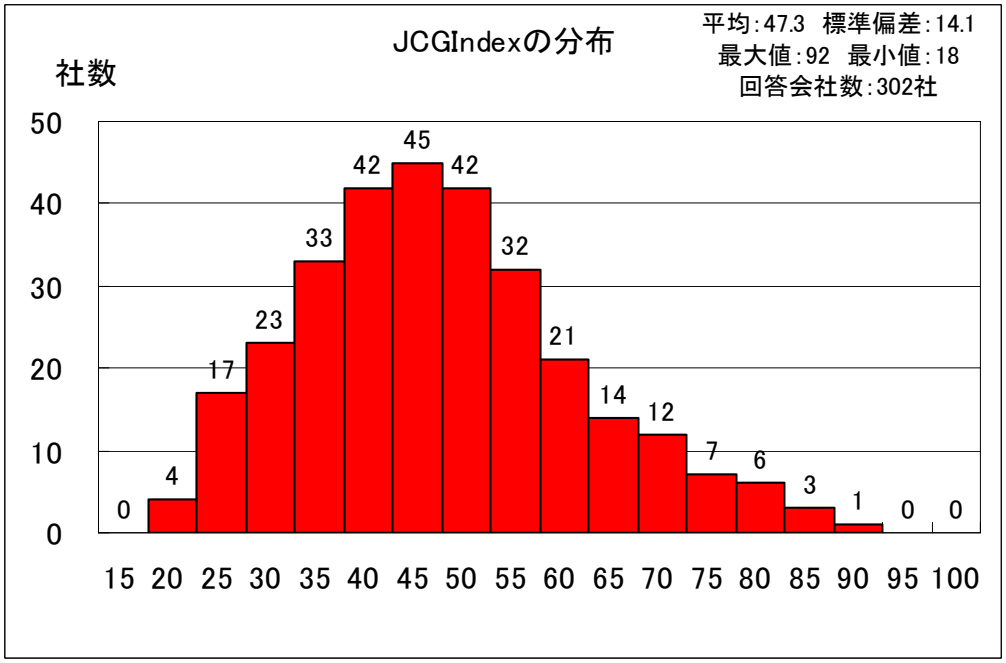
Return on stocks	No of firms	Mean	Minimum	Maximum	Standard deviation
All listed firms	1,273	12.735	0.00	54.30	9.24
responding firms	246	12.720	0.00	45.50	9.35

(%)

2. Distribution of the JCGIndex

The JCGIndex for individual companies was distributed widely, ranging from a maximum of 92 to a minimum of 18. Given that the model that JCGR adopts is an ideal one, companies achieving 80 or higher scores effectively achieve a maximum level of corporate governance. Unfortunately, some companies score less than 30 (a few even fall below 20); it cannot be helped that they fail to achieve even a minimum level of management, let alone governance.

The mean JCGIndex was 47.3 (last year, 48.0), the standard deviation was 14.1 (last year, 12.9), and there was a normal distribution around the mean.



(note) The x axis depicts a range of +/- 2.5 around the number indicated. For example, the number 15 depicts a range greater than 12.5 and less than 17.5. Because the JCGIndex is rounded to the nearest integer, the reported range is 13 to 17.

3. Board with committees and JCGIndex

In April 2003, the Commercial Code was revised to allow the introduction of the Board with Committees structure. This system was developed into the company with committees' structure, which was introduced by the Companies Act in May 2006 along with the board of corporate auditors' structure. The spirit of this new law, to facilitate the separation of governance by an independent board of directors and management by executive officers, is similar to the JCGR corporate governance principles. In the 21st century business environment, characterized by increasing globalization and rapid technological change, a governance system that ensures transparency, clarifies the responsibility of management for performance, and ensures that management makes its best efforts is critical.

Although the company with committee's structure makes it easier to create this kind of governance structure, it is still possible to establish this sort of governance with the board of corporate auditors' system. The JCGIndex is designed so that even if a firm has not introduced the company with committees' structure, if its governance structure assures the separation of management and monitoring, these efforts will be duly reflected in a higher JCGIndex.

Of the 302 firms that responded to the 2006 JCGIndex survey, 22 firms had introduced the company with committees' structure. Of the top 16 companies in the JCGIndex, 11 companies had introduced the

company with committees' structure. Of the top 50 companies, 19 companies had introduced this structure, and 8 of the top 10 firms had introduced it. Thus, while the company with committees' structure is well-represented in the list of high JCGIndex firms, not all high JCGIndex firms had introduced this structure.

Whether or not a company has a company with committees' structure, if it has clarified its structure for management accountability and has satisfied the necessary conditions in each category, it can obtain a high JCGIndex equivalent to that of a company that has adopted the company with committees' structure.

Questions of the structure of the board aside, even the top JCGIndex firms are still far from the maximum 100 points and there are many challenges ahead both for companies that have adopted this structure and those that have not.

4. The JCGIndex by industry

The following figure shows the average JCGIndex by industry for 2006 and 2005. We report results only for industries for which 5 companies or more responded.

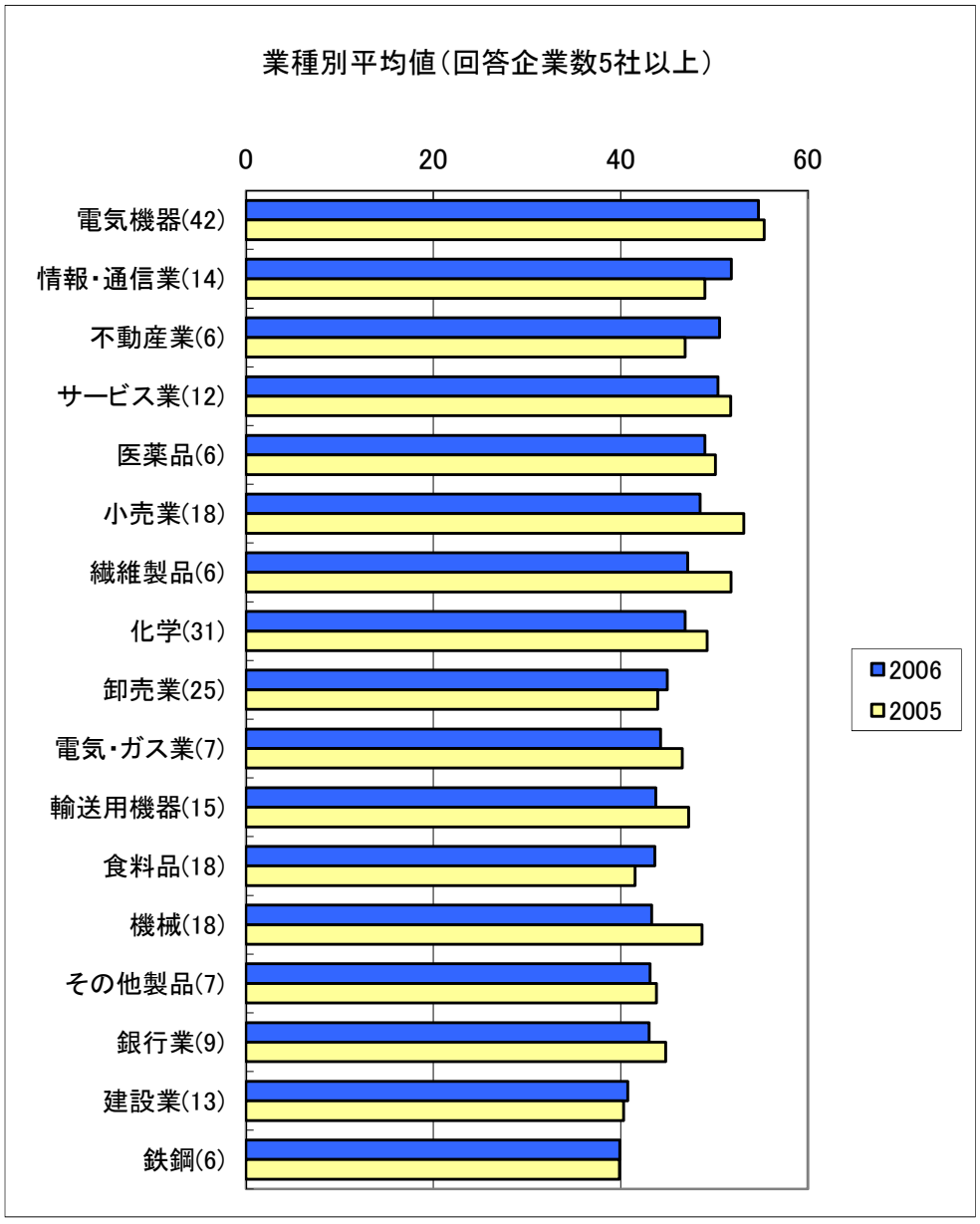
Note that changes in the average JCGIndex are attributable to the changes in the questionnaire (questions and point allocations) as well as changes in responding firms, and do not necessarily indicate that corporate governance in a given industry improved or worsened from last year.

(note) In the figure below, the industries of five or more responding firms are arranged in the following order. Number in the parenthesis after the industry name indicates the number of responding companies.

Electric appliances (42)
Telecommunications (14)
Real estate (6)
Service industry (12)
Pharmaceutical (6)
Retail (18)
Fiber products (6)
Chemical products (31)
Wholesale (25)
Electricity and gas (7)
Transportation equipment (15)
Food (18)

Machinery (18)
Other manufacturing (7)
Banking (9)
Construction (13)
Iron and steel (6)

The average JCGIndex by industry



5. Score by category

The following table reports the average points by category for the 302 responding firms. While firms achieved a relatively high percentage of total possible points in Categories III and IV, the achievement

rate for Categories I and II was much lower. This clearly indicates that the separation between the governance and management through independent boards has yet to be fully accomplished.

Until 2005, the achievement rate for Category II was significantly lower than the other Categories. This year, with the rate for Category I dropped and the rate for Category II increased from last year, the achievement rates for the two Categories on governance are roughly the same. The assumed reason is that even companies with board of corporate auditors have accepted outside directors to ensure the same level of auditing function as the companies with committees. As for management, while the achievement rate for transparency remarkably improved, the rate for management system dropped. That could be because we added questions on internal control and introduced questions on anti-takeover measures. We consider internal control and the protection of shareholders in Japan inadequate.

Category	Point allocated (A)	Mean (B)	Achievement rate (B) / (A)
I Corporate objectives and CEO responsibility	28 (28)	10.2 (12.0)	36.4% (42.9%)
II Structure and function of board of directors	25 (25)	8.7 (7.7)	34.8% (30.8%)
III Management system	27 (27)	15.1 (16.9)	55.9% (62.6%)
IV Transparency and communication to shareholders	20 (20)	13.3 (11.4)	66.5% (57.0%)

*Results in 2005 are in parentheses.

III. JCGIndex and on financial performance

In this section, we analyze differences between high and low JCGIndex firms in financial performance, and separately compare performance for each of the 4 categories of the JCGIndex between high category point firms and low category point firms. This report presents comparisons of unadjusted data. We have also created a supplementary report that shows comparisons of data adjusted for industry. Just as before, the differences in these two sets of analyses are not great, suggesting that our results are stable and robust to industry differences.

1. The definition of high and low JCGIndex groups

To analyze the relationship between the JCGIndex and firm characteristics, we constructed two groups:

high JCGIndex firms, with JCGIndex greater than one standard deviation above the mean (mean is 47.3 points, standard deviation is 14.1 points) and low JCGIndex firms, with JCGIndex greater than one standard deviation below the mean.

High JCGIndex firms: 51 firms with JCGIndex of 62 or more	(47.3+14.1=61.4)
Low JCGIndex firms: 54 firms with JCGIndex of 33 or less	(47.3-14.1=33.2)

We also used this method to construct groups of high and low firms for each of the four categories that make up the JCGIndex.

2. Analysis of relationship between JCGIndex and firm performance

(1) Method of analysis

We used the high and low JCGIndex groups constructed as described above to compare financial characteristics of high and low JCGIndex firms, and to compare these to all responding firms. Comparisons are shown in the form of graphs. We show the differences in means and report the degree of statistical significance.

Financial information is averaged over the previous 3 years (2003-2005) and 5 years (2001-2005), using consolidated reports. Firms that did not report data for the entire period were excluded from our comparison, so there is some variation in the number of firms used for each of the comparison.

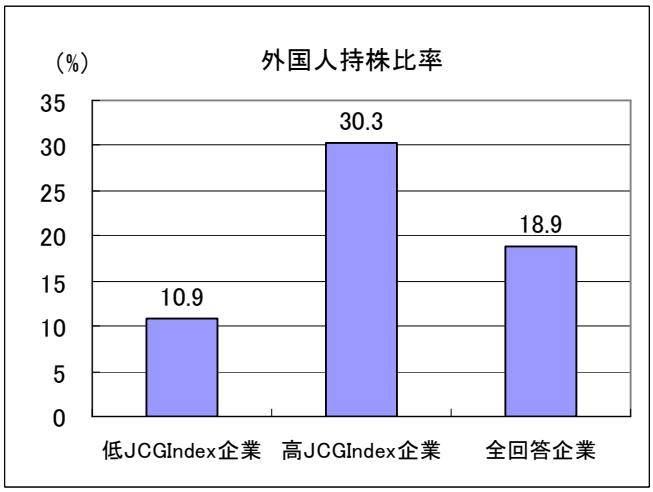
Return on assets (ROA) is profits before payment of interest and tax divided by total assets (averaged across beginning and ending of period). Return on equity (ROE) is profits after tax divided by total shareholders' equity (averaged across beginning and ending of period). Thinking of leverage, ROE should be larger than ROA. However, because ROA includes tax and ROE deducts tax, ROA is larger than ROE in some cases.

The return on common stock is the sum of the dividends and capital gains (or capital loss) for the period, divided by the share price at the beginning of the period.

(2) Characteristics of firms responding to the JCGIndex

First, we present some of the more interesting differences between the characteristics of firms in the high and low JCGIndex groups.

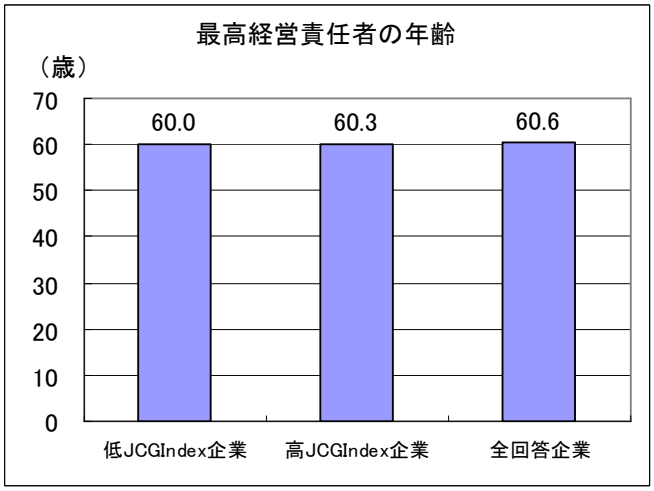
a. Percentage of foreign ownership



Just as 2005, foreign ownership is higher in high JCGIndex firms than in low JCGIndex firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 282
High JCGIndex firms: 48
Low JCGIndex firms: 51

b. Age of CEO



The CEOs of high JCGIndex firms are older than CEOs of low JCGIndex firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 279
High JCGIndex firms: 48
Low JCGIndex firms: 46

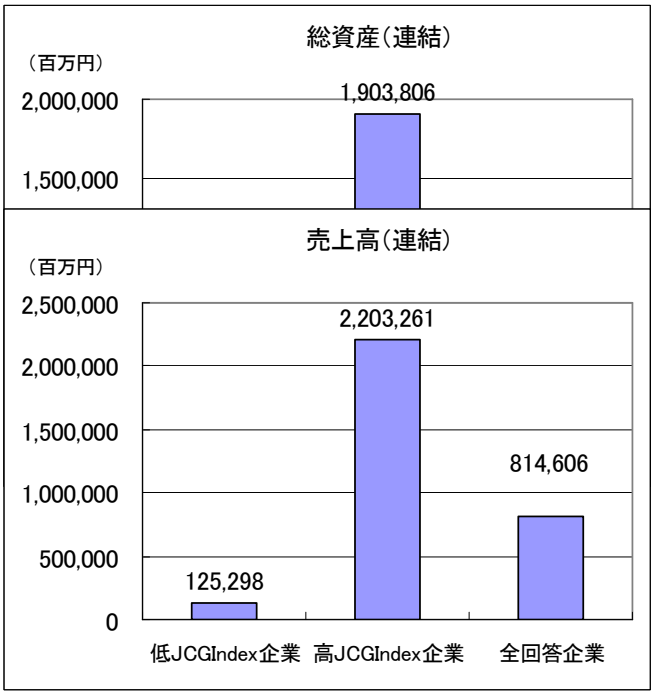
In 2005, the CEOs of high JCGIndex firms were three years younger than CEOs of low JCGIndex firms, but this difference is not observed this time.

(3) JCGIndex and firm size

a. Total assets (consolidated, average of 3 years)

Total assets of high JCGIndex firms are greater than total assets of low JCGIndex firms, and this difference is statistically significant (at the 1% level). This result is the same for the 5-year average of total assets.

Total responding firms: 271



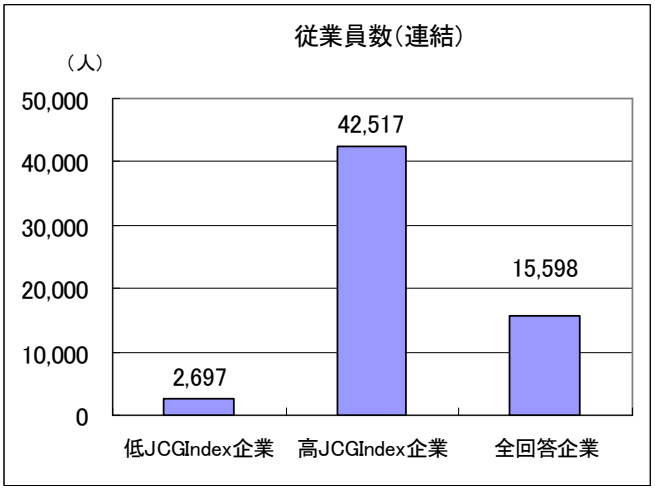
High JCGIndex firms: 44
Low JCGIndex firms: 46

b. Total sales (consolidated, average of 3 years)

Total sales of high JCGIndex firms are greater than total sales of low JCGIndex firms, and this difference is statistically significant (at the 1% level). This result is the same for the 5-year average of total sales.

Total responding firms: 271
High JCGIndex firms: 44
Low JCGIndex firms: 46

c. Number of employees (consolidated, average of 3 years)



Number of employees of high JCGIndex firms is greater than number of employees in low JCGIndex firms, and this difference is statistically significant (at the 1% level). This result is the same for the 5-year average of number of employees.

Total responding firms:271
High JCGIndex firms: 44
Low JCGIndex firms: 46

As in past surveys, firms with high JCGIndex have much larger sizes in total assets, sales and employee numbers than low JCGIndex firms.

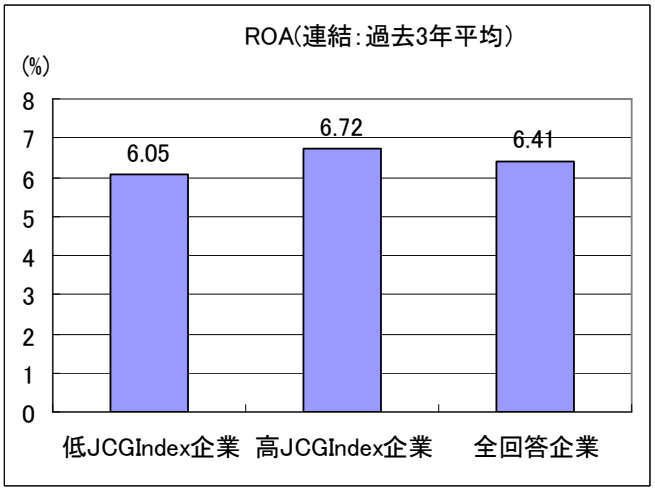
(4) JCGIndex and rate of return on capital

The essence of corporate governance from the perspective of shareholders is to maintain a return on capital invested. We compared return on total assets (ROA) and return on shareholders' equity (ROE) between high and low JCGIndex groups. For both 3- and 5-year averages, ROA and ROE are higher for

high JCGIndex than for low JCGIndex firms, but the difference is not statistically significant.

a. ROA (consolidated, average of 3 years and 5 years)

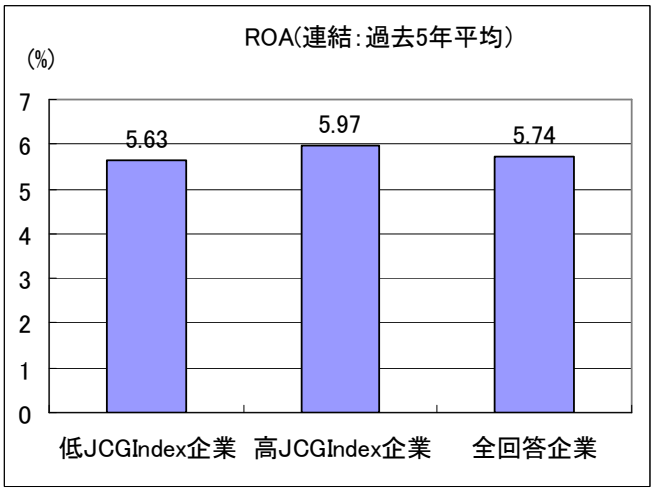
<3 years>



ROA for high JCGIndex firms is higher than ROA for low JCGIndex firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 266
High JCGIndex firms: 43
Low JCGIndex firms: 45

<5 years>

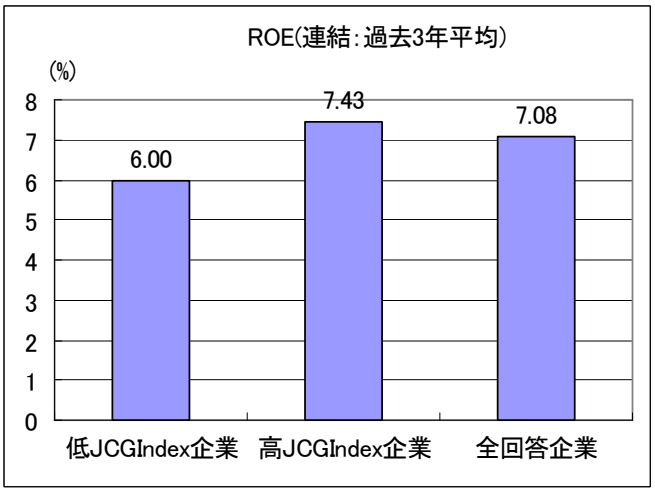


ROA for high JCGIndex firms is higher than ROA for low JCGIndex firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 256
High JCGIndex firms: 41
Low JCGIndex firms: 43

b. ROE (consolidated, average of 3 years and 5 years)

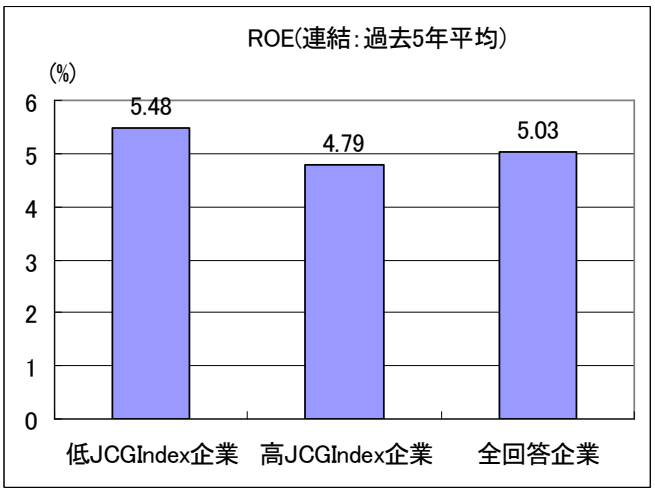
<3 years>



ROE for high JCGIndex firms is higher than ROE for low JCGIndex firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 264
High JCGIndex firms: 43
Low JCGIndex firms: 45

<5 years>



ROE for low JCGIndex firms is higher than ROE for high JCGIndex firms, but this difference is not statistically significant (at the 10% level).

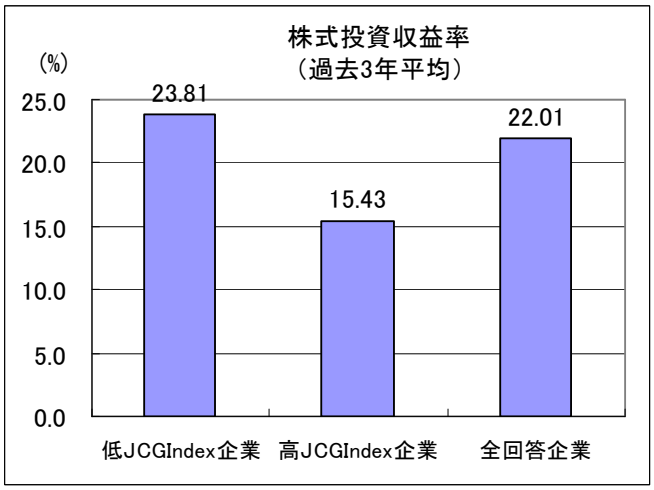
Total responding firms: 253
High JCGIndex firms: 41
Low JCGIndex firms: 43

(5) JCGIndex and rate of return on equity investment (average of 3 years and 5 years)

In the surveys from 2002 to 2004, taking into consideration the measure of investment risk, beta (β), high JCGIndex firms had higher returns on investment. This pattern has reversed since last year. This reversal can be attributable to the fact that several companies that reformed the governance in the aftermath of the poor performance have now scored high JCGIndex. Further analysis is required to examine this hypothesis.

The JCGIndex should be compared with the future performance (ROA, ROE, and return on common stock), but as of now, we are unable to conduct analysis from this perspective because the history of our survey is short, and the size of the samples is too small. Now that we have enough data, we will be able to analyze the relationship between the JCGIndex and the future performance next time.

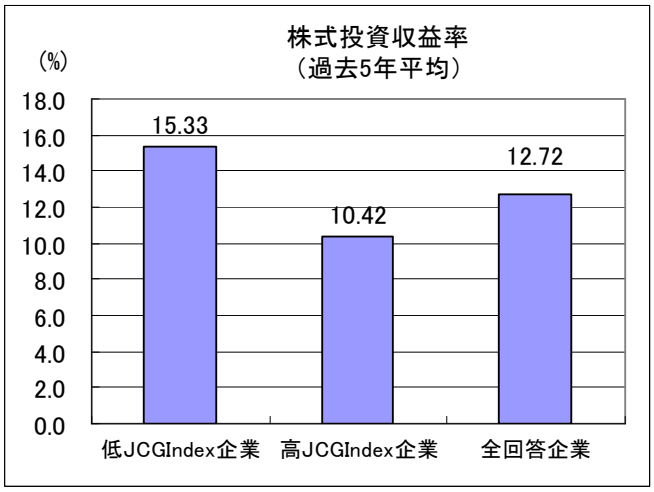
<3 years>



Return on common stock is lower in the high JCGIndex firms than in the low JCGIndex firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 270
High JCGIndex firms: 47
Low JCGIndex firms: 46

<5 years>



Return on common stock is lower in the high JCGIndex firms than in the low JCGIndex firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 246
High JCGIndex firms: 44
Low JCGIndex firms: 40

<adjustment for risk>

In a world where there is risk, return (in other words, average profitability in past years or future expected profit) cannot be evaluated without thinking about differences in risk. In modern capital markets, high risk=high return and low risk=low return, for both individual stocks and entire portfolios. This degree of risk is measured by the beta (β), and the risk-adjusted expected return of an investment is calculated as follows:

Expected return = interest rate + β× (expected market return - interest rate)

This formula is called the CAPM, or capital asset pricing model. According to this model, the expected return of a stock is a function of the risk-free rate (interest rate) plus the difference between the expected market return and risk-free rate, times a beta (β). The beta represents the contribution of a single stock to the total variance of the market portfolio, and thus is a measure of the relative risk of a stock. Predictions

for the return for stocks listed on the first section of the Tokyo Stock Exchange in excess of the risk-free interest rate are in the range of 3% to 5%. The beta of the market portfolio is set at 1 and is the weighted average of betas of all listed stocks. Thus, betas of individual stocks are distributed around 1.

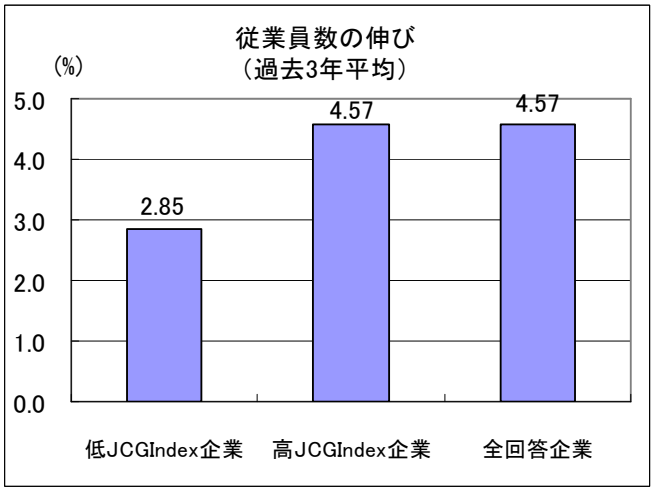
From 2002 to 2004, the beta of high JCGIndex firms was higher, but the return was also higher for these firms. So, shareholders of high JCGIndex firms received returns in excess of the risk. Since 2005, however, the trend has reversed: even though the beta of high JCGIndex firms is higher, the return is lower for these firms, meaning that the performance was very unfavorable for shareholders. Probable reason is stated at the beginning of this section.

	3-year β	5-year β
High JCGIndex firms	1.098	1.078
Low JCGIndex firms	0.877	0.862
All responding firms	0.902	0.906

(6) JCGIndex and growth in number of employees (consolidated, in 3 years)

Japanese companies seem to have secured profit through laying off employees in the past decade, but this is not the case when looking at our survey for five years: High JCGIndex firms, which enjoy better performance, increase the employees. Note that the difference between high JCGIndex firms and low JCGIndex firms is not statistically significant.

Above all, it would be fair to say that companies with good governance establish high performance without reducing employment.



Growth in employment for high JCGIndex firms is higher than growth in employment for low JCGIndex firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 270*
High JCGIndex firms: 44
Low JCGIndex firms: 46

* 1 outlier was removed.

IV: Category score and financial performance

1. Relationship between category score and JCGIndex

The following table shows the average number of points for each of the 4 categories that make up the

JCGIndex for the high and low JCGIndex groups. In the parentheses, we report the contribution of each category expressed as a percentage of the total points. The difference between the high and low JCGIndex groups in the contribution of each category to the total is evident. While each category contributes to the total to roughly the same degree in the high JCGIndex firms, the contribution of Categories I and II is significantly smaller than Categories III and IV in the low JCGIndex firms. This indicates that the JCGIndex reflects the quality of a company's governance.

category	I	II	III	IV	JCGIndex
High JCGIndex firms	16.5 (23.5%)	16.4 (23.2%)	19.9 (28.3%)	17.6 (25.0%)	70.5 (100%)
Low JCGIndex firms	5.4 (18.7%)	4.3 (15.1%)	10.0 (34.9%)	8.9 (31.3%)	28.6 (100%)

2. High and low firms by category and performance

In the following section, we create groups of high and low firms for each category and compare their performance. We calculated the high and low groups in the same way as we calculated the high and low JCGIndex groups. The high groups consist of firms for which the points in a given category are over one standard deviation above the mean for that category, while the low groups consist of firms for which the points in a given category are over one standard deviation below the mean.
We refer to the total points received in categories I, II, III, and IV as Cg1, Cg2, Cg3, Cg4.

3. Category I (Corporate objectives and CEO responsibility)

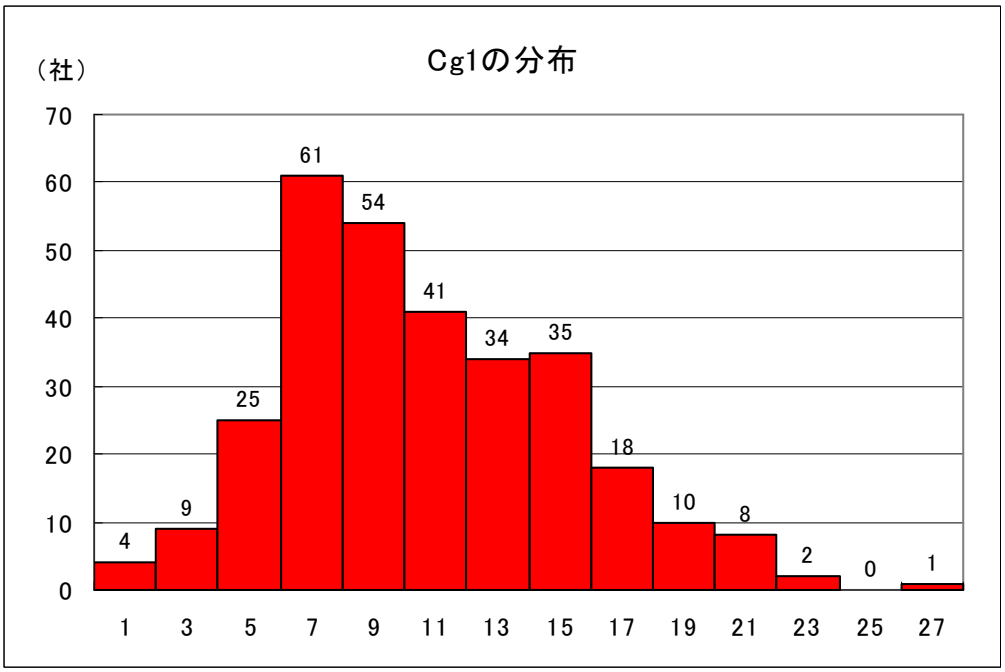
(1) Distribution of Category I score (Cg1), and definition of high and low Cg1 groups

High and low Cg1 firms are defined as follows;

High Cg1 group: 53 firms for which Cg1 is 15 or more

Low Cg1 group: 38 firms for which Cg1 is 5 or less

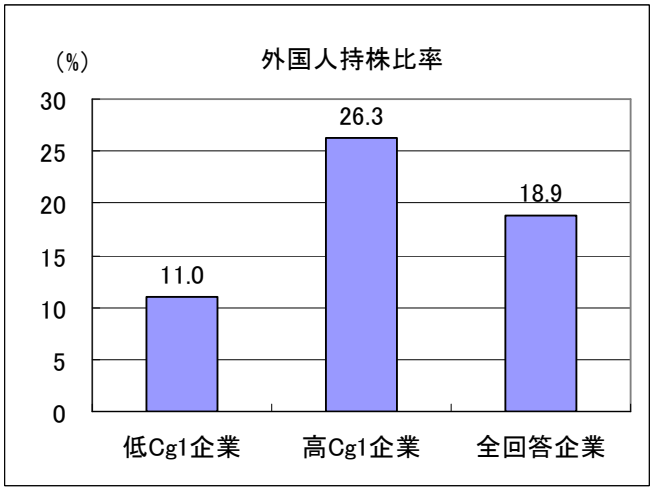
Distribution of Cg1



Mean: 10.2, Standard deviation: 4.5, Maximum, 26, Minimum 0

(2) Cg1 and firm characteristics

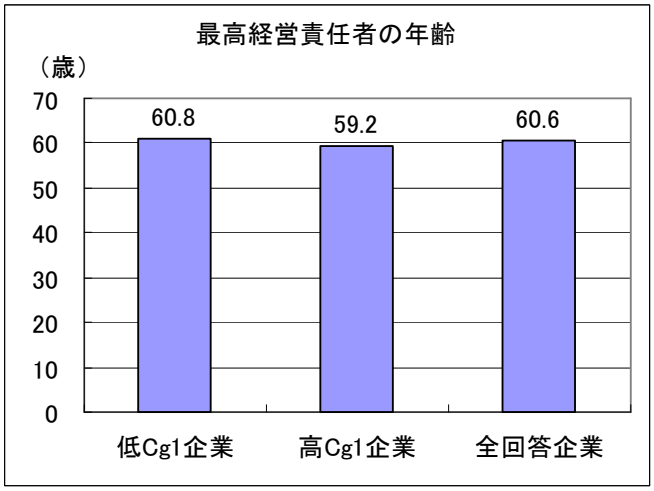
a. Percentage of foreign ownership



Foreign ownership is higher in high Cg1 firms than in low Cg1 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 282
High JCGIndex firms: 50
Low JCGIndex firms: 34

b. Age of CEO

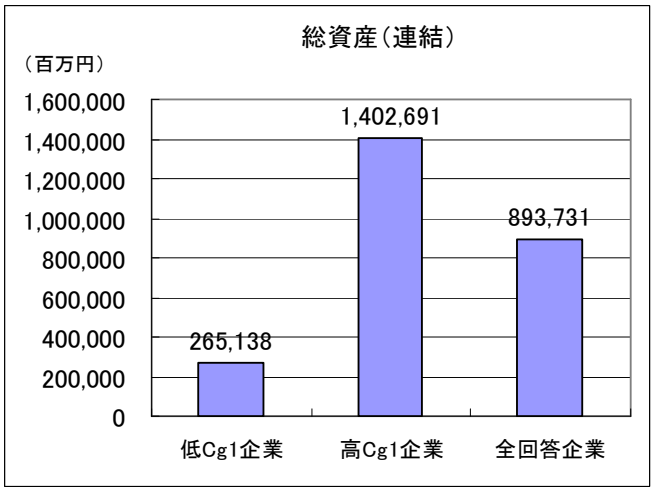


The CEOs of high Cg1 firms are younger than CEOs of low Cg1 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 279
High JCGIndex firms: 49
Low JCGIndex firms: 35

(3) Cg1 and firm size

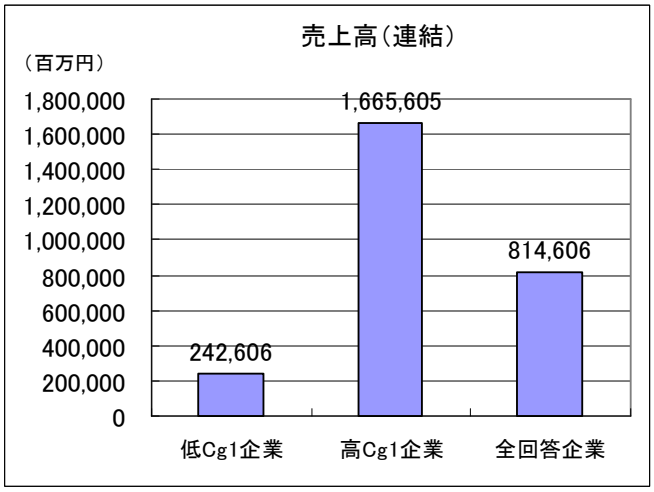
a. Total assets (consolidated, average of 3 years)



Total assets of high Cg1 firms are greater than total assets of low Cg1 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 45
Low JCGIndex firms: 32

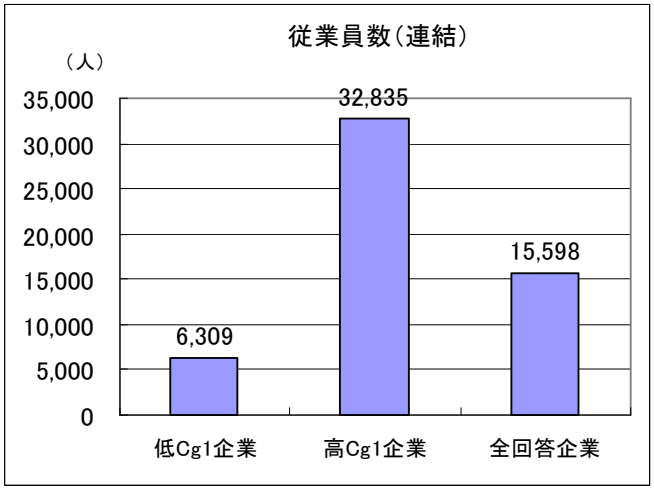
b. Total sales (consolidated, average of 3 years)



Total sales of high Cg1 firms are greater than total sales of low Cg1 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 45
Low JCGIndex firms: 32

c. Number of employees (consolidated, average of 3 years)



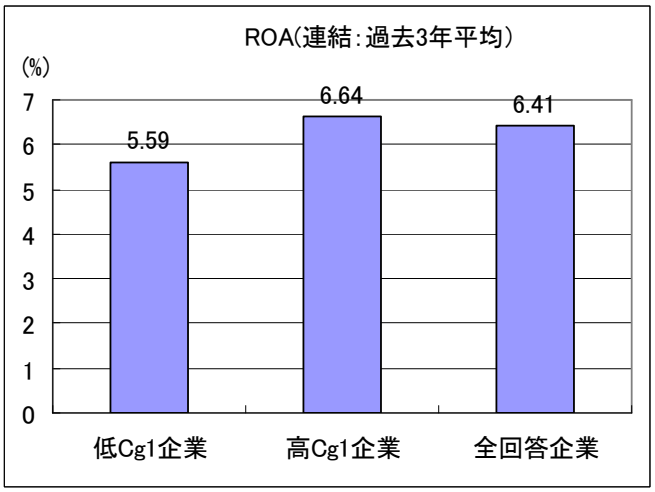
Number of employees of high Cg1 firms is greater than number of employees in low Cg1 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 45
Low JCGIndex firms: 32

(4) Cg1 and rate of return on capital

a. ROA (consolidated, average of 3 years and 5 years)

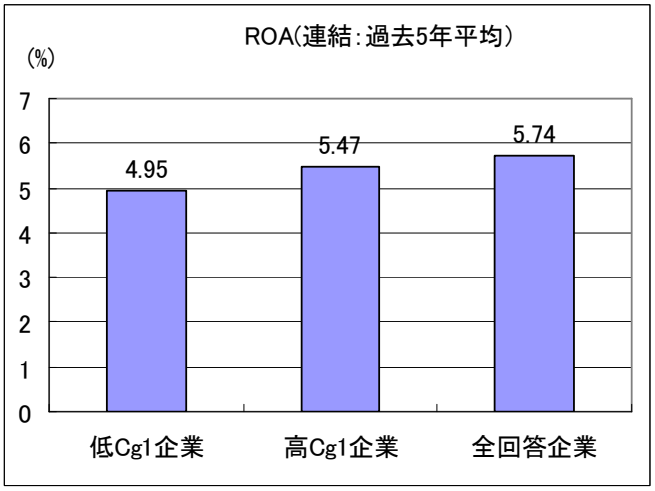
<3 years>



ROA for high Cg1 firms is higher than ROA for low Cg1 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 266
High JCGIndex firms: 43
Low JCGIndex firms: 31

<5 years>

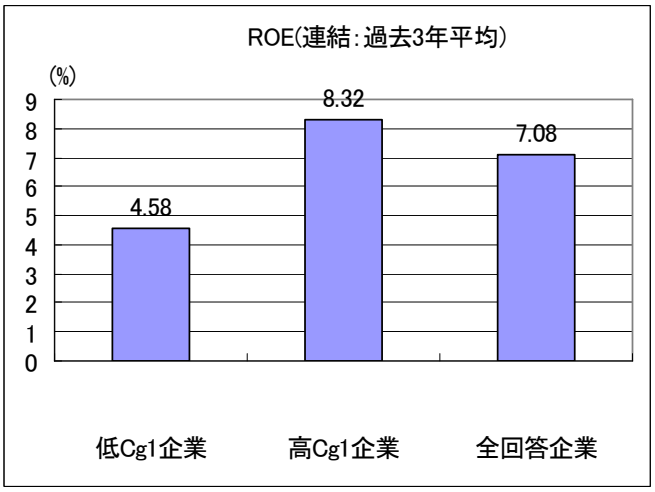


ROA for high Cg1 firms is higher than ROA for low Cg1 firms but this difference is not statistically significant (at the 10% level).

Total responding firms: 256
High JCGIndex firms: 43
Low JCGIndex firms: 29

b. ROE (consolidated, average of 3 years and 5 years)

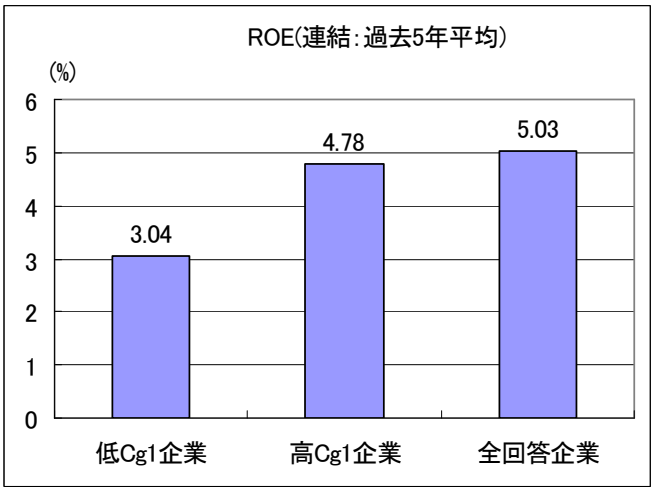
<3 years>



ROE for high Cg1 firms is higher than ROE for low Cg1 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 264
High JCGIndex firms: 42
Low JCGIndex firms: 31

<5 years>

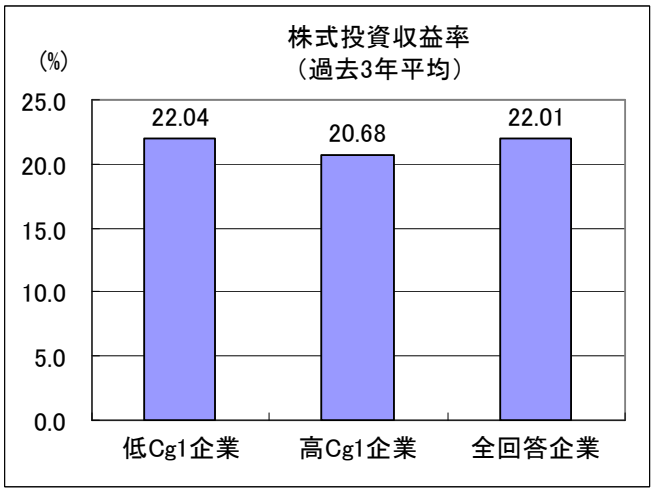


ROE for high Cg1 firms is higher than ROE for low Cg1 firms, and this difference is statistically significant (at the 5% level).

Total responding firms: 253
High JCGIndex firms: 42
Low JCGIndex firms: 29

(5) Cg1 and rate of return on equity investment (average of 3 years and 5 years)

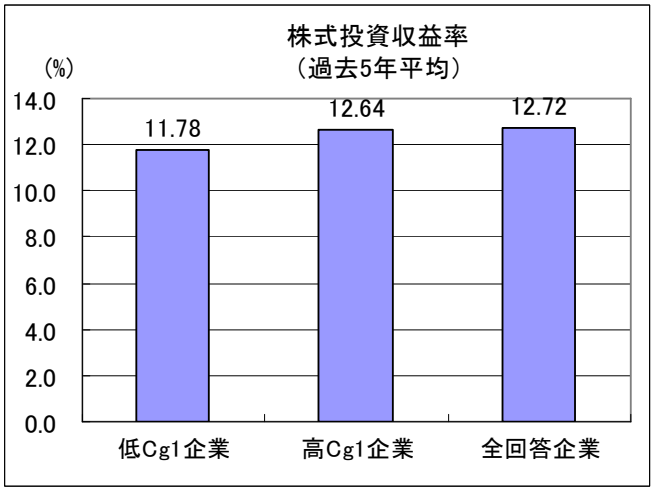
<3 years>



Return on common stock for low Cg1 firms is higher than for high Cg1 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 270
High JCGIndex firms: 49
Low JCGIndex firms: 30

<5 years>



Return on common stock for high Cg1 firms is higher than for low Cg1 firms, but this difference is not statistically significant (at the 10% level).

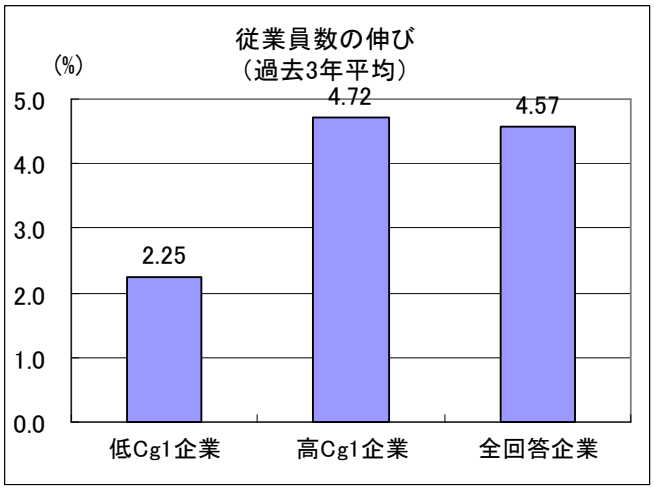
Total responding firms: 246
High JCGIndex firms: 44
Low JCGIndex firms: 26

<adjustment for risk>

The following table shows the betas of high and low Cg1 firms for 3 and 5 years. The difference between betas for the two groups is statistically significant in both cases (at the 1% level). During these periods, some of the downside risk of the high Cg1 firms is seen; even though the risk is higher for high Cg1 firms, there is no difference in return on common stock between high and low Cg1 firms.

	3-year β	5-year β
High Cg1 firms	1.134	1.114
Low Cg1 firms	0.744	0.799
All responding firms	0.902	0.906

(6) Cg1 and growth in number of employees (consolidated, 3-year growth)



Growth in employment for high Cg1 firms is higher than growth in employment for low Cg1 firms, and this difference is statistically significant (at the 10% level).

Total responding firms: 270*
High JCGIndex firms: 45
Low JCGIndex firms: 32
*1 outlier was removed.

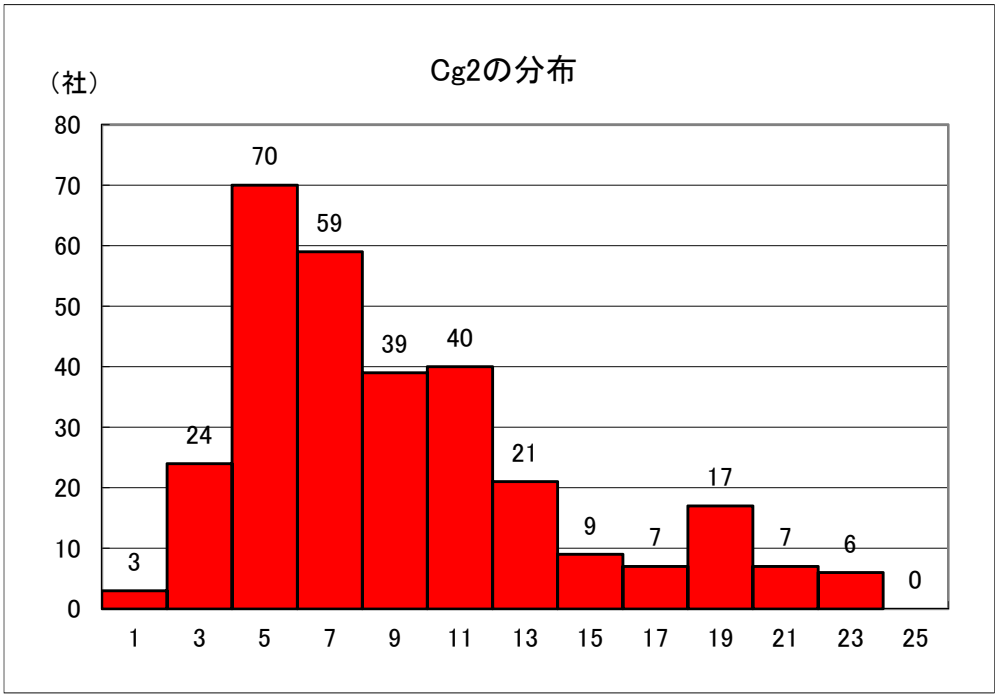
4. Category II (Structure and function of board of directors)

(1) Distribution of category II (Cg2), and definition of high and low Cg2 groups

High and low Cg2 firms are defined as follows;

High Cg2 group: 46 firms for which Cg2 is 14 or over
Low Cg2 group: 27 firms for which Cg2 is 3 or under

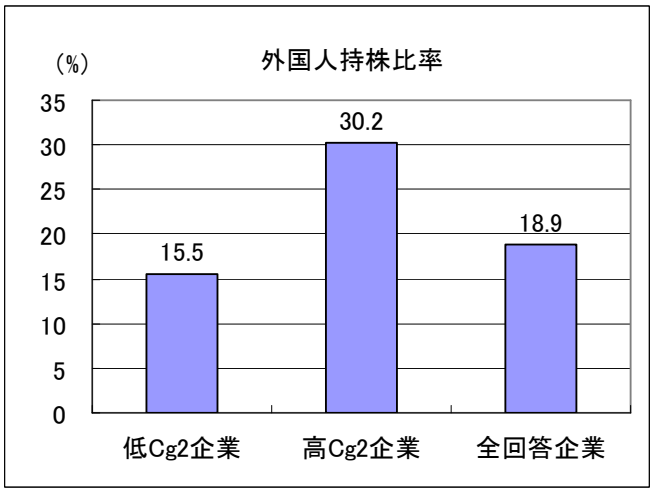
Distribution of Cg2



Mean: 8.7, Standard deviation: 5.0, Maximum, 23, Minimum 1

(2) Cg2 and firm characteristics

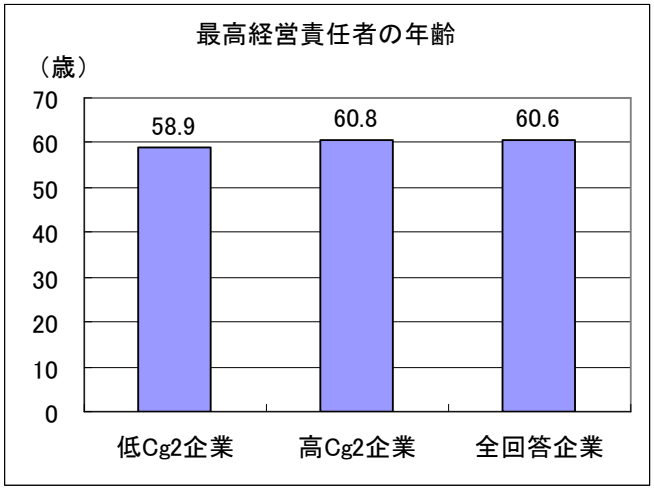
a. Percentage of foreign ownership



Foreign ownership is higher in high Cg2 firms than in low Cg2 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 282
High JCGIndex firms: 45
Low JCGIndex firms: 26

b. Age of CEO

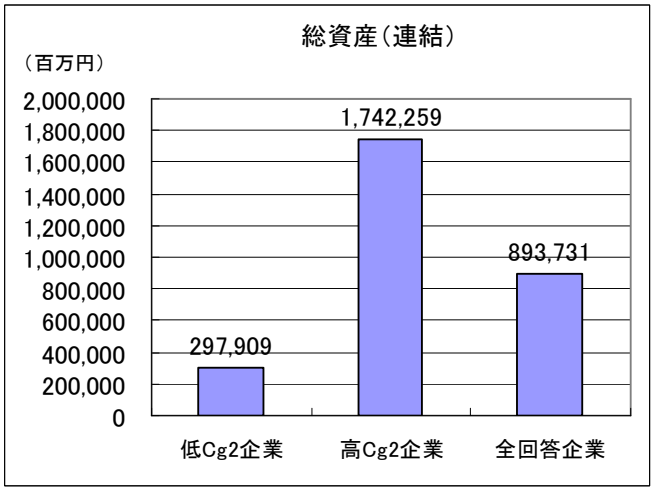


The CEOs of high Cg2 firms are older than CEOs of low Cg2 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 279
High JCGIndex firms: 45
Low JCGIndex firms: 23

(3) Cg2 and firm size

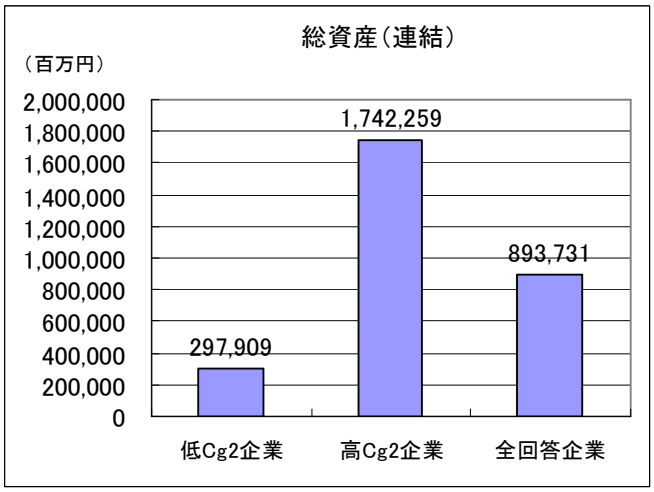
a. Total assets (consolidated, average of 3 years)



Total assets of high Cg2 firms are greater than total assets of low Cg2 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 40
Low JCGIndex firms: 25

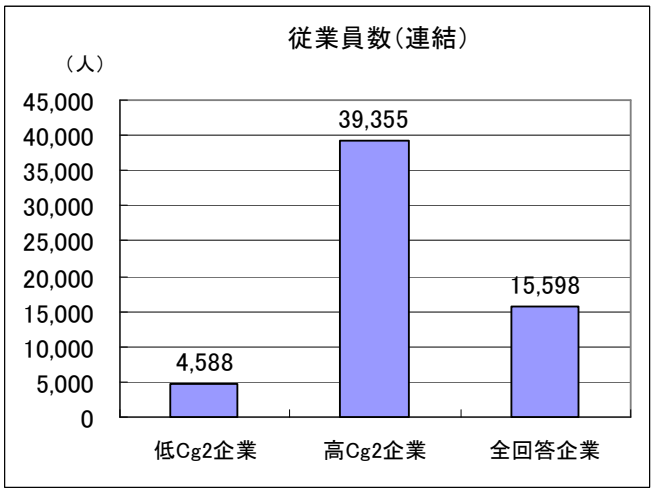
b. Total sales (consolidated, average of 3 years)



Total sales of high Cg2 firms are greater than total sales of low Cg2 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 40
Low JCGIndex firms: 25

c. Number of employees (consolidated, average of 3 years)



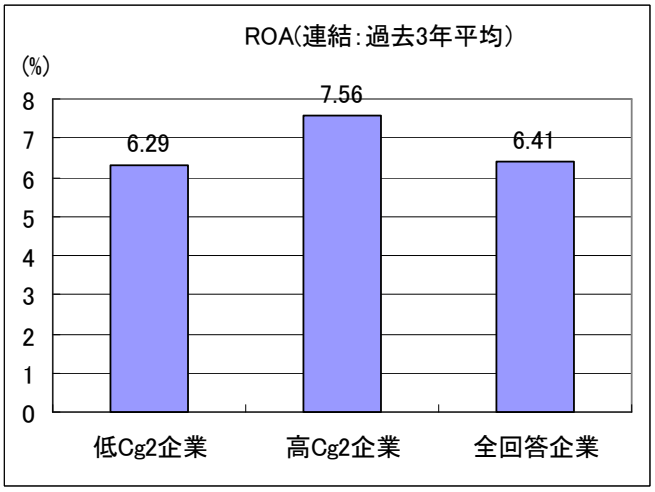
Number of employees of high Cg2 firms is greater than number of employees in low Cg2 firms, and this difference is significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 40
Low JCGIndex firms: 25

(4) Cg2 and rate of return on capital

a. ROA (consolidated, average of 3 years and 5 years)

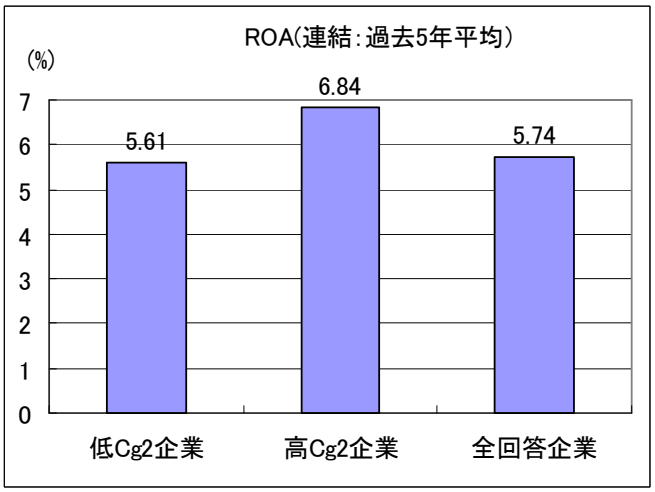
<3 years>



ROA for high Cg2 firms is higher than ROA for low Cg2 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 266
High JCGIndex firms: 38
Low JCGIndex firms: 25

<5 years>

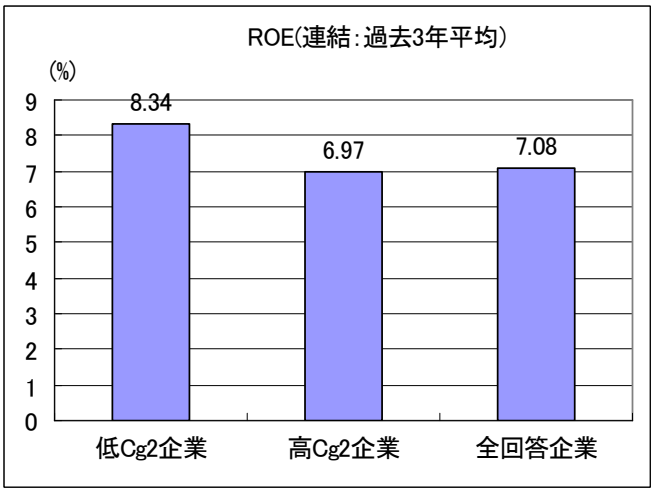


ROA for high Cg2 firms is higher than ROA for low Cg2 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 256
High JCGIndex firms: 37
Low JCGIndex firms: 23

b. ROE (consolidated, average of 3 years and 5 years)

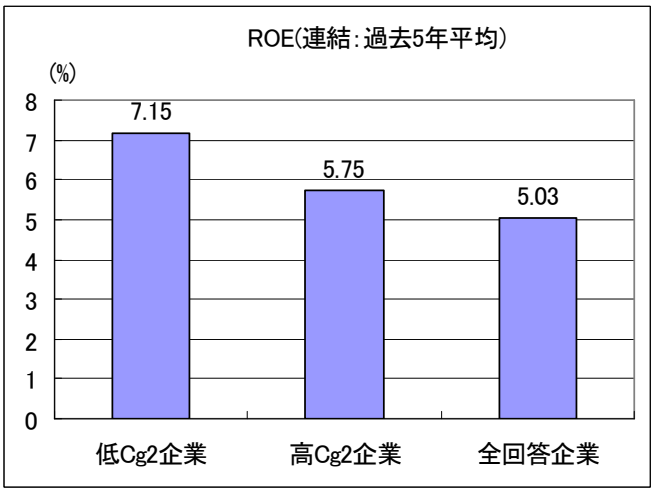
<3 years>



ROE for low Cg2 firms is higher than ROE for high Cg2 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 264
High JCGIndex firms: 38
Low JCGIndex firms: 25

<5 years>

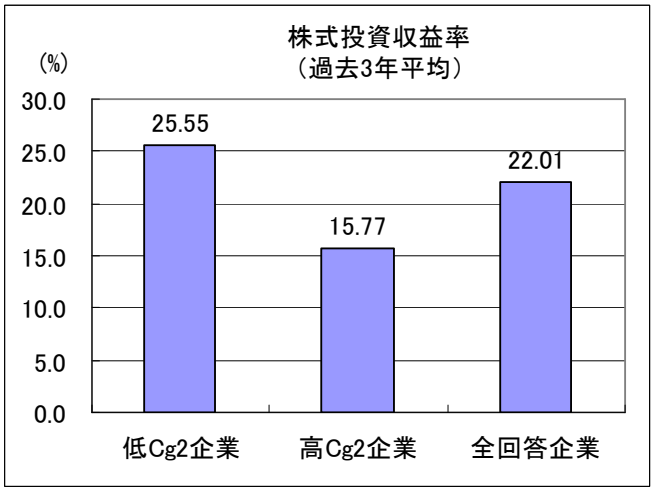


ROE for low Cg2 firms is higher than ROE for high Cg2 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 253
High JCGIndex firms: 36
Low JCGIndex firms: 23

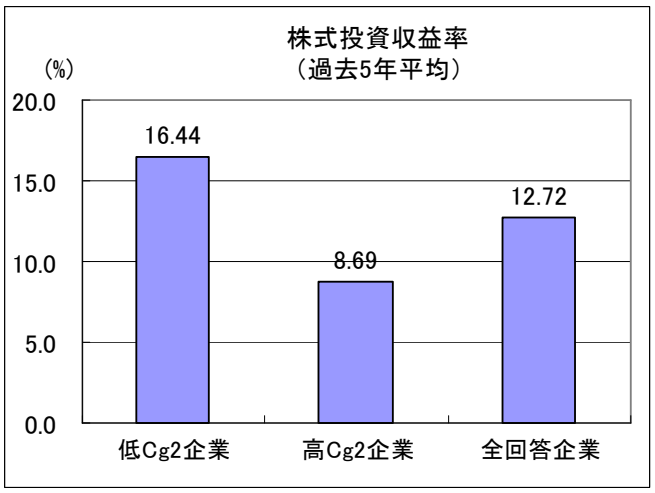
(5) Cg2 and return on common stock (average of 3 years and 5 years)

<3 years>



Return on common stock for low Cg2 firms is higher than return on common stock for high Cg2 firms, and this difference is statistically significant (at the 5% level).
Total responding firms: 270
High JCGIndex firms: 42
Low JCGIndex firms: 24

<5 years>



Return on common stock for low Cg2 firms is higher than return on common stock for high Cg2 firms, and this difference is statistically significant (at the 1% level).

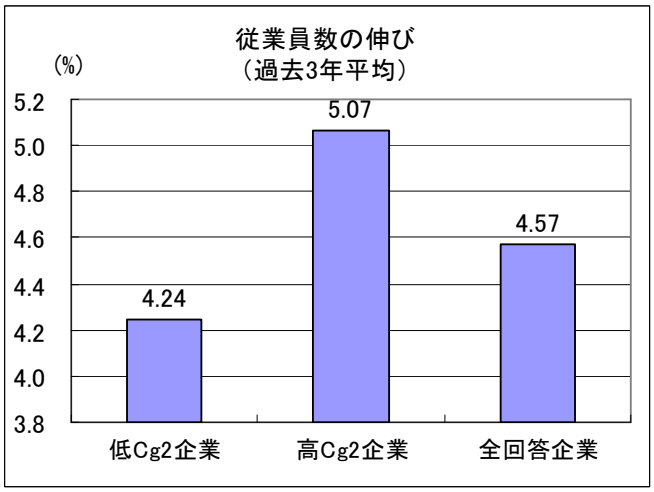
Total responding firms: 246
High JCGIndex firms: 39
Low JCGIndex firms: 21

<adjustment for risk>

The following table shows the betas of high and low Cg2 firms for 3 and 5 years. The significance level of the difference between the betas of high and low Cg2 firms is 5% for 3 years, and 1% for 5 years. During these periods, some of the downside risk of the high Cg2 firms is seen; even though the risk is higher for higher Cg2 firms, the return on common stock was lower for these firms.

	3-year β	5-year β
High Cg2 firms	1.113	1.079
Low Cg2 firms	0.863	0.779
All responding firms	0.902	0.906

(6) Cg2 and growth in number of employees (consolidated, 3-year growth)



Growth in employment for high Cg2 firms is higher than growth in employment for low Cg2 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 270*
High JCGIndex firms: 40
Low JCGIndex firms: 25

*1 outlier was removed.

5. Category III (Management system)

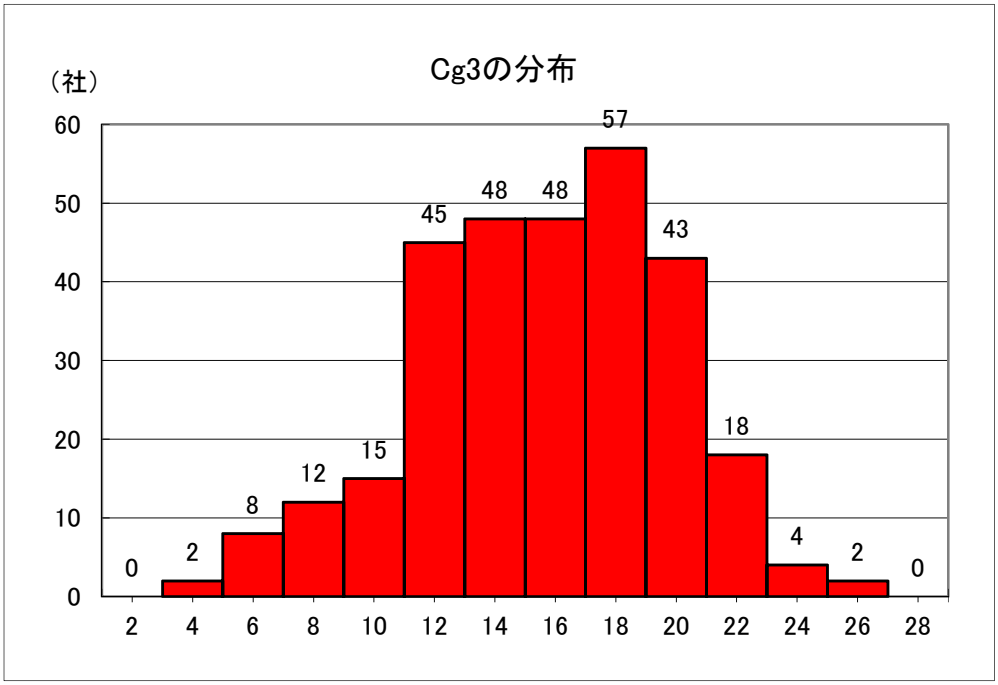
(1) Distribution of category III score (Cg3), and definition of high and low Cg3 groups

High and low Cg3 firms are defined as follows;

High Cg3 group: 44 firms for which Cg3 is 20 or more

Low Cg3 group: 49 firms for which Cg3 is 11 or less

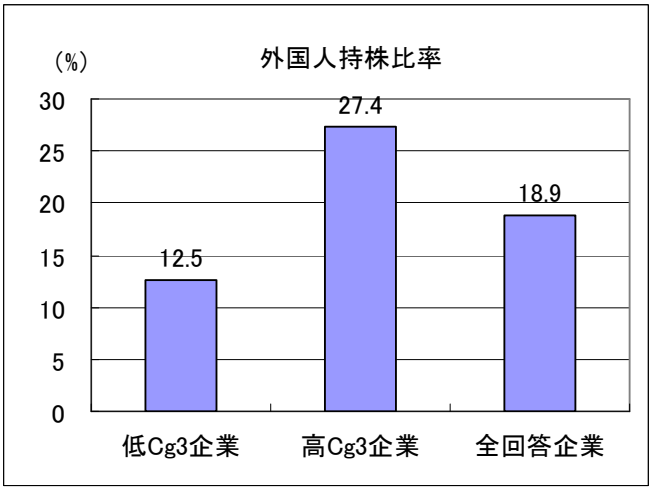
Distribution of Cg3



Mean: 15.1, standard deviation: 4.1, maximum, 26, minimum 4

(2) Cg3 and firm characteristics

a. Percentage of foreign ownership



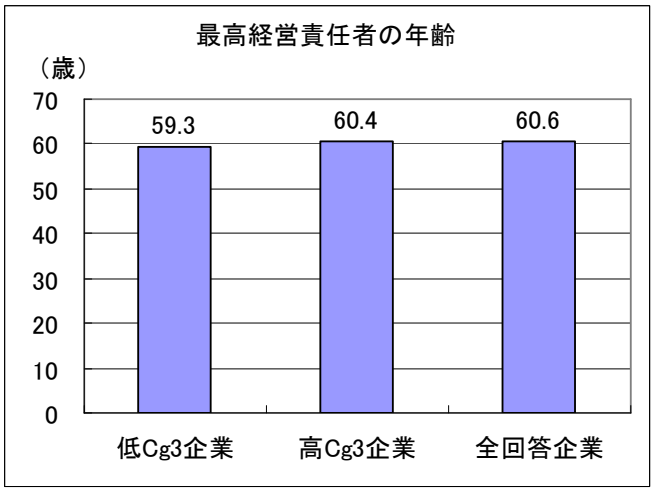
Foreign ownership is higher in high Cg3 firms than in low Cg3 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 282

High JCGIndex firms: 43

Low JCGIndex firms: 47

b. Age of CEO

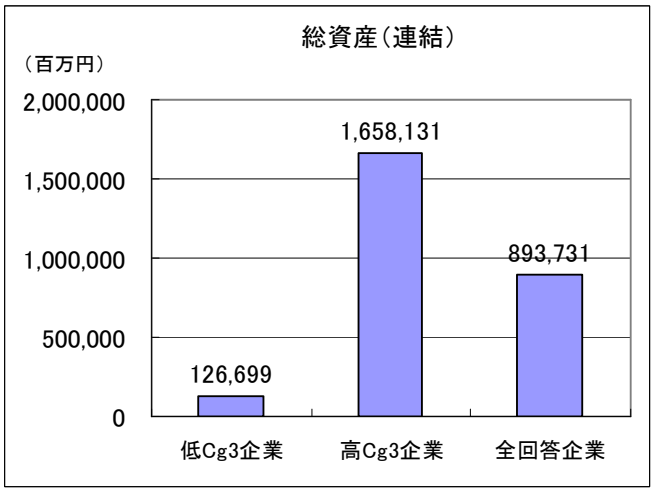


The CEO's of high Cg3 firms are older than CEO's of low Cg3 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 279
High JCGIndex firms: 41
Low JCGIndex firms: 41

(3) Cg3 and firm size

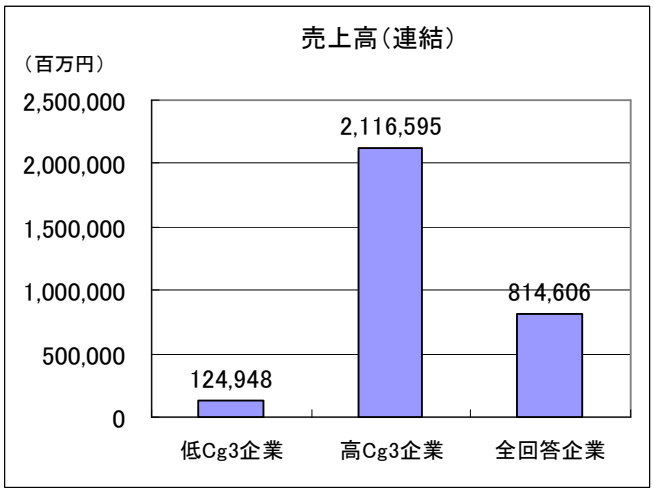
a. Total assets (consolidated, average of 3 years)



Total assets of high Cg3 firms are greater than total assets of low Cg3 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 40
Low JCGIndex firms: 41

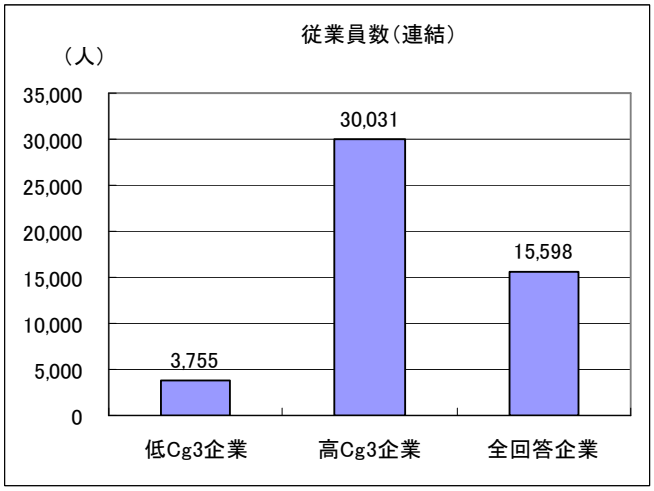
b. Total sales (consolidated, average of 3 years)



Total sales of high Cg3 firms are greater than total sales of low Cg3 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 40
Low JCGIndex firms: 41

c. Number of employees (consolidated, average of 3 years)



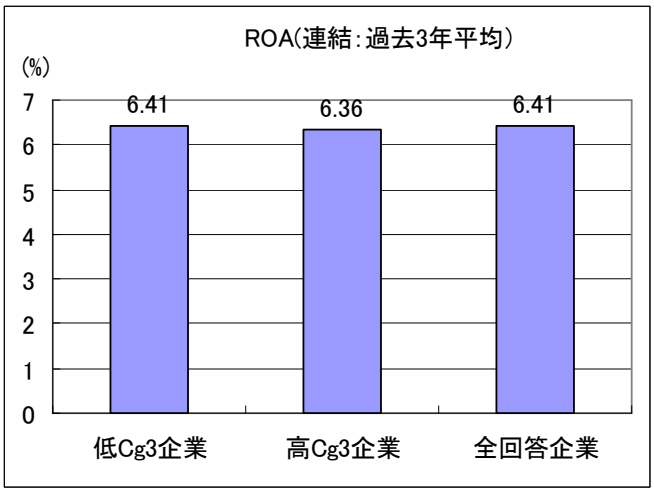
Number of employees of high Cg3 firms is greater than number of employees in low Cg3 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 40
Low JCGIndex firms: 41

(4) Cg3 and rate of return on capital

a. ROA (consolidated, average of 3 years and 5 years)

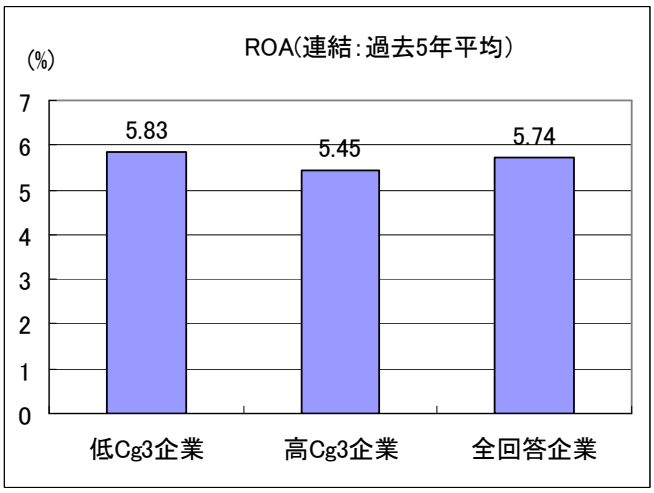
<3 years>



ROA for low Cg3 firms is higher than ROA for high Cg3 firms but this difference is not statistically significant (at the 10% level).

Total responding firms: 266
High JCGIndex firms: 39
Low JCGIndex firms: 41

<5 years>

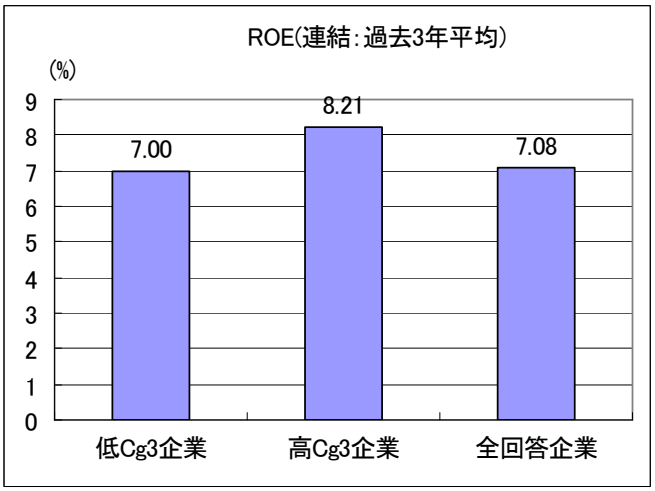


ROA for low Cg3 firms is higher than ROA for high Cg3 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 256
High JCGIndex firms: 38
Low JCGIndex firms: 39

b. ROE (consolidated, average of 3 years and 5 years)

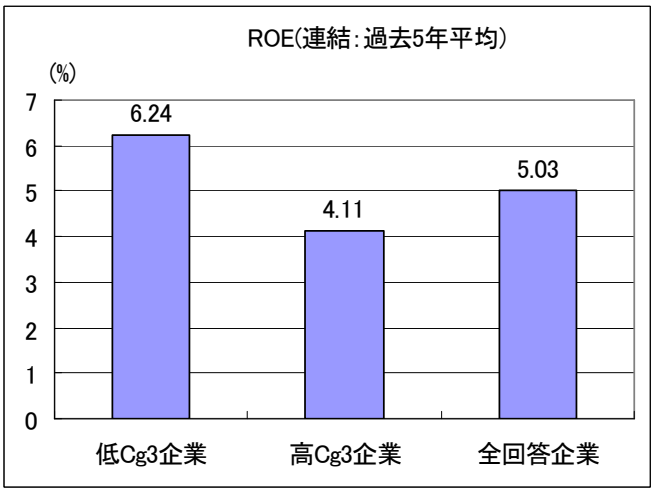
<3 years>



ROE for high Cg3 firms is higher than ROE for low Cg3 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 264
High JCGIndex firms: 39
Low JCGIndex firms: 41

<5 years>

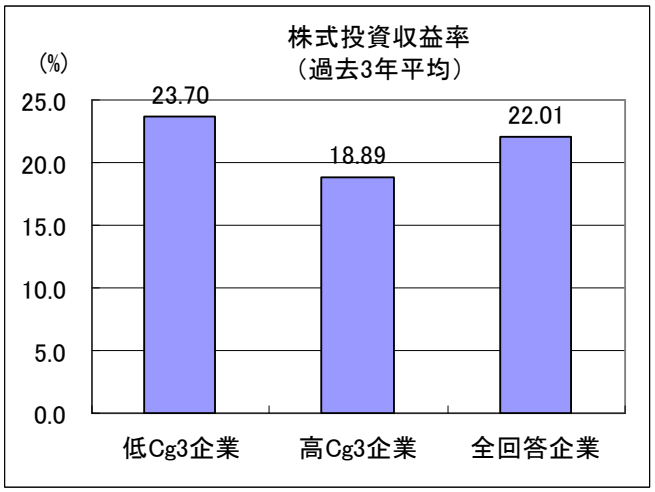


ROE for high Cg3 firms is lower than ROE for low Cg3 firms, and this difference is statistically significant (at the 10% level).

Total responding firms: 253
High JCGIndex firms: 38
Low JCGIndex firms: 39

(5) Cg3 and rate of return on equity investment (average of 3 years and 5 years)

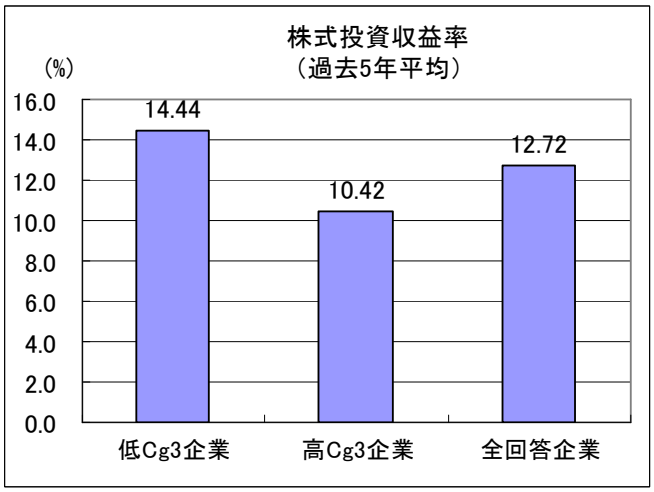
<3 years>



Return on common stock for low Cg3 firms is higher than return on common stock for high Cg3 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 270
High JCGIndex firms: 42
Low JCGIndex firms: 44

<5 years>



Return on common stock for low Cg3 firms is higher than return on common stock for high Cg3 firms, and this difference is statistically significant (at the 5% level).

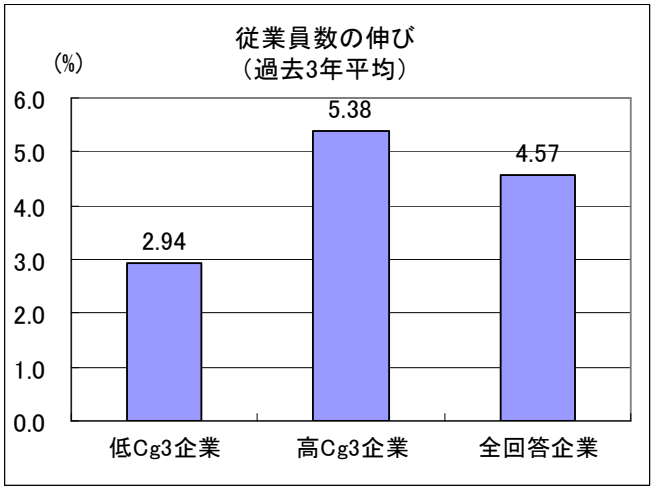
Total responding firms: 246
High JCGIndex firms: 40
Low JCGIndex firms: 38

<adjustment for risk>

The following table shows the betas of high and low Cg3 firms for 3 and 5 years. The difference between betas for the two groups is statistically significant only for 5 years (at the 5% level).

	3-year β	5-year β
High Cg3 firms	1.045	1.078
Low Cg3 firms	0.891	0.875
All responding firms	0.902	0.906

(6) Cg3 and growth in number of employees (consolidated, 3-year growth)



Growth in employment for high Cg3 firms is higher than growth in employment for low Cg3 firms, and this difference is statistically significant (at the 10% level).

Total responding firms: 270*
High JCGIndex firms: 40
Low JCGIndex firms: 41
*1 outlier was removed.

6. Category IV (Transparency and communication with shareholders)

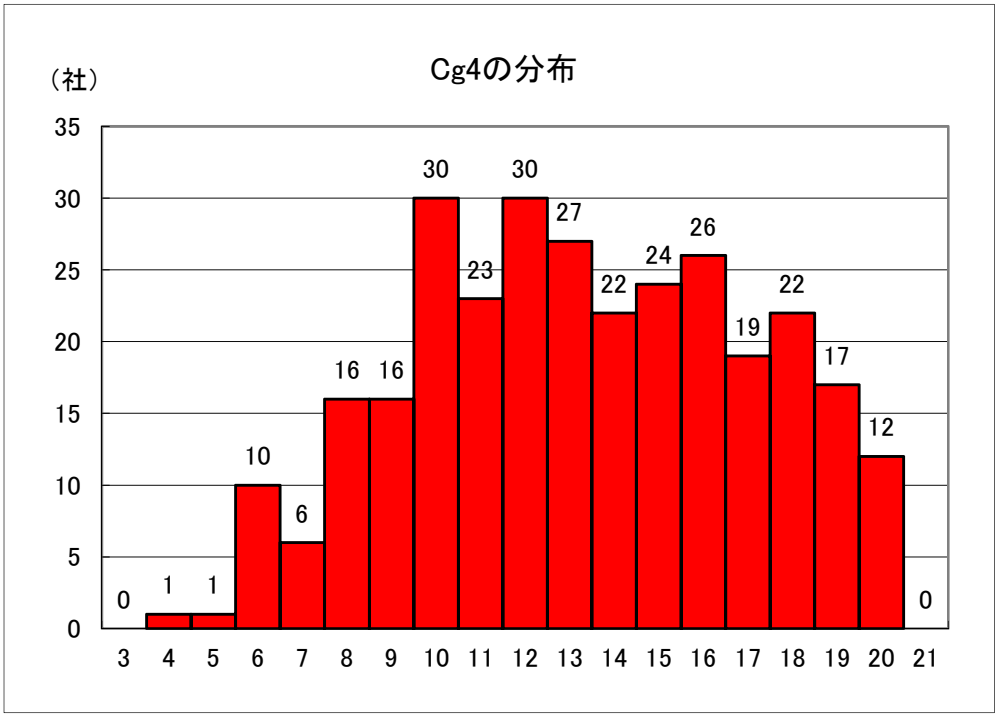
(1) Distribution of category IV (Cg4), and definition of high and low Cg4 groups

High and low Cg4 firms are defined as follow;

High Cg4 group: 51 firms for which Cg4 is 18 or over

Low Cg4 group: 50 firms for which Cg4 is 9 or under

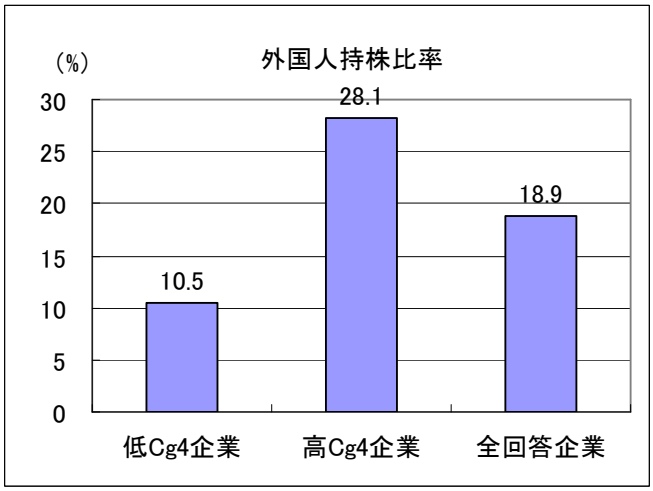
Distribution of Cg4



Mean: 13.3, standard deviation: 3.8, maximum, 20, minimum 4

(2) Cg4 and firm characteristics

a. Percentage of foreign ownership



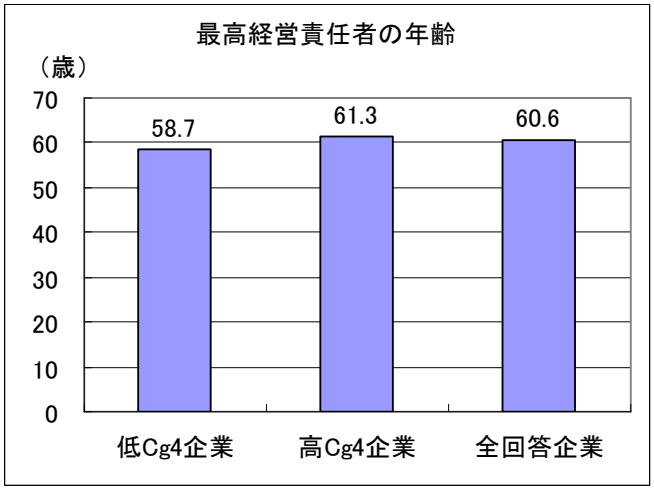
Foreign ownership is higher in high Cg4 firms than in low Cg4 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 282

High JCGIndex firms: 50

Low JCGIndex firms: 47

b. Age of CEO

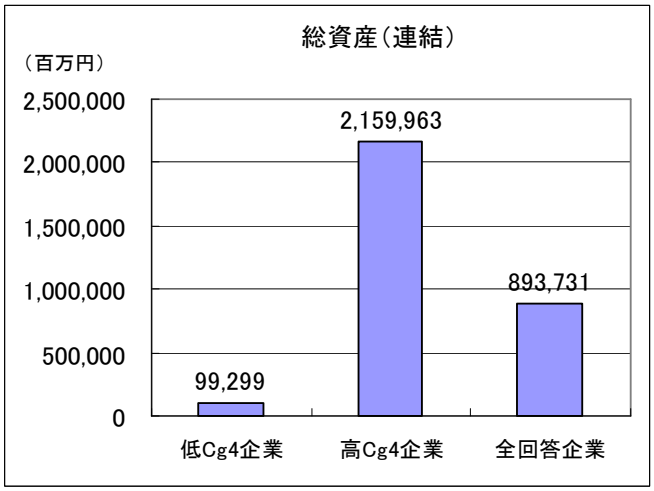


The CEOs of high Cg4 firms are older than CEOs of low Cg4 firms, and this difference is statistically significant (at the 5% level).

Total responding firms: 279
High JCGIndex firms: 48
Low JCGIndex firms: 43

(3) Cg4 and firm size

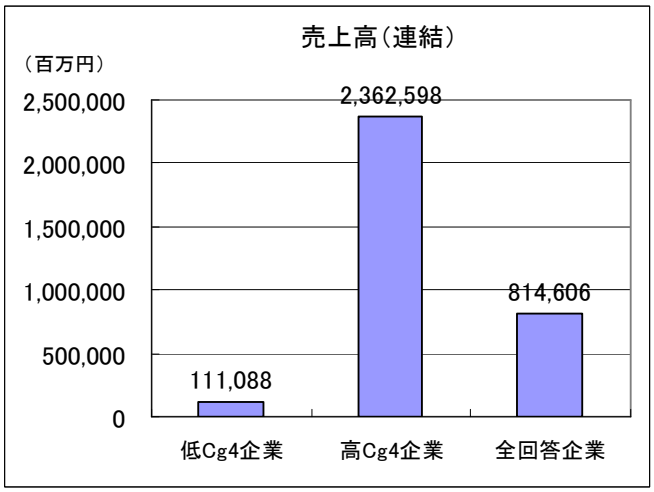
a. Total assets (consolidated, average of 3 years)



Total assets of high Cg4 firms are greater than total assets of low Cg4 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 44
Low JCGIndex firms: 44

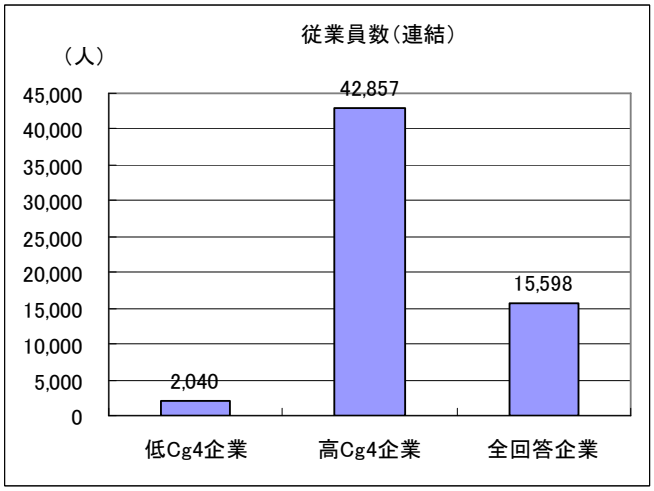
b. Total sales (consolidated, average of 3 years)



Total sales of high Cg4 firms are greater than total sales of low Cg4 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 44
Low JCGIndex firms: 44

c. Number of employees (consolidated, average of 3 years)



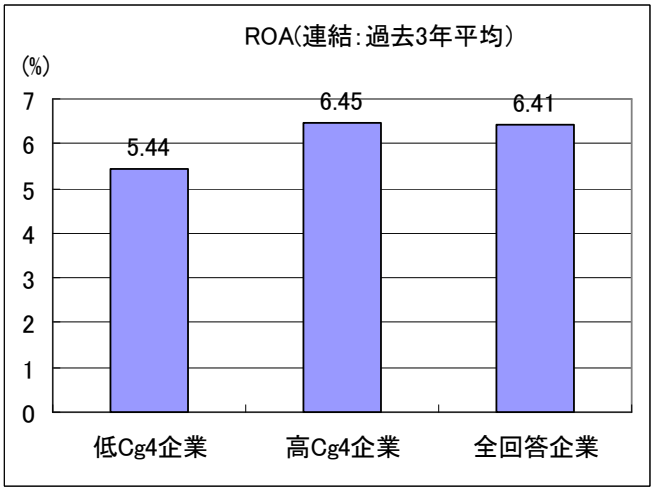
Number of employees of high Cg4 firms is greater than number of employees in low Cg4 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 271
High JCGIndex firms: 44
Low JCGIndex firms: 44

(4) Cg4 and rate of return on capital

a. ROA (consolidated, average of 3 years and 5 years)

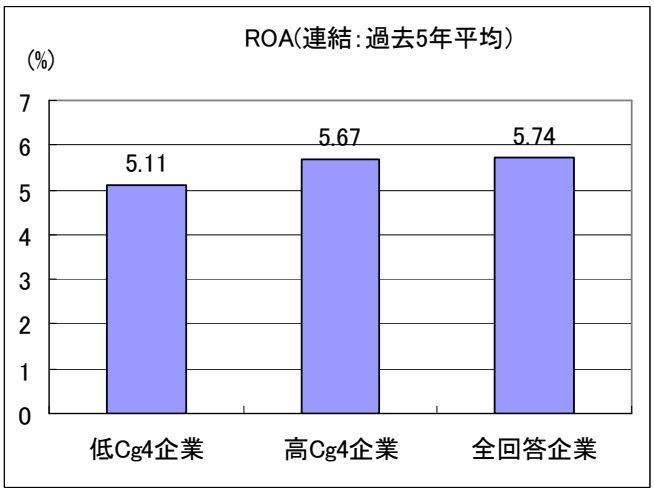
<3 years>



ROA for high Cg4 firms is higher than ROA for low Cg4 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 266
High JCGIndex firms: 43
Low JCGIndex firms: 46

<5 years>

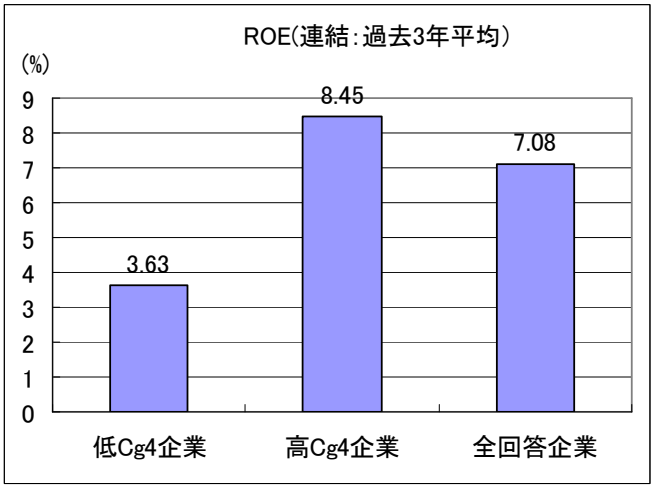


ROA for high Cg4 firms is higher than ROA for low Cg4 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 256
High JCGIndex firms: 39
Low JCGIndex firms: 41

b. ROE (consolidated, average of 3 years and 5 years)

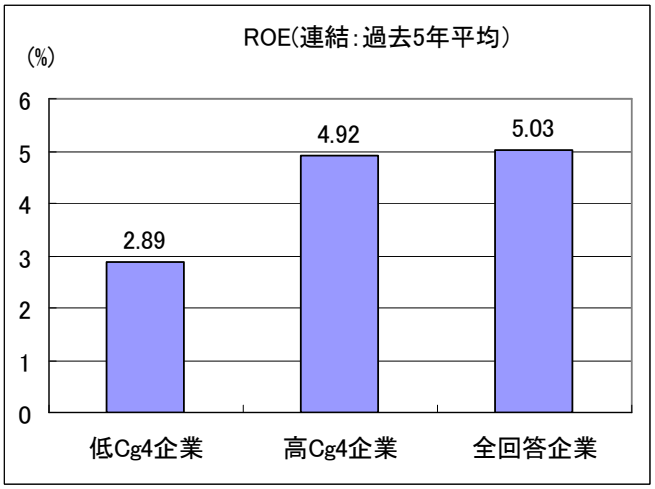
<3 years>



ROE for high Cg4 firms is higher than ROE for low Cg4 firms, and this difference is statistically significant (at the 5% level).

Total responding firms: 264
High JCGIndex firms: 43
Low JCGIndex firms: 43

<5 years>

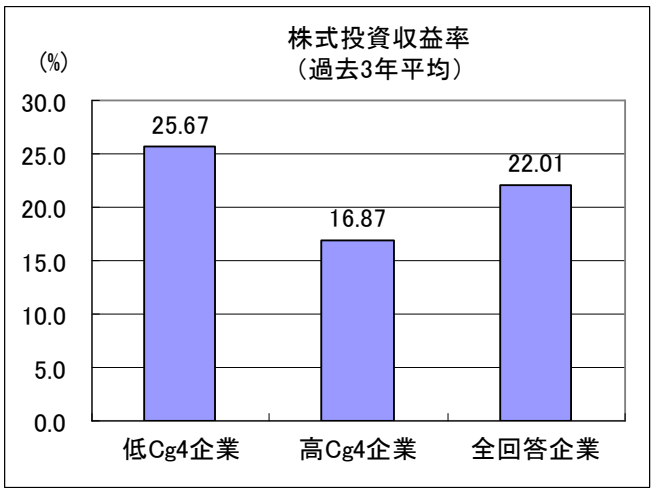


ROE for high Cg4 firms is higher than ROE for low Cg4 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 253
High JCGIndex firms: 39
Low JCGIndex firms: 40

(5) Cg4 and rate of return on equity investment (average 3 years and 5 years)

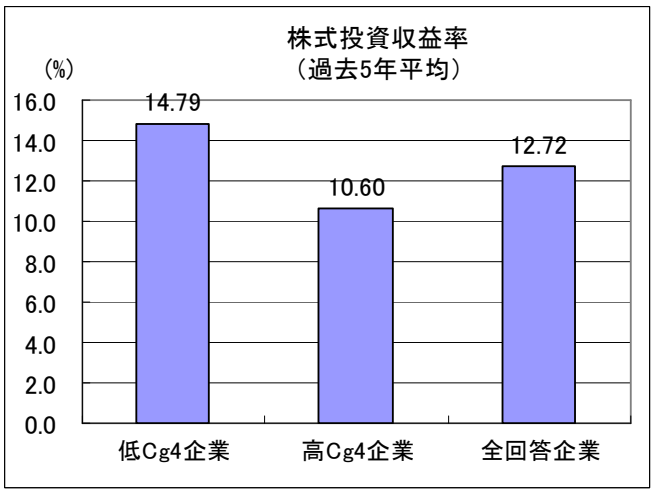
<3 years>



Return on common stock for low Cg4 firms is higher than return on common stock for high Cg4 firms, and this difference is statistically significant (at the 1% level).

Total responding firms: 270
High JCGIndex firms: 46
Low JCGIndex firms: 44

<5 years>



Return on common stock for low Cg4 firms is higher than return on common stock for high Cg4 firms, and this difference is statistically significant (at the 1% level).

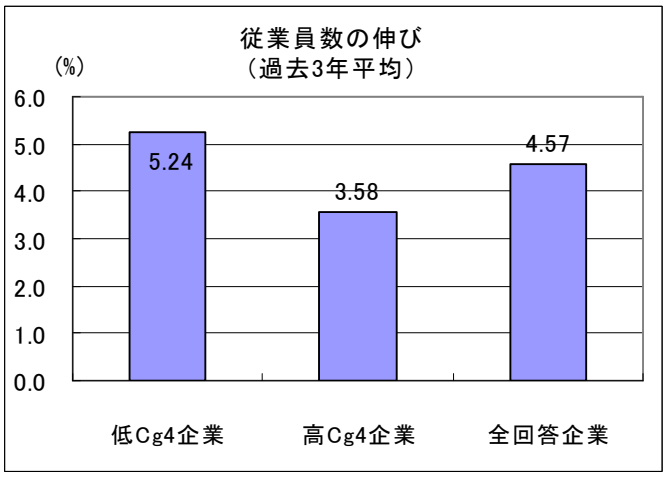
Total responding firms: 246
High JCGIndex firms: 43
Low JCGIndex firms: 39

<adjustment for risk>

The following table shows the betas of high and low Cg4 firms for 3 and 5 years. The difference between betas for the two groups is statistically significant for both 3 and 5 years (at the 1% level).

	3-year β	5-year β
High Cg4 firms	1.059	1.059
Low Cg4 firms	0.770	0.788
All responding firms	0.902	0.906

(6) Cg4 and growth in number of employees (consolidated, 3-year growth)



Growth in employment for low Cg4 firms is higher than growth in employment for high Cg4 firms, but this difference is not statistically significant (at the 10% level).

Total responding firms: 270
High JCGIndex firms: 44
Low JCGIndex firms: 44

Conclusion

Over 5 consecutive years, a total of 660 firms have responded to the JCGIndex survey. In each year, these responses have shown a clear relationship between the JCGIndex and firm performance. High JCGIndex firms enjoy superior performance to low JCGIndex firms. The closer a firm's governance system is to the JCGR corporate governance model, the more value it provides to its shareholders.

Compared to 2002-2004, however, the level of statistical significance in comparisons of performance for high and low JCGIndex groups has declined since 2005, and high JCGIndex firms do not necessarily provide a higher return to shareholders. One possible explanation is that firms that have recently been experiencing poor performance have embarked on governance reforms. As a result, the high JCGIndex group mixes firms that have excellent performance and governance with troubled firms that have recently revised their governance systems. We are conducting further research to better understand this phenomenon.

When evaluating the results, it is necessary to keep the following in mind: First, these results reflect past performance and do not necessarily mean a future relationship. Second, while the sample size of 302 is in itself is not small, it represents only 20% of the about 1,700 Tokyo First Section listed firms. However, over five years, we have found very similar results among different sets of responding firms. This suggests that while the annual sample size has been small, our findings are robust. Third, the relationship between the JCGIndex and financial results that we show here is correlation, and not causation, and further research is necessary to establish causal relationships.

We JCGR, an NPO operated by unpaid staff, greatly owe to donors who have a profound understanding on corporate governance. We are all the more obliged to maximize your kind support by continuing the Corporate Governance Survey so that we can offer ever more convincing proposals underpinned by the accumulation of data.

(Note)

An explanation of the data used for analysis

1. Industry classifications
   Tokyo Stock Exchange industry classifications
2. Financial data
   Source: NEEDS (Nikkei Shinbunsha data bank)
   Firms covered: Tokyo Stock Exchange First Section firms (1,747 firms as of November 18, 2006).
   Items: Total assets, sales, number of employees, ROA, ROE (firm-based and consolidated)
   Period: January 2001 to December 2005
3. Return on common stock
   Source: Nihon Shoken Keizei Kenkyusho 2005 Kabushiki Toshi Shueki Ritsu
   Firms covered: Tokyo Stock Exchange First Section firms (1,747 firms as of November 18, 2006).
   Items: Monthly returns on individual stock and market
   Period: January 2001 to December 2005
4. Beta
   Calculated by Fujitsu Research Institute Source: Toyo Keizai Inc., “Stock Price CD-ROM 2005”
5. Calculation of characteristics of the responding firms
   Average, minimum, maximum and standard deviation of the responded firms were compared with those of the Tokyo Stock Exchange First Section firms, based on consolidated financial data for the previous 3 or 5 years.

	item	consolidation	term	data	Formula
1	total assets	○	3year average	NEEDS total assets (FB144)	total assets＝total debts＋total equities
2	sales	○	3year average	NEEDS sales (FC001)	revenue from sales activities as operating activities
3	ROA	○	3year average	NEEDS ROA（FP01034）	return on asset＝（operating income＋interest and discount charge income）／total of debt・minority interest・assets of 2 period -average×100
4	ROE	○	3year average	NEEDS ROE(FP01147)	return on equity＝net income／total equities of 2period-average×100
5	employees	○	3year average	NEEDS employees (FE056)	number of employees at year-end
6	stock return	－	3year average	Nihon Shoken Keizei Kenkyusho stock return	① Calculated monthly stock return ② Calculated average of period covered (1year, 5years, 10years)

Note 1) Tokyo Stock Exchange First Section firms: 1,747 firms as of 11/18/2006
The number of Tokyo Stock Exchange First Section firms was 1,696 when JCGR sent the mail survey as of 07/13/2006.
Note 2) Consolidated accounting takes priority according to SEC accounting requirements.