

Japan's Soaring Land Prices

By Hiroshi Takeuchi

Japanese land prices are soaring—not only in Tokyo but also in Osaka, Nagoya and all the other major urban areas. Nor is this phenomenon restricted to the downtown areas; it extends even into the suburbs. According to figures released recently by the National Land Agency, the price of an average commercial site in Tokyo went up 34.4%, and an average residential site 18.8%, in 1986 (Fig. 1; see also Table 2, p. 43). This in turn had a ripple effect that pulled up prices in all of the score of other cities with populations of 500,000 or more. Likewise, the Economic Planning Agency's *Annual Report on National Accounts* gives a total value of ¥1,051 trillion (approx. \$7.5 trillion at ¥140/\$) for all Japanese land as of the end of 1985—an increase of over ¥600 trillion (approx. \$4.3 trillion), or 133%, over the last 10 years.

There are a number of reasons for these stratospheric land prices. The first is the recent boom in demand for office space. Companies need more room now, and the new "intelligent" buildings have twice as much space per employee as the older buildings do. Much of this space is needed for the computers and other information-processing equipment that companies need to stay competitive.

Land prices have been affected as Japanese society has become conspicuously more international, more deregulated and more information oriented. This is evident even in the building where I work. IBM has the first three floors, Lloyds Bank is on the fourth floor, and the tenth through twelfth floors are occupied by the giant American securities company Merrill Lynch. Japan is more open than ever before, and all of the big international companies are flocking to Tokyo, expanding their offices and beefing up their staffs in an effort to take advantage of the information revolution that is taking place here. Thus the demand for office space is driving up land prices.

The second, and perhaps the most important, reason is that there is so much money floating around. As Japanese companies have cut back on capital in-



There are good reasons why land prices in Japan are high, but the problem has gotten out of hand.

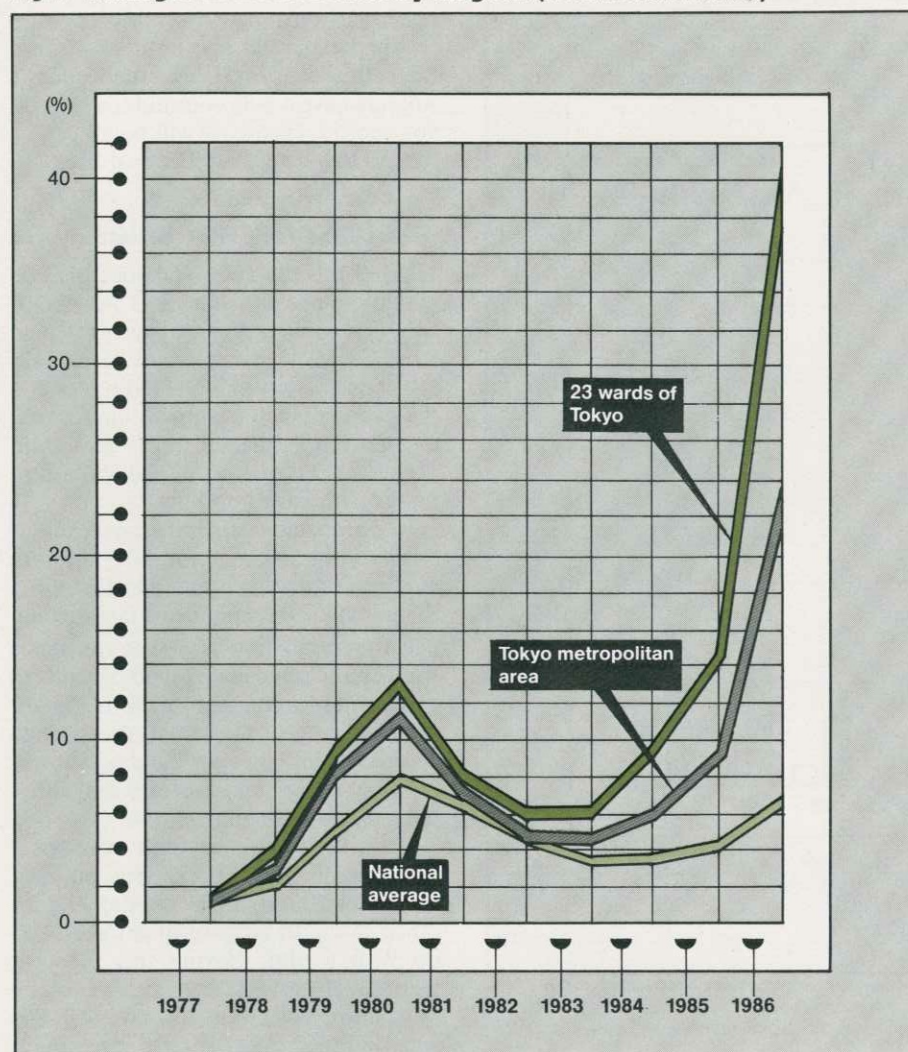
vestment and the government has tightened its belt, excess liquidity has been created with nowhere to go. Likewise, the yen's appreciation over the past two years and the collapse in oil prices have given companies ¥14 trillion in windfall profits—money that is not being plowed back into building plants or expanding facilities because of the pessimistic economic outlook. And because the official discount rate is a fantastically low 2.5%, putting your money in the bank is little better than putting it in the *futon*. With interest rates so low, companies are finding rapidly rising land and stocks better investments than financial instruments.

Is public works a cure?

On top of this, the government has shifted to easier money in a bid to prevent a recession. The normal prescription for

a recession (in this case brought about by the yen's appreciation) would be a heavy dose of government public works spending, but the government is already deep in the red and does not have much leeway for additional deficit spending. And even if the government did try to pump up the economy with pork-barrel projects, it would not have much of an impact because 80% of the money would be drained off just paying for the sites. If, for example, the government spent ¥1 trillion on public works and the whole ¥1 trillion went for road construction or other infrastructure improvements, the multiplier effect would mean that the ¥1 trillion would translate into ¥2-¥3 trillion in demand and the government could expect to get part of this back in taxes. But with ¥800 billion disappearing for site acquisition, the only multiplier effect is that from the remaining ¥200 billion.

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Fig. 1 Changes in Land Prices by Region (commercial sites)

Source: Survey of Prefectural Land Prices, National Land Agency

Since it is impossible to hope for much of a boost from government spending, the government has instead turned to easier money. But easier money in the face of a sluggish economy is like pushing on a wet noodle, and the excess liquidity has gone off in unexpected directions to drive up the price of land, stocks and even golf-club memberships.

Given this situation, people with money to spare have decided that the demand for downtown land is far from satiated and have started speculating in real estate. Downtown Tokyo land prices are out of sight as a result. And people who sold their holdings in the downtown area have been driven to buy up extensive holdings in upper-class suburban areas by a provision of the tax law providing tax-free treatment for home-sale profits so long as the money is used to buy another home. This has in turn driven up suburban land prices. A speculative herd psychology has been generated that says you should buy now before things get any more expen-

sive. Urban land prices—and even suburban land prices—are going up all over Japan as a result.

Sapping productive resources

Of course, there is nothing wrong with land prices going up gradually as the economy grows—and it is probably a good thing that they should rise somewhat, since land prices are one barometer of economic activity. As is sometimes pointed out, you could buy the whole United States twice over for the total price of all the land in Japan, and the reason for this is that Japan has about 10% of the world's GNP crammed into a very small area. Even though the United States might have three times the GNP, it has far less than half the GNP per land area. In that sense, it is only right that Japanese land should be expensive. This is the perfect place to locate plants. Transportation is

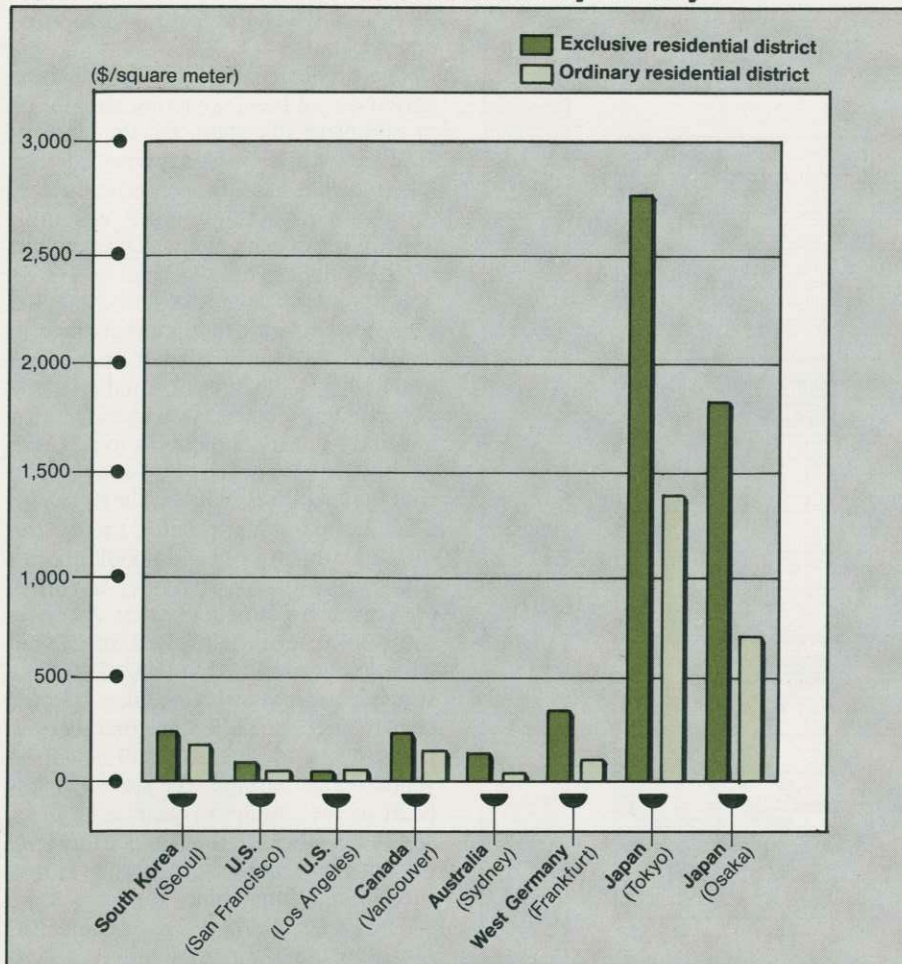
convenient to almost everywhere, and there is a large pool of highly skilled workers available.

The problem is that land prices have gotten out of hand, shooting straight up in complete disregard for the pace of GNP growth. For land prices all over Japan to soar like this, cut loose entirely from any moorings with economic growth, it can only mean that economic mechanisms are not working.

Soaring land prices are suffocating the economy. Businessmen cannot hope to buy land at today's inflated prices, and even if they could buy and build on it, the new building would be so expensive that it would be nearly impossible to pay for it in the normal course of business. With land selling for ¥30 million (about \$216,500) per square meter, there is no way any company—be it a noodle shop, a department store or whatever—can break even on an investment like that. A noodle shop on a newly purchased site would have to charge ¥1,500 (about \$10) for a simple, no-frills bowl of noodles. It would have to price itself out of the market even before it started. There are still a lot of old shops doing business on land that has been in the family for years and years, and these shops are managing to survive, but anyone trying to start fresh on a new site faces an impossible situation.

These high land prices are also one reason why other Japanese prices are so high, since land prices are reflected in high price tags on almost everything. For example, Japanese consumer prices are now about three times what they are in the United States. A cup of coffee that costs about ¥100 in the United States will cost you about ¥300 in Japan. So even though Japan's per capita national income may be the world leader at \$15,000, since prices are three times what they are in the United States, this is actually equivalent to only about \$5,000 in U.S. purchasing power. As a result, Japanese living standards are still low despite the nominal affluence. This is not only true in comparison with the United States. The Japanese salaried worker in Tokyo probably does not even live as well as his Korean counterpart in Seoul (Fig. 2). The average worker in Seoul has a nice house with about twice as much room as the Tokyo worker has, and even though Seoul has a population of about 10 million and only four subway lines, the average commuting time is only about 40–50 minutes. By contrast, hour-and-a-half commutes are not uncommon in the Tokyo area.

And as downtown commercial sites have gone up, the trickle-out effect has

Fig. 2 Residential Land Price Differentials by Country

Note: The Shoto area in Shibuya was taken as a typical exclusive residential district and the Matsubara area in Setagaya as a typical ordinary residential district in Tokyo, the Tezukayama area in Sumiyoshi as a typical exclusive residential district and the Minoo 3-chome area in Minoo as a typical ordinary residential district in Osaka.

Sources: Survey Results of International Land Values 1982, Japanese Association of Real Estate Appraisal; Foreign Economic Statistics Annual, Bank of Japan

pushed suburban residential land prices up as well, pushing workers who want to buy homes farther and farther out from the center of town. If you think today's workers have a long commute, wait until you see the encore. It will be all people can do to get to the office and back.

Tax holding, not sales

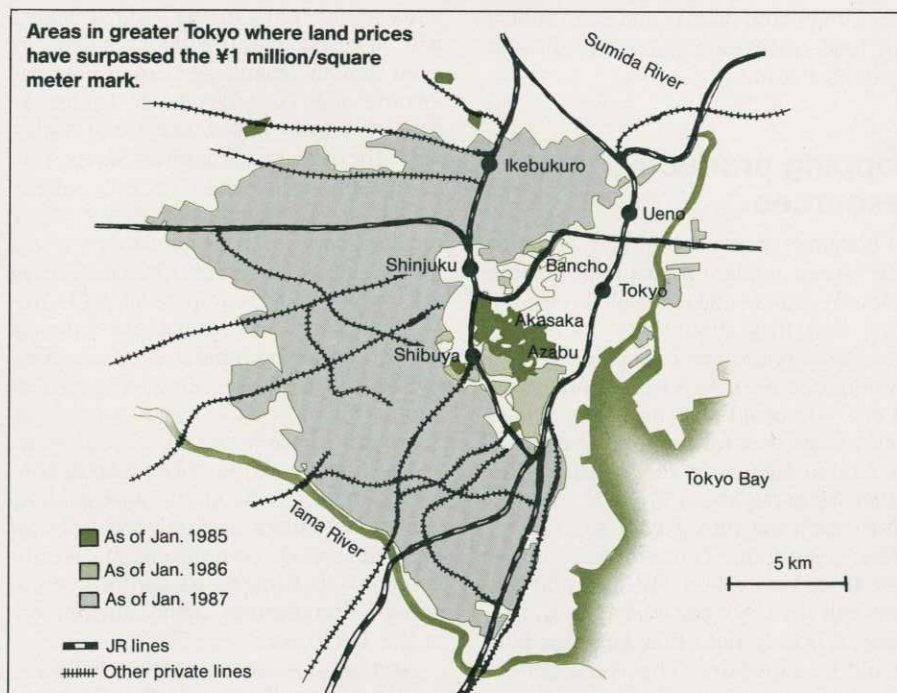
While this run-up in land prices may be making some companies and individuals rich, it is doing nothing whatever to help most honest companies and hard-working people. Even though land prices and the economy will eventually find a new equilibrium as market forces come into play, it will take an act of political will to bring them back into line.

It is imperative that the government screw up its courage and take the bull land market by the horns. The first thing to be done is to announce a far-reaching plan to redevelop such idle sites as waterfront landfills and abandoned railyards to quash land speculation in Tokyo and environs. These plans should also include specific target dates for building subway line extensions, expressways and other infrastructure amenities.

If all of these sites were developed, there would be a rush of new building that could quickly meet the demand for office space. In fact, we might even end up with a glut. Having this prospect before them would very quickly cool the speculative fever that has swept Tokyo and drain off most of the increase in land prices.

Orthodox policies are also needed to increase the supply of land. One way would be to up the tax on holding land and lower it on trading land (Table 1). If it were possible to jack up the tax cost of holding land in downtown Tokyo, most people would want to sell their land and move someplace where the tax costs were lower. Holding the tax on the profit from selling land down would also be an added incentive to sellers. Another obvious policy possibility is to tax agricultural land in urban areas, and even suburban areas, at the same rates as the surrounding land, be it commercial or residential. This issue of reforming land taxes is certain to come increasingly to the fore as an important policy issue.

Liberalizing agricultural imports and creating a more competitive market can also play an important role in encouraging part-time farmers to make their land available for other uses. If the amount of available land increases, land prices will not go up as fast and it will be cheaper to build roads, railways and other infrastruc-



Sources: Tokyu Land Corporation

Table 1 Property Taxes in Leading Industrialized Countries

	FY	Property tax as percentage of national income	Property tax as percentage of tax revenues
Japan	1970	1.0	5.4
	1975	1.5	7.9
	1980	1.7	7.3
U.S.	1970	4.3	15.0
	1975	4.3	15.6
	1980	3.2	11.1
Britain	1970	4.6	11.1
	1975	4.7	12.6
	1980	4.9	12.0
France	1970	1.1	3.9
	1975	1.3	4.3
	1980	1.4	4.5
West Germany	1970	0.5	1.7
	1975	0.5	1.7
	1980	0.5	1.6

Note: Property taxes have been figured taking the fixed property tax, city planning tax and special land holding tax (instituted in fiscal 1973) for Japan; property taxes for the United States; rates for Britain; *foncier bâti, foncier non bâti* and *taxe d'habitation* for France; and *Grundsteuer* for West Germany.

Source: *Issues in National and Local Government Finances and Tax Policy*, Financial Research Institute, Japan Legislation Society, 1985

ture facilities. The readier availability of faster and more convenient transportation between the downtown areas and the suburbs might encourage people to commute from these new areas and hence disperse land demand somewhat.

If air and rail transport networks can cut the time to Tokyo from outlying areas, this may stem the steady influx of population into Tokyo. In the longer run, however, it may well be necessary to consider ways of reversing the concentration of business, political and cultural interests in the Tokyo area and decentralizing Japanese society.

Although there is no guarantee that these policies will make more land available, that the availability of land will facilitate building, that the resultant building activity will stimulate the economy, that today's excess liquidity can be directed into production, and that it will be possible to stop the land speculation, it is certain that Tokyo and the other great Japanese cities will be unable to meet the international information revolution's challenges and that Japan will become an economic backwater if nothing is done.

Stimulate by restructuring

If the government will move energetically to abolish its confining restrictions, not only on the use of land but also on

agriculture, services and the rest of the economy, there should be a burst of growth as innovative people find new ways to use the outstanding facilities at their command more productively. Japanese manufacturing workers have worked their way to the forefront in international productivity, and there is no reason why people in other sectors could not do the same if they were allowed.

This revitalization with new economic structures would naturally stimulate new capital investment, in large part for new machinery and construction works—a boost to domestic demand that could more than make up for the contraction in demand resulting from the shrinkage of the trade surplus. If this were done, the Japanese economy would grow normally and nonmanufacturing sectors would be more modern and more efficient, with the result that there would be a sharp improvement in the quality of Japanese life. It might even be possible for the country with the world's top per capita GNP to have the world's top living standards as well.

Happily, these changes are already under way in the economy. In April 1985, the Nippon Telegraph and Telephone Public Corporation (NTT) was privatized and Japanese telecommunications lines are just as deregulated as American lines. Three new companies are poised for

entry into the domestic telecommunications market, 300 value-added communications networks have been established, and over 300 new cable television operations have been set up. The telecommunications industry has been unleashed, and it has become lively as a result.

Continuing this trend, the Japanese National Railways (JNR) was privatized and broken up this April, and the new regional railway companies are engaged in ambitious programs to spruce up their stations, renovate their rolling stock and redevelop their idle real estate and other assets. This is bound to be another strong source of productive investment.

Even the tax picture is changing as there is talk of reducing direct taxation and raising indirect taxation. In the long run, corporate income taxes have to come down or companies will find it too expensive to locate in Japan. It is impossible to tell what will happen to the idea of a value-added tax, now that it has been killed once in the Diet, but I suspect it would have gotten a more favorable reception if it had been a flat 3% across the board rather than 5% with a confusingly complex exemptions schedule.

Agriculture is another area where reform is urgently needed. As the government idles more and more paddy land in an effort to maintain the balance between supply and demand, this is increasingly antagonizing the big full-time farmers, and the national "Nokyo" agricultural cooperative may be the ultimate victim. Blindly resisting import liberalization will simply mean that Japanese agriculture is less and less competitive.

This is not as it should be. Japan is ideally suited to agriculture. There is rich soil and abundant rainfall, the people are hardworking, and the farm machinery is the best there is. There is no reason why Japanese agriculture should not be able to compete on world markets. In fact, Japanese eggs are among the cheapest in the world. Seeds and seedlings are competitive. Vegetables are competitive. All of the fields that are out from under the yoke of government controls are holding their own. But where the government's heavy hand is evident, productivity goes down the tubes and the price of Japanese rice ends up nine times more expensive than the international market price.

Agriculture used to be a sacred cow, but people are now talking about radically liberalizing farm imports. A new wind is clearly blowing. The Japanese economy is moving toward major changes, and today's exorbitant land prices will have been a blessing in disguise if they accelerate this movement.