

# Weaker Foundations

With the momentum from several years of strong growth, the real estate and construction industries have generally done well in fiscal 1990, even though there are signs that the easy-money boom may be ending.

With strong front-loading of housing starts in the first half of the year to get in ahead of the anticipated higher interest rates, starts were higher in first-half fiscal 1990 than in 1989. At the same time, the very tight labor situation has leveled out the peaks and troughs on the supply side, even as real estate companies faced with higher interest rates have sought to lighten their interest liabilities by getting their inventories to market as quickly as possible. As a result, it is expected that fiscal 1990 housing starts will be a strong 1.6 million at least.

In nonresidential construction, plant and equipment investment, especially in manufacturing industry, has started to taper off. This is because of the sense of uncertainty about corporate earnings resulting from higher oil prices as a result of the Gulf crisis, higher labor and other costs due to the labor shortages, and higher capital procurement costs as a result of higher interest rates and soft stock prices.

Nevertheless, this sector is expected to continue strong for some time to come because companies are still repositioning and restructuring for long-term diversifi-

cation, because it is impossible to cut corporate strategic investment in preparation for the imminent structural changes, and because the government has made a commitment to massive public works spending as part of its Structural Impediments Initiative (SII) agreement with the United States.

Thus nonresidential construction will continue strong and total starts are likely to total 260 million square meters (about the same as fiscal 1989). In money terms, the up-scaling of the market is likely to mean that the total investment will be over ¥77 trillion (approximately 6% more than in fiscal 1989).

In housing, the higher interest rates, lending stringency and uncertainty about what land prices are going to do are expected to induce a wait-and-see attitude among consumers in fiscal 1991. Accordingly, the slower pace of starts that showed up in the second half of fiscal 1990 will probably continue in fiscal 1991, and the market will argue for slower growth once the real estate companies have sold off their surplus property inventories. Given this, rental housing is likely to suffer the sharpest decline.

Although subject to the same rebuilding demand schedule as owner-occupied homes, rental property starts will track actual demand very closely.

With the lull in home purchasing, investment buying is also off and people are



People flock to see show houses on new developments. But a lull in purchases of new homes is expected in 1991, and housing starts may slip below 1.5 million.

being much more selective about where they put their money. As a result, how well a given property does will depend more on the property itself than on any vague "market conditions," and generalization will become more difficult. Another factor that has to be considered is the softness in the used home market, since this hobbles people who intend to sell their old homes and move to higher grade accommodation. As a result of all of these factors, there is a very real possibility that housing starts may slip below the 1.5 million mark in fiscal 1991.

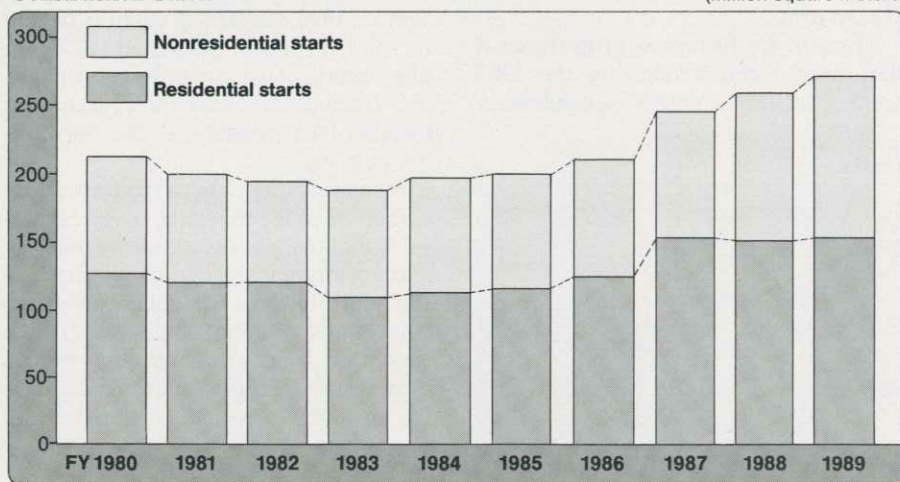
Yet the construction industry will be sustained in fiscal 1991 by its massive back-orders and by the many new development projects being planned. Basically, the industry is expected to enjoy a stable year. Nonetheless, complacency would definitely be out of order, since the economic outlook is uncertain and companies are rethinking their capital investment plans.

One final note on this industry: Japan's politicians and bureaucrats are making noises about enacting some kind of new land-holding tax. Because this new tax is intended to make land-holding more expensive, it stands to reason that it should promote more efficient use of land and encourage people to sell their unused or little-used property. At the same time, it will also create bottom-line pressure on rental properties. While it is still too early to tell what will come of this debate in the Diet, this is something that, like the bank restrictions on financing real estate deals, warrants careful attention.

(Nobuo Jinnai, economist)

## Construction Starts

(million square meters)



Source: Annual construction statistics, Ministry of Construction