

Topics

Japanese Structural Changes

Vol.1 Land Prices

Are Japanese Land Prices Still Expensive?

The series of three “Topics”, named “Changes in the Japanese Structure” will explore structural changes that are impacting Japan currently, including land prices, asset’s holding structure and capital flows.

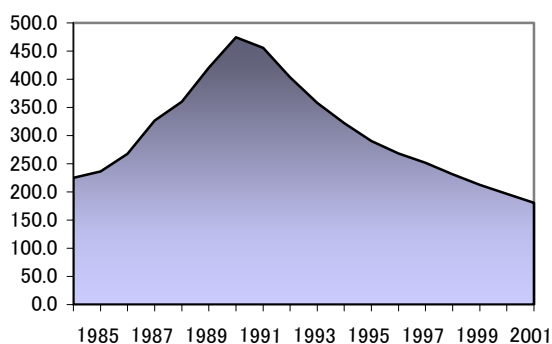
The first issue of the series deals with land prices. Japanese land price have increased fivefold during the bubble economy, however, they have been decreasing for over ten years since the collapse of the bubble economy. It is difficult to explain this phenomenon merely by the economic cycle theory. Moreover, it cannot also be explained as an adjusting trend, since the land values have dropped below the level of the pre-bubble period and still decreasing.

Are Japanese land prices still expensive? Some say that Japanese land is still expensive and will continue to decrease. Their reason is that the Japanese economy should be viewed within the global economy, and that the land prices will go down to the equilibrium point resulting from the competition with China and other Asian nations.

However, others say that current Japanese land prices are undervalued and have dropped more than they should. This was common opinion in 1995, since the prices declined below the pre-bubble level.

As of the moment, the former global equilibrium theory seems to be widely accepted. Graph 1 below shows the movement in land prices before and after the peak of the bubble economy. Land prices have already exceeded the level of a simple adjustment of the bubble economy. Therefore, adjustment of the bubble economy may not be the only reason why land prices are decreasing.

Graph 1: Movement of Official Land Price



Source: Land, Infrastructure and Transportation Ministry

Note: Index-linked price in each year is calculated according to 1970 price being 100.

Eiji Enomoto

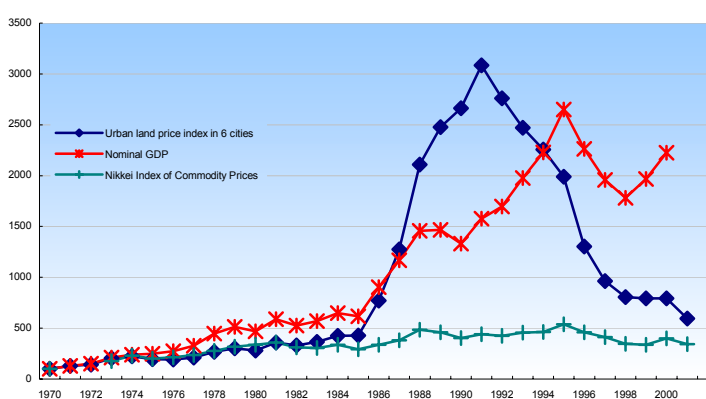
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The global equilibrium theory should be examined to see if Japanese land prices remain too expensive. The easiest way to accomplish this, as is done by global corporations to compare their costs, is to convert prices in to US dollars. To what extent have Japanese land prices changed on the basis of the US dollar?

Graph 2 shows the price index in US dollars since 1970, when \$1 was ¥360. What is significant here is the comparison between “Urban land price index on 6 cities” and “Nikkei commodity price index”. “Commodity price index” is said to reflect the global price trend, since it consists of goods such as soybeans, sugar, cotton, wool, oil and iron and steel, i.e. goods that are traded frequently in global market.

Graph 2: Price Index in US Dollar



Source: Nominal GDP: Cabinet Office, Nikkei Index of Commodity Prices: NIKKEI, Urban land price index in 6 cities: Japan Real Estate Institute

Note: Calculated in US\$, 1970 price being 100

This graph shows that land prices during the bubble economy were incredibly high. Land prices rose five times in yen, however, they increased tenfold on the basis of the US dollars. Japanese land prices have become higher than we expected based on dollar (i.e. on global view) since 1985, after the Plaza Agreement, however, the land prices have been adjusted to global standard from 1992 to 2002. The above graph also indicates that the land prices should soon be recover the healthy balance with price index as it did in 1985. Although one final adjustment is still required, land price should hit the bottom in near future.

Compared with GDP, which has been in the recession for a long time, land prices are also showing a trend like other import commodities. This is caused by the global competition, and can be viewed as a symbol of Japanese structural changes. I believe that global comparison is crucial in the present real estate price analysis

Eiji Enomoto