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C I T

LVT: SHOCK THERAPY WORKS IN JAPAN

A TOP British real estate agency has launched an index of land values, which it says could be used to forecast trends in the economy.

Four years ago, when the Centre for Incentive Taxation launched EI as a monthly economics bulletin, we warned that land prices were a major signal of the state of health of the economy. Few of the experts listened.

During those Lawson boom years, EI was the sole harbinger of bad news based on an analysis of the dangers of exponential growth in land prices. Month-by-month we tracked the economy and explained that land prices would be the first to peak and turn down - followed by a crash in construction, which would lead the economy into a pit.

Now Hillier Parker, whose head of research is EI reader Russell Schiller, has published *Residual Land Values*. Affirms Mr Schiller: "Had such an indicator been in existence four years ago (sic), some of the damage caused by too much development, leading to oversupply, could have been avoided." Such an indicator was, of course, available four years ago to EI readers!

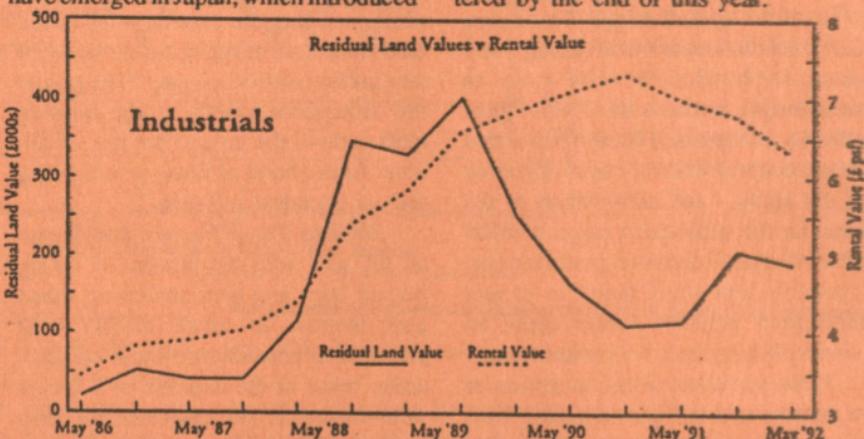
Hillier Parker's calculations of profits to be made out of land deals indicate that values fell during the late-1980s boom - as EI warned at the time (the trend for industrial land is shown in the graph). Explains Mr Schiller: "When the residual land value of a site is calculated to be lower than the open market land value, the site is not worth developing."

The Hillier Parker index (reviewed in *Land & Liberty*, Sept.-Oct., 1992, p.6) adds further evidence for the cyclical pattern of 18-year land prices which have repeated themselves around the world for the last 200 years.¹ Hillier-Parker records the rise in land values from 1985 to the peak (1988-89). The accelerated growth in UK land prices was documented in

Costing the Earth, a CIT study published in 1989.² Updated figures have regularly appeared in EI, whose focus now shifts to the problem of restoring full employment: see pages 2-4.

LAND DATA, by itself, cannot help the policymakers. Forecasters will now have to redeem themselves by rewriting the parameters of their models on the basis of a theory that makes sense of the real world.

◆ Clues to the appropriate reforms have emerged in Japan, which introduced



a land-value tax (LVT) this year (see *Land & Liberty*, May/June, p.3). The tax was designed to curb land speculation, and is already working. After a disastrous crash in house-building last year, the economy is now experiencing a recovery in construction - the only buoyant sector in Japan, right now. Reason: the land-value tax is forcing idle urban land into use.

Owners used to pretend their valuable acres were farmland (frequently, they did not even bother to gather in the rice). This forced land prices upwards as cities sprawled outwards. Japanese "farmers" are now leading the way in the house-building sector. Firms that make steel-frame prefabricated houses report a recovery in business. Foreign investors are

buying their shares. Foreign investors' holdings in Daiwa House Industry shares have jumped to over 16%.

The OECD and the Japan Center for Economic Research forecast a growth rate for this year which is the lowest since 1974 - the last time Japan suffered a land-led crash. The index of industrial production has been negative since last October. But analysts now say that the stimulative effects of the housing upturn will be felt in the rest of the economy: they hope the macro-economic benefits will be registered by the end of this year.

EI is less optimistic: the land-led crisis in the real estate sector will continue for more than another year, with banks tightening credit in response to their sour real estate loans. But there is no doubt that it was the shock therapy of LVT on over-priced paddy fields which has nurtured the first seeds of recovery.

Meanwhile, in Britain, the construction sector has registered a 19% drop in orders. Half the UK's senior property directors and fund managers now say there will be no pick-up before the end of 1994, and a quarter of them pessimistically forecast recovery in 1995 or later.

1. *The Power in the Land*, Fred Harrison, Shepheard-Walwyn, 1983.
2. *Costing the Earth* (editor: Ronald Banks), London: Shepheard-Walwyn, 1989.