Jolt for Japanese

JAPAN'S annual $80 bn trade surpluses have fuelled one of the hottest bouts of land speculation ever experienced in this century. The Paris-based Secretariat of the OECD commends a tax on the value of land as a necessary reform. DAVID REDFEARN reports.

THE OECD has urged Japan to place a tax on land values. "The present tax system", it states "tends to discourage the release of underused land."

It goes on: "Nonetheless, reform is urgent. Distorting markets and using land inefficiently has (sic) a significant adverse effect on living standards".

In other words, inequitable land tenure and taxation causes poverty.

The Paris-based Organisation for Economic Co-operation and Development is not a reforming body so nothing must be expected resembling open denunciation of economic systems as they are. Nevertheless, between the lines of the carefully veiled language, and alongside the customary emphasis on the minutiae of trade balances and monetary strengths and weaknesses, it is possible to read an all-too-familiar story.

• OSAKA'S office blocks boom is not matched by housing construction.

First there is some recognition of poverty, and how it is affected by current economic developments. For example, although there was a rise in domestic consumption during 1987, it was to be found more in non-wage-earners' than in wage-earners' households.

This was not surprising because, at the beginning of a period of boom, unearned income rises more rapidly than earned. The fortunate recipients of this unearned income will also be the ones to benefit if, as is hoped, recent increases in imports can be maintained to give home consumers the advantage of the high yen.

All the same, there has been recent discussion in the Diet about the possibility of achieving another cut in income tax by the introduction of broadly-based indirect taxation. Such taxation, as the survey fails to mention, is guaranteed to bear heavily on the poor, and to let the rich off lightly. This is how the survey deals with poverty. What then does it have to say about some of its effects, though not described as such within its pages?

It is now more than 60 years since Parker Thomas Moon[2] *summarised the economic motives for imperialism, as stated by the imperialists themselves. The ones of interest for our present purpose are:*

(1) the sale abroad of manufactures that cannot be absorbed by the domestic market;
(2) the investment abroad of capital for which the domestic market affords no scope, and
(3) the demand of industrial nations for raw materials that cannot be produced at home.

Moon does not seem to have given due weight to the background to the first two motives namely the low wages that prohibit workers from consuming the equivalent of what they produce.

Japan, activated by the same three motives, is achieving by "peaceful penetration" what she failed in the end to achieve by war.

There appears to have been, in mid-1985, a peak in the last export-led expansion, from which there was a fall-off caused by a large appreciation in the value of the yen. The export of goods and services is projected to rise by 6% in 1988, and by 5 ¼% in 1989.

The authors of this survey

(1) *Japan*, Organisation for Economic Co-Operation and Development, Paris, 1988.
(2) Parker, Thomas Moon, *Imperialism and world politics*, New York: Macmillan, 1926.

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COSTING US DEAR

	Japan	United States	France[1]	Canada
Area (km^2)	377800	9363500	549000	9976000
Density (person/km^2)	324.7	25.5	100.8	3.0
Value of land[2]	4540.0	2950.0	172.1	256.2
(per cent GDP)	317.5	74.7	29.4[3]	70.1
(per cent wealth)	54.9	21.0	7.6[3]	19.9
Value of housing				
(per cent GDP)	49.7	88.4	153.9[3]	64.0
(per cent wealth)	8.6	24.9	39.8[3]	18.2
Value of non-residential structures				
(per cent GDP)	48.9	50.0	92.8[3]	140.0
(per cent wealth)	8.5	14.1	24 [3]	39.8

1. 1983.
2. Dollar billions at purchasing power parity exchange rates in 1985 (which value a dollar at Y 222, FF 7.27 and C$ 1.22).
3. The value of structures includes the value of underlying land.

Sources: OECD, *Main Economic Indicators;* Management and Coordination Agency, *Japan Statistical Yearbook* 1987; National Land Agency, *Land Price Publication;* INSEE, *Comptes des Patrimoines;* Statistics Canada, *The NAtional Balance-sheet Accounts, 1961-1985;* U.S. Federal Reserve *Flow of Funds.*

THE quality of housing in Japan is notoriously inferior to standards in other industrial countries because families cannot afford decent-sized plots on which to construct their homes.

But this is not just a domestic problem. The cost of Japan's residential land affects the rest of the world. For the price of land forces families to save more out of their incomes than ought to be necessary. The Japanese savings ratio is extraordinarily high compared with rates in, say, the USA or Britain.

The result is lower domestic consumption of goods, leaving less scope for other countries to export their products to Japanese consumers.

In Japan, however, an aggressive approach to exporting goods is vital just to keep the output from factories high and unemployment low. This, inevitably, creates an imbalance in foreign trading relationships, and has led to friction which, so far, has been contained within diplomatic channels.

The answer? Says the OECD: "Lower land prices would reduce savings and encourage greater investment in housing. By thus affecting domestic saving-investment balances, this change would tend to reduce the current external surplus."

So lower land prices are the key to higher-quality housing in Japan and less friction between trading partners.

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attribute the failure to achieve a durable change from exports to domestic demand mainly to a subsequent weakening of the yen, thereby showing that they share Moon's blindness to the more influential effect of low wages.

This drive to export is accompanied by the one to invest abroad. The reason for this is not only Moon's "surplus capital", but also the "comparative advantage" of having labour-intensive work, as for example in the textile and electrical industries, done in places where wages are even lower than they are in Japan. Here the place of Korea, Taiwan, Hong Kong and Singapore is being taken over by the Philippines, Thailand, Malaysia and Indonesia.

As a result of these shifts, domestic employment in Japan is estimated to fall by 0.6m by 1995. The consequent lower wages will complete the vicious circle of which the survey shows no awareness.

RAW MATERIALS, the subject of Moon's third point, are now often obtained – peacefully – in exchange for long-term loans. A more insidious tendency, which will make eventual land reform more difficult in other countries, is Japanese investment in real estate overseas.

Once more it must be stated that there is no sign in this survey of any perception that low wages are the ultimate cause of imperialism, warlike or peaceful, or that land value taxation would clear the way for higher ones. In fact, they do not see the distorted land market as much more than an obstacle to home-ownership.

Nevertheless, the facts set out are impressive enough. Despite its relatively small area, 377,800 km² as against the 9,363,500 km² of the United States, the 549,00 km² of France, and the 9,976 km² of Canada, the total value of the land of Japan is more than that of the land of these other three countries put together. *What an opportunity for taxation!*

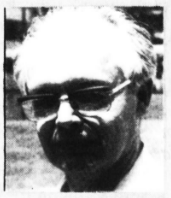
In fact, there is *land value taxation in Japan, but only at the rate of 1.4%, and based on assessments that represent only a fraction of the actual market value. Faced with a significant capital gains tax if they sell, owners naturally prefer to hold, even if they themselves have no immediate use for the land.*

The way in which assessments are falling behind reality is dramatically illustrated by the example of Chiyodaku, where valuation for the holding tax on commercial land fell, between 1984 and 1986, from 15.3% to 6.5% of its current market value.

There was a similar fall, in Minatoku, from 18% to 5.9%; and, in Setagayaku, valuation of land

FINNISH FORAY

Helsinki probes the LVT option



SOARING land prices in Helsinki have panicked Finland's government into proposing a tax on land zoned for multi-family residential buildings. A rate of 10% on the taxable value in the first year diminishes to 5% in subsequent years.

The plan has not received the unqualified blessing of Finland's leading land-use expert, Professor Pekka Virtanen of the Helsinki University of Technology, pictured right.

In recent years, he has published articles in the Finnish newspapers advocating a fully-fledged system of land value taxation - or a partial variant of that fiscal policy, in which the tax rate is reduced on the value of buildings and raised on the value of land.

Even so, Prof. Virtanen reluctantly accepts the new tax as "better than nothing." But, he points out, the tax is shot through with loopholes. Even the municipalities which would gain from the revenue can sidestep the obligation to impose the tax.

"The politicians are being cautious," reports Prof. Virtanen. "They feel that land value taxation is not very popular even among ordinary people, to say nothing of the bigger landowners. They accept the 'penalty tax' because it is a temporary solution, and directed at some bigger landowners, especially the so called 'grunders' or big developers who own large tracts in the Helsinki region.

"This is a typical case where politicians count probable votes and do not think about the problem or the effective solution."

The deterrent effect of the tax on the land hoarders is not likely to be effective. For the assessed value of land in Helsinki is notoriously low, and the gap between taxable and market values has increased in the past 12 months as prices have risen steeply.

A committee set up by the Ministry of Finance to investigate the workings of the property tax is expected to report at the end of January; observers do not expect it to propose radical reforms.

In fact, the Helsinki land market is likely to be aggravated further this year, for the government proposes to raise the tax on the capital gains made from the sale of land. Owners are expected to withhold their sites from the market, thereby restricting the supply of land further - and forcing up prices even higher!

The reasons for the boom in real estate are the same as those that operated throughout the world since the crash of the stock markets in October 1987. Explains Prof. Virtanen:

"Many investors got frightened and sold their bonds and debentures to invest in more secure and concrete objects.

"Simultaneously - by a mere chance - the Bank of Finland slackened its rule that you had to save a certain amount of money (normally 20% of the price of the residence to be bought). Now the lending became 'free'. You could borrow money up to 100% of the value of the house or apartment. Even more than that, you could have 'eternal' loans, i.e. loans for which you only pay interest.

"These two factors suddenly caused a sharp rise in demand, and prices grew at annual rates of 30% to 50%.

"There were no demographic or planning explanations for the steep rise in prices, and foreigners play no role in our real estate market: they have very limited rights to acquire real estate in Finland."

for residential use fell from 19.3% to 16.6% of the market value.

More recent changes are not reflected in these figures; for revaluations are carried out only once every three years. A further limitation is that any tax increase is restricted to 10%.

Taking into account these additional factors, some critics have estimated the average tax rate on land to be only 0.15%, as compared with the nominal 1.4%.

"Reform of the taxation of land," says the survey, "has become more important given the rapid recent rise in land prices." We cannot but agree. Yet its authors put forward the possible difficulty that, because land prices have risen faster than incomes, some land-holders may not be able to afford a more realistic rate of tax.

This is hardly admissible; for the increased taxes themselves, or even the knowledge that they were on the way, would start to bring the prices down from their present monopoly-induced level. Furthermore, other, less just, taxes could be reduced in compensation.

A word of warning. Japanese advocates of the increased land value tax will need to look sharp; for there is already a movement afoot to decrease it still further.