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New Patterns of Property Investment in “Post-Bubble” Tokyo: The Shift from Land to Real Estate as a Financial Asset

Natacha Aveline-Dubach

I. Introduction

During the second half of the 1980s, Tokyo experienced a so-called “land bubble” of dramatic magnitude. In the five central districts, the price of land multiplied sixfold between 1983 and 1990, by far exceeding prices in other Asian cities such as Taipei and Hong Kong, where they nonetheless also reached world highs. In the early 1990s, however, prices collapsed, with a drop of more than 70 percent in the business quarters of the Japanese capital. Since then, land markets have remained sluggish with the exception of a slight recovery between 2005 and 2007, which was then rapidly swept away by the effects of the Global Financial Crisis in 2007-2008 (GFC).

The booming phase of the “bubble” generated a great deal of literature on the spatial restructuring induced by skyrocketing land prices in the large urban areas, particularly in Tokyo (Noguchi, 1989; Machimura 1992, 2000; Hayakawa & Hirayama, 1991; Hasegawa, 1995, Aveline, 2003, 2004; Saito & Thornley, 2003). Comparatively, the post-bubble period received very little attention. Yet Tokyo is in the grip of changes that are just as radical as those that affected it during the 1980s. In the space of scarcely a decade its center has skyscrapers mushroom, whilst the former industrial zones east of the city have been converted on a wide scale into densely-packed residential districts. This new

restructuring phase occurred at a time when the economic climate was far less bright than it had been during the bubble years. The financial crisis of the 1990s marked a halt in Tokyo's rise to power as the region's major financial market, coinciding with a growing awareness that the Japanese population was rapidly ageing. The Japanese financial system took more than ten years to reabsorb its bad debts and was unable to avoid heavy restructuring. However, during this period, capital did not cease flowing into property development. This abundant source of real estate finance capital came from new, collective investment schemes (investment funds). American investment banks were first on the scene, launching private funds in Japan in 1997, to take advantage of the distressed property market. Since then, securitization techniques in the form of J-REITs (Japanese Real Estate Investment Trusts) have been introduced to offer large-scale exposure to "core"¹ property assets through listed shares. J-REITs specialize in the management of long-term building portfolios². They are the only vehicles that opens up broad access to long-term large real estate holdings through small stakes. As such, they embody the most mobile form of bridging finance

1 "Core" investment implies the holding of properties on a long-term basis (more than 10 years). Since it seeks stabilized properties involving low risk, the returns are not high. Core properties can also be held by private funds on a shorter term basis (from 5 to 10 years). However, the first funds launched by American investment banks were opportunistic funds, seeking high capital value in a very short period of time (inferior to 4 years). REIT shares are accessible to individual investors through the stockmarkets, while private funds are restricted to institutional investors or wealthy individuals.

2 A REIT is an investment vehicle that invests in various sub-sectors of the real estate markets (office, housing, retail, logistics . . .). Listed on the stock exchange, it distributes most of its net income to investors. In Japan, the J-REIT funds raise money through an initial public offering together with commitments from their sponsors, key investors and bank loans. The amount raised is used to purchase properties in order to increase the fund's building portfolio. When properties are sold, the proceeds of the sale can either be reinvested or, if the manager believes it appropriate, distributed to investors. However, J-REITs acquire properties for long-term income yield, and not for capital appreciation on resale, and therefore income from sales is limited to 10 percent of their revenues.

capital to real estate. Over the period 2001-2011, J-REITs contributed to approximately one-third of the total exposure on Japanese property markets by investment funds (Figure 9-1), attracting primarily domestic capital flows—from regional banks and household savings—but also irregular waves of foreign capital. Yet the impact of REIT investment has gone far beyond the provision of alternative funds for real estate. The focus by J-REIT asset managers on risks and returns in a perspective of long-term investment has marked a total break with previous local practices that were exclusively directed at short-term capital gains on land. As a result, not only did Japanese property operators have to comply with REIT regulations and techniques, they also had to change their understanding of the very notion of “real estate.”

This chapter focuses on the change in the status of land in Tokyo’s real estate economy under the influence of real estate securitization. The main argument is that the development of REITs, against a background of demographic shrinkage and sluggish land prices, has put an end to the use of land as a “quasi-financial” asset that characterized the golden age of the developmental state. With the (re)embedding of land in the economy of urban development, investment strategies in the Japanese property industry are shifting from an exclusive focus on land to a more conventional conception of real estate.

Since their launch in Japan in the early 2000s, REITs have spread across Asia, reaching seven countries. However, large REIT markets are only seen in three cities that have a “global control capacity,” i.e., Tokyo, Singapore, and Hong Kong. The development of J-REITs thus brings into focus the relevance of Sassen’s global city hypothesis (Sassen, 1991, 2005). REIT investment operates through a transnational system that interconnects the three global cities’ property markets as targets for the allocation of capital to Asia by global institutional investors. Yet no matter how globalized financial property investment is, the provision of the underlying physical assets (i.e., the portfolios of buildings in the case of REITs) still depends on the way local conditions shape the built environment (Wood, 2004; Rutland, 2010). It is widely recognized

that real estate is a fairly autonomous sector of the economy in which property development takes place as a full-fledged process that involves a wide range of agents (Faegin, 1987; Haila, 1991; Beauregard, 1994; Charney, 2001). The production and use of the building environment is framed by the local institutional context, defined by Keogh and D'Arcy as "a network of rules, conventions and relationships which collectively represent the system through which property is used and traded" (Keogh & D'Arcy, 1999: 2046). Individual strategies carried out by the various agents involved in building production also contribute to challenging and transforming resources, rules and ideas in the real estate industry (Healey & Barrett, 1989).

Land stands as a primary resource in the process of urban development. Therefore, the nature and structure of land ownership as well as the related rules (both formal and informal) that govern land-use rights are of critical importance in shaping the supply of property (Needham & Verhage, 1998; Needham & Lowe, 2006; Aveline, 1995, 2004; Lin, this book). Likewise, the structure of capital flowing towards real estate, i.e., the various channels through which financial resources circulate, strongly influences the making of the building environment. Research on property investment through financial channels has shed light on very selective strategies of asset acquisition, both in functional and spatial terms. Asset managers show a preference for office and retail, to the detriment of less profitable sectors such as housing (Jones, 2007). The spatial distribution of assets is equally narrow, characterized by a concentration on core locations in prime cities. Empirical evidence of these hyper-centralized patterns has been presented in various urban contexts. Henneberry and Roberts (2008) argue that the geographical distribution of office property investment in the UK is hampered by the primacy attributed to portfolio benchmarking. Other authors explain the poor spatial diversification by a strong aversion to risk and building "illiquidity" that prompts asset managers to avoid non-core locations (Theurillat *et al.*, 2010; Attuyer *et al.*, 2012; Aveline *et al.*, 2012).

This chapter draws on this previous research to give an account of the functional and spatial change in property investment introduced by securitized real estate in Tokyo. Yet the above change must be examined through the prism of land and capital supply with a long-term perspective. In the first section, I describe the land bubble of the 1980s as the natural outcome of a long tradition of using land as a “quasi-financial asset” under the guidance of the developmental state. Particular attention is paid to the complex structure of land ownership and its critical role in the formation of the speculative mechanism. The second section examines the dynamic of change that opened up after the bursting of the bubble in the early 1990s. I address the change in the structure of capital for property markets, paying special attention to the residential sector. These results are based on twenty in-depth interviews with various agents of the securitized real estate markets, conducted in 2009 and 2010 (J-REIT asset managers, real estate valuers, officials from the National Land Agency). Other sources include data from ARES³, J-REIT websites and unpublished documents released by the real estate industry.

II. The Land Bubble of the 1980s, an Outcome of the Developmental State’s Policy

The Japanese “land bubble” was one of the numbers of speculative mechanisms that followed the deregulation of financial markets initiated in the early 1980s in the United States, then in Europe and Japan, and finally in Southeast Asia (Renaud, 1997; Mera & Renaud, 2001). In the case of Japan, deregulation came as a shock since the Japanese financial system had been highly compartmentalized and controlled by the developmental state (Fujita, 2011). But the unprecedented magnitude of the Japanese land cycle could not be merely explained by a growing flow of banking credit towards real estate. The literature on the “bubble” has

3 The Association for Real Estate Securitization, a Japanese think-tank promoting the securitization of real estate and providing information on J-REITs.

highlighted the complex interaction of three key factors in the formation of the speculative mechanism.

The Japanese economy first underwent structural changes as a result of the expansion of the financial industry and the internationalization of the productive systems. Tokyo became a command center for the increasingly far-flung operations of Japanese transnational corporations and a financial and commercial hub, attracting a major share of office property investment (Douglass, 1988, 1993; Machimura, 1992). To adapt Tokyo's urban space to this change, local and central authorities then implemented a substantial relaxation of the urban planning and construction rules (Hayakawa & Hirayama, 1991). Neoliberal policies went so far as to overestimate the demand for office space and put large-scale public landholdings⁴ up for sale through auction, thus encouraging expectations of further rises in the price of land (Machimura, 1992, 1998; Saito & Thornley, 2003). Japanese firms were additionally incited to invest in land by lenient tax and accounting rules. Low taxation of land holdings and deductible profits against land purchases encouraged firms to buy and keep land idle, often with no accompanying property development project (Shigemi, 1991; Noguchi, 1989). They could draw "hidden assets" (*fukumi eki*) from a growing discrepancy between the book value (set at the original price) and the actual value of their landholdings, whilst enjoying increased lending capacity through the appraisal of collateral at actual land values (Dehesh & Pugh, 2000; Oizumi, 1994).

These tax and accounting incentives for landholding were, in fact, part of a broader policy conducted by the developmental state to turn urban development over to the private sector and boost the balance sheets of both conglomerates and SMEs. As a result, land has been disembedded from the urban structure and placed at the heart of the Japanese economic model as a "quasi financial asset." Taking into account

4 At the time, wide expanses of land were very rare in Tokyo and therefore highly sought-after by developers. The question of the fragmentation of plots of land will be dealt with more fully in the next section.

this characteristic allows us to understand the proportions attained by the expansion of the bubble at the end of the 1980s.

1. The Emergence of Land as a Quasi-Financial Asset

The particular status of land in the Japanese economy dates back to the foundations of the developmental state at the end of the 19th century (Johnson, 1982; Hill & Kim, 2000). The state attempted to prevent foreign capital from seizing vast sectors of the economy by channeling domestic resources into industrial development. This left Japan with limited resources for achieving its modernization program. Urban development was thus not considered a priority and the government contented itself with providing the bare minimum in urban infrastructure such as a water supply, arterial roads, highways, ports and airports.

The other major aspects of urban development were left to the initiative of the private sector. Amongst private operators, railway groups played the most critical role in shaping Tokyo’s residential suburbs and major railway stations. Not only did these groups provide a variety of transport services (taxi, bus and coach transport in addition to trains), they also supplied a wide range of urban services alongside and beyond their railway networks: residential development, electricity supply in residential zones,⁵ hotel and leisure businesses, and retail services on various scales (Aveline, 2003). In terms of operating revenues, the private railway groups are nevertheless dwarfed by the *keiretsu*-affiliated real estate companies (Mitsui Fudosan, Mitsubishi Jisho, Sumitomo Fudosan), which hold large office and retail properties in prime locations nationwide and account for a significant share of housing production.

Handing responsibility for part of urban services over to private railway companies and property developers meant allowing in exchange a certain flexibility in planning and building regulations. So although Japan has a long tradition of urban planning with a land-use zoning

5 Railway companies originally produced electricity for their transportation activity. The surplus electricity was then sold to households living in the companies’ residential areas. They stopped producing electricity in 1941.

system and a building code dating back to 1919, numerous loopholes in the regulations have allowed continuous urban sprawl on the urban fringe and haphazard densification in built-up areas.

This high flexibility in construction regulations encouraged property investors to constantly expect further deregulation, thus exerting a strong upward pressure on land values. The state's lack of involvement in housing policy only exacerbated the situation. Housing policies constantly promoted home-ownership for middle-class households by relying as much as possible on market forces and keeping social housing provision at a low level (Hirayama, 2007). Even the skyrocketing of land prices in the late 1980s did not alter the government's faith in the market. It responded by further relaxing planning and construction regulations in line with a strict supply-led land policy. As prices rose even higher, middle-class households had to purchase their homes in increasingly remote areas and to extend their loans to fifty years or more. As long as they could afford home-ownership they viewed the burden of heavy mortgage repayments as necessary if they were to accumulate capital for their old age.

Social consensus over "ever-rising land values" was also achieved through the increased protection of individual land ownership. Although a compulsory purchase procedure was introduced in Japan in 1919, it has been difficult for the public authorities to place public welfare above private land rights. It has been equally difficult to impose the designation of land-use zones in which land rights would be definitively restricted to use for public benefit, such as in zones dedicated to protecting the environment or historical heritage. The reason is that severe restrictions that arbitrarily strike certain land parcels would be regarded as an infringement of the principle of equality between landowners.

This liberal environment facilitated the use of land as a quasi-financial asset. The total disdain for the buildings erected on the land also contributed to this situation. Buildings are viewed as highly perishable goods with a maximum life expectancy of thirty to forty years. No sooner has a building been delivered than its value begins to decrease.

This perception may result from Japan’s highly unstable environmental conditions (earthquakes, tsunami, landslides etc.), which constantly threaten to destroy the building stock. However, cyclicality and renewal are also firmly rooted in Japanese customs, aesthetic patterns and social life (Ronald & Hirayama, 2006). In multi-storey residential buildings, each unit holds a ratio of the shared land value. This reflects the view that the land it is built on is the only valuable component of the property. Constructed objects therefore may be seen as bundles of technologies, performances and services—all subject to rapid obsolescence—rather than as tradable goods. As anti-seismic and IT technologies improve, taller buildings can be rebuilt every few decades, so making FAR (floor-area-ratio) regulations flexible is of primary importance (Aveline-Dubach, 2008).

This rapid turnover in construction makes land all the more valuable as an asset owing to the constant increase in its building capacity. Land therefore came to play a vital role in Japan’s economic growth model. Widely used as collateral for banking credit, land holdings became a major substitute for banking risk appraisal. Large amounts of capital were allocated to SMEs using what Wood calls the “land standard” (Wood, 1994), whilst big companies benefited from the growing hidden assets on their landholdings. Land was also a core component of the clientelist system of the Liberal Democratic Party (LDP), which ruled the country for more than five decades (Kerr, 2002). By implementing land reform in 1946, the LDP achieved political stability in rural areas and gained strong support from farmers. It also won a great deal of political support by relinquishing public plots of land situated in prestigious locations at low prices (Calder, 1986).

Japan is not the only country where land stands at the core of the economic system. As pointed out by Haila (2000), Hong Kong and Singapore have also shaped their growth models on land rent. In both of these inward investment-led economies, the state took control of land—entirely in the case of Hong Kong, partially in Singapore—and implemented a differentiated policy in the various segments of the

markets. In the housing sector, the cost of land was kept at a low level in order to maintain the low-wage workforce necessary for attracting foreign industrial investment; whereas in the private sector land was supplied at high cost in order to finance public infrastructure and facilities (Schiffer, 1985). In Japan, there was no need to maintain low wages as the economy did not rely on foreign investment; however, keeping land values rising was essential for sustaining collateral values, attracting private investors to urban development and gaining political support from farmers and home-owners. This explains the astonishingly slow reaction of the public authorities when land prices ballooned in the late 1980s, the government having waited four years before implementing countermeasures.

2. The Role of Land Ownership Restructuring in the Formation of the Speculation Mechanism

Although land had become a quasi-financial asset, it nonetheless remained the primary raw material of urban development. The “land bubble” of the 1980s was the product of this contradiction. To meet the need of large-scale sites for building to international standards in Tokyo’s core areas, massive restructuring of land-ownership was needed. However, the regrouping of land parcels involved a complex set of legal and regulatory aspects. Back in the early 1980s, ownership was so fragmented that it seemed a challenge to turn Tokyo into a truly “global city.” Low and mid-rise constructions dominated, with large amounts of wooden-frame housing units and “pencil-buildings.” The average height of buildings in the twenty-three special wards did not exceed 3.4 stories, including the ground floor (Noguchi, 1994). The size of land plots owned by individuals in the special wards was on average 217 square meters and almost half of the parcels were smaller than 100 square meters (TMG, 2000: 51). In addition, property rights were complex, notably in the central wards, as one parcel frequently held different types of rights: rights on the landed property (*sokochiken*), land-lease rights (*shakuchiken*) and building tenant rights (*shakkaken*).

Plot fragmentation and multiple ownership meant that creating plots large enough for major building construction required the time-consuming intervention of specialized operators known as *jiage-ya* who were experienced in negotiating techniques with property right holders (Aveline, 1995).

Low building density was not only caused by a fragmented land structure; it also resulted from the method used to calculate the applicable FAR (floor-area ratio). FAR regulations were set for each zone in land-use plans, but the applicable FAR had to be recalculated for each parcel in accordance with the width of the adjacent road. For example, a parcel located next to a four-meter-wide road in a non-residential zone would be granted a volumetric ratio of no more than 240 percent (a 240-square-meter floor area could be built on a 100-square meter parcel), even if a FAR of 800 percent had been legally established in the zone. This arrangement was designed to restrict high-rise buildings to streets able to handle greater volumes of traffic (Sorensen, *et al.* 2010). In 1987, the method for calculating the applicable FAR was deregulated in non-residential areas in an attempt to speed up urban restructuring by increasing building density. Prior to the revision, the applicable FAR of a parcel facing a four-meter-wide road could be increased if it were combined, in the form of a single construction site, with a contiguous lot facing a road wider than twelve meters. In this case the FAR jumped from 240 to 800 percent. Despite being applied very discreetly, this revision dramatically encouraged the grouping together of parcels and sent a positive signal to *jiage-ya*. These operators actively purchased small contiguous lots occupied by individual houses with low applicable FAR and combined them with parcels facing wider roads. The resulting construction sites were sold to developers at a value reflecting the highest applicable FAR. Given the scarcity of large parcels and the numerous narrow roads in Tokyo in the early 1980s, one can easily imagine the tremendous profits generated by this process of land grouping.

In the central wards, where the legally permitted FAR in the business zones attained 1,000 percent, actual density did not exceed 400 percent.⁶ *Jiage-ya* concentrated their activities on the five central wards in an attempt to draw the highest possible profits from the growing demand for large-scale office buildings. Initially, most of the profits generated by the gap in FAR came from residential blocks but small landowners soon became aware of the high potential of their properties and attempted to share the “land rent” with *jiage-ya*. The land spiral spread deep into the residential zones located at a distance from arterial roads, which had previously been protected from speculative transactions. *Jiage-ya* agreed to pay excessive prices for these tiny plots because they were expecting sizeable profits from the grouping of parcels. The unification of two distinct land markets within residential blocks—or to put it another way, the disappearance of the huge gap in FAR regulations within blocks—was a decisive factor causing a disruption of scale in the process of land value escalation (Aveline, 1995).

The growing integration of fragmented land submarkets by the *jiage-ya* had the effect of creating new land value benchmarks that were completely irrational. In this real estate economy driven by expected capital gains on land, the endogenous regulatory mechanism that usually drives down properties values when yields plunge, did not operate. Exogenous factors were equally defective since the State, at both central and local levels, was reluctant to intervene in the markets. Moreover, the banks were keen to deliver credit based on extravagant land collateral values to survive in a newly deregulated global financial market.

After four years of frenetic speculation by Japanese institutional investors (mostly firms and insurance companies) both in domestic and international property markets (US, Europe, and Australia), Tokyo’s land bubble suddenly collapsed. This disaster was attributed to the drastic increase of interest rates by the Bank of Japan (BoJ) in the fall 1989. True, the demonstration of BOJ’s willingness to break the speculation

6 Tokyo Metropolitan Government, *Tokyo no tochi 2000, op. cit.*, pp. 68-69.

mechanism reflected a major change in the central government’s policy—or to put it differently, indicated the launching of a pro-active policy towards what had become a “financial bubble.” But the property markets had been actually showing signs of breathlessness before the government decided to take action.

The banking sector was seriously affected by the fall in land values. In the grip of an accumulation of bad debts, the banks had to rapidly redress their accounts. Securitization was therefore introduced to unblock the property markets by increasing their liquidity (Ide, 1999). This tool was not limited to reabsorbing the financial crisis, however, but was the favored instrument in the remarkable urban restructuring launched in the late 1990s. This process took place in a political, economic and demographic context radically different from that which preceded it. In the next section, I examine how urban governance adapted to the new deal by funneling capital accumulation towards the central areas.

III. Financialisation of Property Markets and New Urban Paradigm

1. The Change in Urban Paradigm

In the early 1990s, the urban paradigm that had prevailed since the post-war period was abruptly reversed. It had been characterized by a chronic scarcity of land resulting from continuous urban growth, all of which generated a virtually uninterrupted rise in land values. All these parameters were overturned after the explosion of the “land bubble” (Table 9-1).

First of all, scarcity of land became an over-abundance of land. The crisis brought a halt to the re-grouping operations by the *jiage-ya*, who found themselves with collections of small plots they had purchased at totally unmarketable values. Similarly, Japanese companies that had benefited from “hidden assets” with the growth in prices, recorded

“hidden losses” on land acquired at high prices during the bubble.⁷ Forced to restructure, they had to dispose of their numerous unused parcels, which no longer offered any prospect of capital gains on land whilst carrying increasing charges resulting from tax and accounting reforms.

Secondly, anticipation of continued urban growth was challenged by the growing awareness of the seriousness of having an ageing population. In 1990, the fertility rate in Japan fell to 1.57 children born/woman, a level that was lower than that of the black year of 1966.⁸ This trend was then confirmed since the ratio continued to decrease (1.21 in 2011) and the Japanese population began to fall from 2005 onwards.⁹ Although Tokyo is one of the few Japanese prefectures to have a rise in population numbers, urban shrinkage has already begun within the confines of the suburbs and in Tama New Town (Doteuchi, 2003; Ducom, 2008; Yoshida, 2010). Under these conditions, the “land myth” (according to which land values can only increase) has been well and truly debunked, even though the swings of capital markets might cause sporadic upward movements in land values, as was the case during the period 2005-2007.¹⁰

Lastly, the crisis has ruined hopes of making Tokyo into a financial capital at regional level. While the Japanese economy was struggling with its accumulation of bad debts and the radical restructuring of its financial system, other Asian cities such as Hong Kong and Singapore were

7 Accounting regulations allowed the value of land to be recorded as the historic purchase value, so that any increase in the value of the land would generate hidden assets that were not written down in the accounting books. On the other hand, land bought during the period when land prices had attained unprecedented heights suffered a loss that was not recorded in the accounts.

8 This “year of the horse” was characterised by a massive postponement of births for fear of giving birth to a daughter who might kill her future husband.

9 In December 2004, the Japanese population had reached its height with 127.848 million inhabitants. According to official estimates, it is expected to fall to 64 million in 2100 at its highest estimate, and to 37.7 million at its lowest estimate (source: Ministry of Land and Transport).

10 The recovery of the land markets is the result of an intense flow of investments into private security funds by foreign financial establishments.

strengthening their position as financial hubs. Tokyo’s relative position in Asia is also challenged by the increasing importance of Shanghai and Seoul both on the world stage and at regional level.

Table 9-1 Summary of changes from the 1980s to the 2000s

Pre-bubble period	Post-bubble period
Overall context of urban development	
High demographic growth	Low demographic growth, ageing population
Continuous urban growth, urban sprawl	Urban shrinkage in peripheral areas
Scarcity of land	Large supply of construction potential through massive deregulation of construction rules
Urban governance focusing on regional and intra-urban balanced development	Urban governance focusing on Tokyo’s regional positioning
Residential model: single-family house in the suburbs	Residential model: condominium near a railway station
Behavior of the players in the property markets	
Ever-rising land values (except in 1973) → land myth	Decreasing land values, sporadic rise → end of the land myth
Land ownership-oriented business operations	Real estate business operations focusing on “utilizing” properties
Comparison method as primary appraisal method	Discounted cash-flow method as primary appraisal method
Price formation based on expectation of future capital gains	Price formation based on utility value (yield-driven)
Emphasis put on land markets	Emphasis put on real estate markets
Opacity in property markets	Greater transparency (though limited to REIT funds)
Built environment	
Continuous building process spreading from the center to the periphery	Fragmented evolution with surge in “hot spots” in the center and decrease in peripheral areas
Buildings reconstructed every 30-40 years in order to keep pace with new anti-seismic and IT technologies	Skyscrapers constructed without any limitation of duration Renovation becoming a growing alternative to systematic reconstruction.
Low to mid-range building density	High building density in many districts
Single residential model and housing status (individual house, owner-occupation)	Diversified residential model and residential status (emergence of rental condominiums held by institutional investors)

Source: The author.

This accumulation of problems has led to a change of direction in urban governance. The latter had driven a vast movement of land consolidation during the 1980s to facilitate the building of office blocks to international standards. This policy had reduced the fragmentation of the parcels but at the same time had contributed to the spectacular rise in land values. The first reflex after the arrival of the financial crisis was therefore to tighten up the rules governing FAR under the pressure of public opinion, which was very critical towards government laxity. But the rapid erosion of land values and the weakening of Tokyo's regional positioning quickly led to the return in force of a neoliberal policy.

In 2001, the Koizumi administration listed its "Urban Renewal Policy" as one of its seven key priorities and set up a headquarters for urban revitalization. The explicit purpose of this policy was to restore the prestige of the Japanese economy by reshaping Tokyo into a "multifunctional concentrated-type city," replacing the former multipolar city. The residential hollowing out seen in the 1980s was to give way to the construction of high-rise housing blocks served by a full complement of retail facilities, with employment zones concentrated in nearby groups of skyscrapers (Yahagi, 2002).

To facilitate the increase in building density, a new wave of deregulation in planning and building rules was launched. In June 2002, the Urban Renaissance Special Measure Law designated "priority districts for urgent redevelopment" where building density could be significantly increased through radically relaxed regulations. A total of sixty-four districts covering approximately 6,567 hectares were designated nationwide. Tokyo received the largest share with seven districts totaling 2,514 hectares (Hirayama, 2010). The geographic distribution of these districts displays a concentration along the waterfront in the eastern part of the city and to a lesser extent in the sub-cores of Shinjuku and Shibuya. It also resuscitates an old project by Mitsubishi Estate seeking to transform the Marunouchi area into a Manhattan zone, a project that had been rejected repeatedly by central and local governments (Saito & Thorney, 2003). It is no accident that these priority districts included

some of the country’s most distressed land markets, those which had experienced the sharpest boom-bust fluctuations with a drop of seventy to eighty percent in their previous values.

The massive upsurge in building capacity in these districts, as well as in other “hot spots” such as Roppongi Hills and Tokyo Midtown Project,¹¹ has helped curb the decline in collateral land values and subsequently eased the burden on the financial system. Here, too, the Urban Renewal Policy was primarily dictated by macro-economic concerns. It was designed to meet the interests of the property development industry and emphasized the need to regain Tokyo’s competitiveness in order to justify urgent measures bypassing democratic debate. This seems to suggest that the urban policy of the developmental state has not been undermined by the growing grip of finance on property markets. Sorensen argues that the renewal policy has actually shifted the balance of power back again towards the central state to the detriment of local initiatives to protect local low-rise neighborhoods. The massive construction of high-rise buildings has radically transformed Tokyo’s urban landscape. Amongst the existing 350 skyscrapers measuring over 100 meters tall, fifty-four percent were constructed after 2000, compared to fourteen percent before 1985 and thirty-five percent during the “bubble years,” from 1985 and 1995.¹²

2. The Expansion of Investment Funds and New Investment Geographies in Tokyo

Capital supplied by investment funds has played a critical role in urban restructuring. Two types of investment collective schemes exist: private funds (PF) and REITs. The former are short-term funds (usually held over a period of 5-6 years) focusing on property development, while the latter seek returns from long-term investment. With 1,841

11 According to Hirayama, the Roppongi project has been granted a rise in FAR from 327 to 719 percent and the Tokyo Midtown Project from 320 to 670 percent (Hirayama, 2012: 310).

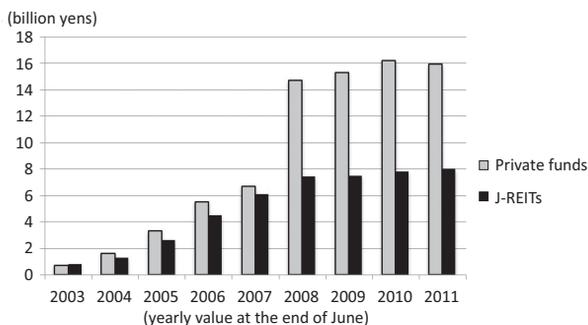
12 Computed in June 2011 by the author using the Emporis database (<http://www.emporis.com/en/wm/ci/bu/sk/li/?id=100297&bt=2&ht=2&sro=0>).

entities in 2011,¹³ PF are by far the most common. Most of them only possess one property but this is often a major property complex of large value. More than 65 percent of the value of their assets is concentrated in Tokyo, half in office property and 12 percent in residential property (this nonetheless represents half the number of buildings). In June 2011, the accumulated value of the portfolios held by PF totaled 15.9 trillion yen (US\$206.6 billion, Figure 9-1). The J-REIT funds,¹⁴ of which there are 35 including 32 based in Tokyo, have a far lesser portfolio value (8 trillion yen in 2011) but unlike PF, each trust unit has a large portfolio of buildings. The largest J-REITs are controlled by the big Japanese financial and industrial groups (Mitsubishi Mitsui, Nomura, and Daiwa) and tend to specialize in one category of assets. This allows them to streamline the management of the portfolio, since the properties do not have the same lifespan depending on their function. For example, residential buildings, which are much smaller than office buildings and condemned to fall into obsolescence more quickly, are renewed more frequently (on average every 20-40 years). The seven REITs specializing in office properties each possess between 50 and 60 assets¹⁵, the accumulated value of which represents a third of the total value of the properties held by the 35 J-REITs. The residential portfolios of the big groups are much bigger in terms of the number of properties (between 100 and 200 assets per fund) but their accumulated value only represents 18 percent of those held by all the J-REITs put together.

13 Ministry of Finance, *Fando monitoringu chôsa no shûkei keka ni tsuite* (Monitoring Survey on the Capitalization of Funds), September 2010. This figure does not include foreign funds licensed in Hong Kong or Singapore, but these account for a very small share of the total.

14 J-REIT funds buy buildings and rent out real estate. In exchange, their investors—mainly small investors whose contributions are collected by mutual funds—benefit from tax advantages. J-REITs are not authorized to make property transactions, but can sell the buildings when they consider them obsolete, on condition that the income from the sale does not exceed 10 percent of their revenue. All their functions, from rental management to maintenance are subcontracted.

15 In cases where the value of the property is very high an asset can be a whole building or part of a building (in particular in the office sector).



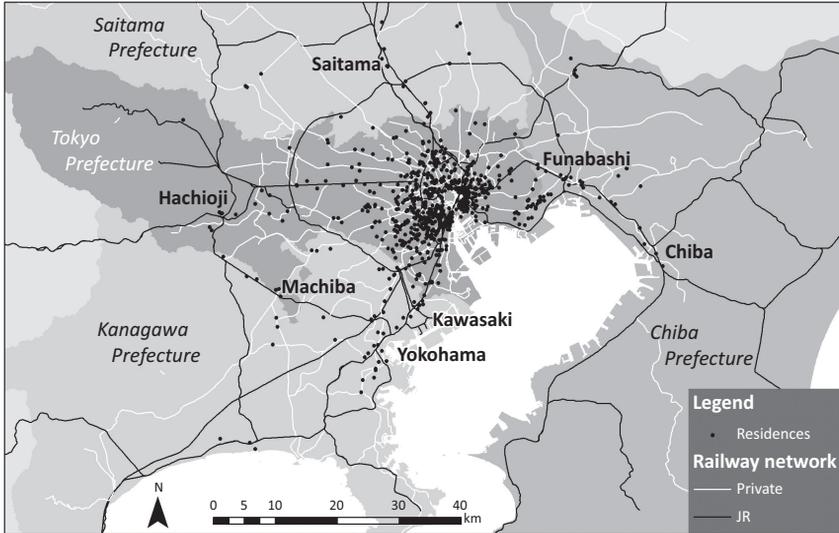
Source: Compiled by the author using the data of the STB Research Institute.

Figure 9-1 Aggregated building value of investment funds in Japan

In all, the J-REITs manage 1,857 assets spread over the entire country. The main characteristic of these portfolios is their concentration in the Tokyo metropolitan area, where almost 70 percent of the properties (1,281) are situated, representing 76 percent of the total value. Moreover, these assets are located in Tokyo’s central zones. This is the result of the constraints of the financial logic that governs these funds. Asset managers purchase properties where they perceive the least investment risks to be. In the office sector, all zones outside Tokyo’s three central wards (Chiyoda, Minato, and Chuo) are considered to carry risks. Even the lively Shibuya and Shinjuku districts are not included in the priority list. Out of the 394 properties held by J-REIT funds, almost half are in the three central districts, in particular along the Hibiya and Ginza metro lines.¹⁶ The distribution of residential funds is more spread out, as one might expect, but almost a quarter of the buildings (23 percent) are situated in the 3 central districts (Figures 9-2 and 9-3). The concentration of investment in the CBD has increased still further since the Global Financial Crisis. To deal with what they perceive as an accentuation of the risk of investment, fund managers have increased Tokyo’s share in the geographical diversification of the portfolios, from 70 to 80 percent of the value of the funds, even to 90 percent in certain cases.¹⁷

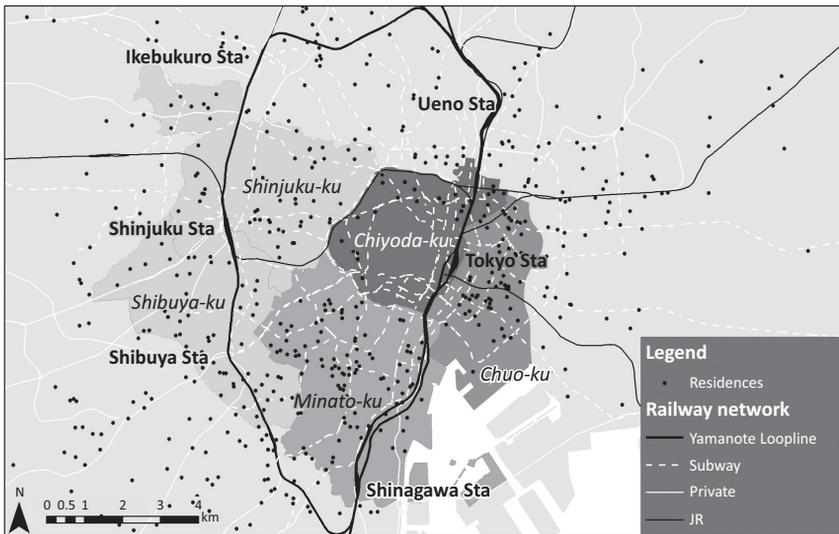
16 Source: Association of Real Estate Investment Trusts. The three central districts are Chiyoda, Minato and Chuo.

17 Geographical diversification is essential in the management of property portfolios in a country subject to natural disasters.



Source : Compiled by the author using ARES data.

Figure 9-2 Spatial distribution of J-REIT residential portfolios in the Tokyo region (as of September 2010)



Source: Compiled by the author using ARES data.

Figure 9-3 Spatial distribution of J-REIT residential portfolios in Tokyo's center (as of September 2010)

3. Diversification of the Residential Supply in the Central Zones

If the concentration of offices in the center of Tokyo is part of the extension of the previous process, it is quite a different matter in the case of housing. Because the return of residential construction in the central zones is an unprecedented phenomenon that no one would have dared predict twenty years ago. It has happened as a result of the amount of land available following the explosion of the bubble and by the return to a policy of massive liberalization of the regulations governing town planning and building.

The backward shift of housing construction from the suburbs to the centre has also been stimulated by a strong disaffection for the residential model of the single-family house. The expansion of the Tokyo urban zone to a radius of 60 kilometers from the center during the bubble years to peripheral areas without adequate public transport links, made the suburban house synonymous with endless commuting. Multistory housing (*manshon*) gradually became a popular alternative to individual housing owing to its lower cost and better accessibility to main railway stations. Merely a first step in the housing ladder at the beginning of the 1980s, a decade later it had taken its place as an ultimate destination in the accession to property (Ronald & Hirayama, 2006). Medium-sized *manshon* tend to be replaced by high-rise housing due to the relaxation of the urban and construction rules. This trend may also be related to the dissemination of the Singaporean model of high-rise condominiums across Asia. Over and above their residential function, these high buildings provide a multitude of services (sports facilities, caretaking, common areas, security systems) that correspond very well to the new aspirations of Japanese households in matters of urban amenities and security. The investment funds have taken advantage of the new popularity of group housing, placing luxury condominiums in their property complexes. Since a strategy such as this was beyond the means of the J-REITs¹⁸, they turned their attention to the middle of the market,

18 The J-REIT funds prefer to limit the amount of their investment for each building to avoid a situation where an accident to a building affects the performances of the rest of the portfolio.

mainly owning medium-sized residential buildings that lack community services but which often have car parking space.

For long-term investment funds such as REITs, the holding of residential portfolios allows to compensate for the vagaries of the business cycles in the office and commercial sectors. Residential investment is also currently stimulated by a steady demand for housing in Tokyo's central districts. The big companies are seeking to move their managers closer to their workplace because of computer security problems which prevent them working at home. They are disposing of their company housing buildings (*shataku*), which are expensive to maintain, and giving housing subsidies to their employees instead. These take the form of housing allowances, which support the institutional housing rental market.

To meet this demand, J-REIT funds try to locate their residential buildings within a commuting time of approximately thirty minutes by subway or railway from Tokyo's CBD, where the largest share of service employment is concentrated. Most housing units in the rental condominiums held by J-REITs are designed for young singles or couples. In the eastern area, where the cheapest rents are available, young "white collar" workers can find affordable accommodation near Nishi Funabashi or Urayasu in the range of 60,000-70,000 yen per month (US\$780-910) for a 28-30 square-meter apartment.

J-REIT residential funds play on the synergy of their portfolios by developing product lines similar to those of hotel chains, guaranteeing quality standards. In doing so, they tend to standardize urban production but contribute to the supply of quality mid-range housing which lends prestige to the rental sector. By raising the status of the tenant, J-REITs contribute to greater residential mobility, a factor that has become crucial at a time when employment in Japan is rapidly becoming unstable.

4. The Emergence of "Real Estate" as Against "Pure" Land

One of the less visible effects of the bursting of the bubble has been the emergence of the notion of "real estate," as a combination of land and the type of building mentioned above as against the

traditional “pure” land asset. Securitization techniques in real estate have greatly contributed to the dissemination of this notion. In so doing, securitization gave real estate a new status at a time when land was suddenly and permanently devalued.

The change in the method of property value appraisal reflects well this new trend. Previously, property assets were appraised according to traditional comparison methods, which consisted of deducing the value of a property by comparing it to other properties in the same district with similar characteristics. This method of calculation ignored the value of the buildings and focused on the characteristics of the land parcels and their potential in terms of capital gain. Such an approach was strongly criticized by Japanese scholars and urban-planners for aggravating the boom-bust cycle (Aveline-Dubach, 2008). With securitization came the spread of DCF (discounted cash-flow method), which has become compulsory for certified real estate experts. According to this method, the value of a property derives from its rental cash flows, thus fully taking into account the intrinsic characteristics of the buildings, with a view to long-term profitability (yields) rather than short-term profit (capital gain).

To preserve good return levels, high technology and service standards must be maintained. This is particularly restrictive for J-REIT funds that run a permanent risk of defection by their investors if their results are not considered good enough. So far from reducing the turnover in construction, securitization tends, in principle, to encourage it in order to maintain the attractiveness of the portfolios. However, this recycling of constructions now takes place without any prospect of urban and demographic growth, which reduces expectations with regard to added land values. Land has not only lost its growth potential with the end of the “land myth” and the beginning of urban shrinkage, it no longer offers advantages as a target for investment now that the tax and accounting privileges it offered firms have been suppressed. Moreover, the practice of renovating buildings is gaining ground in Japanese cities in line with the requirements of “urban sustainability.” It is therefore to

be expected that the turnover in construction will gradually slow down as demographic pressures ease.

The diversification of the property markets is another sign of the emerging interest in building performances. The positioning of REITs on the residential rental market, which hitherto was not of great interest to institutional investors given their focus on short term capital gain, testifies that long-term investment strategies are gaining ground. The growing significance of real estate (with the construction component) versus land can be measured by the increasing use of the Japanese term “*fudôsan*.” Taken from the French word “immobilier” (*fusôsan* literally means “non-mobile asset”) and long confined to the legal and tax fields, this term has been used more and more widely by property market players over the last few years.

With real estate assets now accessible in the form of (public or private) equity on the one hand, and on the other, “pure” land assets that have lost their attraction as an exclusive object of investment, everything leads us to believe that real estate is in the process of taking the place of land as a financial asset. This trend can only increase with the lengthening of the lifespan of the buildings.

This situation is favorable for urban development, as it tends to stabilize land values in the long run. The development of long-term real estate rental investment in the form of the REIT portfolios can also be perceived favorably, particularly in the housing sector where private institutional investment had been notably lacking.

IV. Conclusion

Over the last three decades, the process of urban production has undergone radical changes in Tokyo. The 1980s bubble was the grandiose product of a situation where land had become a “quasi-financial” asset. Everything then conspired to extract land from the urban structure and make it a prime object of investment: the considerable tax and accounting advantages linked to the acquisition of land for firms, the

low carrying costs, the flexibility of planning regulations, the rapid turnover in buildings. The possession of land assets was directed towards the enhancement of capital value, promised by continual urban growth and justified by the virtually uninterrupted rise in land values over the previous fifty years. The speculation mechanism, fed by the flow of bank credits, was exacerbated by the highly fragmented structure of land ownership. By restructuring this complex land ownership, real estate brokers sent prices skyrocketing to completely irrational heights. In a system lacking in regulatory mechanisms, these values became the references on which the whole financial system was based.

However, the bursting of the bubble, together with a radically new context of demographic transition, dealt the final death blow to the status of land as a “quasi financial” asset. With the expansion of real estate securitized funds, new practices and representations emerged in the real estate industry. In the residential sector, owing to a yield-driven strategy that came to replace expectations of capital gains, institutional investors have developed a quality housing rental market, and condominiums in central areas have replaced the suburban house as a residential model. All these changes have given physical properties a new status that the extension of their lifespan is expected to consolidate. Real estate is therefore on its way to taking the place of “pure” land as a financial asset, a development that may bring Japan into line with other industrialized countries.

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