

Heterogeneous Impact of Real estate Prices on Firm Investment¹

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Abstract

We focus on real estate and other fixed tangible assets to study how real estate prices affect their investment behavior in a heterogeneous manner. Theoretically, expectations of declining real estate prices not only reduce overall fixed tangible investment through a collateral channel but also reduce real estate investment through inter-temporal substitution of demand. By employing a unique dataset on firms' land transactions and on their overall investment during the period 1997 through 2006 in Japan, we examine these predictions to find the following. First, the entire fixed tangible asset investment is positively associated with the growth rate of land prices, which evidences for the collateral channel. In contrast, land investment has no statistically significant relationships with the land price growth. Second, a decomposition of land investment into land purchases and sales shows that land sales actually decrease when there is a smaller growth rate of prices. Third, large firms and firms that acquired land during and shortly after the bubble period tend to reduce the amount of land sales. This is consistent with Geltner (2014) that potential sellers of land set their reservation prices at their purchase prices and become reluctant to sell land in the face of a persistent drop in its price.

Keywords: Real estate; Land; Fixed tangible investment; Collateral channel

JEL Classification: G21, G32

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