How demographics affected the fortunes of Japan's private railways

Some of the recent Asian Development Bank Institute podcasts have focused on how governments can attract private investors to public infrastructure projects. Such projects typically offer relatively low returns. This is because governments are usually reluctant to charge the public too much for user fees such as highway tolls.

But governments can offer higher returns to private investors if they share future tax revenue from spillover activities created by new infrastructure. A new highway might bring in new businesses and jobs.

These activities may not have even been anticipated when the highway was being planned. But new business and jobs bring in more revenue for governments—increased taxes on such things as income, property, and sales. And this future tax revenue can be shared with private companies to boost their returns, making their initial investment more attractive.

The idea of sharing future tax revenues with private investors is being promoted by the Asian Development Bank Institute—the ADBI—in Tokyo to help finance the region's huge demand for infrastructure. But Naoyuki Yoshino, the dean of the institute, warns that future revenues need to be sustained for such financing to succeed in the longer term.

Japanese private railway companies played a major role in expanding the country's transport sector in the 20th century. These companies were much more profitable than Japan National Railways, the public railway operator that was split up into seven private companies three decades ago after incurring massive public debt.

The private companies set up earlier saw that they could generate future revenues from land sales after they invested in railways. These privately run train lines created spillover commercial activities such as department stores and hotels. These were located on land adjacent to the train lines that the rail companies had already acquired. With new transport infrastructure in place, the companies were also able to sell off some of their land holdings as housing.

Dean Yoshino says this strategy was key their success.

> Japanese private railways were much more successful than Japan National Railways. They purchased the land before the railway was constructed and then they sold those properties after the railway was completed. So lots of housing was constructed along their lines. They had capital gains by selling those properties—land—and that's why they were very successful.

But as the Japanese economist points out, such capital gains did not last forever. At the same time, profits from commercial activities like department stores and hotels eventually fell victim to the aging of Japanese society.

The sales of those properties were only one shot. However, they are facing future problems, and many of those who purchased the land are close to retirement. All the villages along those railways have many, many old people, and they are no longer using those railways.

In other words, the strategy of the private railway companies was based on people working and spending money—not on pensioners relying on welfare.

> When they were young, they used the trains every day to commute to downtown Tokyo. So the railway lines were profitable and people went to shopping malls and purchased lots of goods and services. But now they've retired and they rely on pensions and social welfare. All of a sudden, they started to consume less. So the Japanese private railway was successful,

> **but faced with an aging population, its profit plan was not so good.**

Dean Yoshino says using the prospect of future tax revenues to attract private investors is still viable—provided that those revenues keep coming.

> **My idea is that along those railways, highways then private companies will come and shopping malls can be created. Then they contribute taxes to the region. As long as their sales keep on going every year the railway company can receive part of those tax revenues in addition to their user charges.**

That was Naoyuki Yoshino, dean of the Asian Development Bank Institute in Tokyo, talking about private railway investment and the graying of the population in Japan.

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