

The Speculation and Crowding Out Channel: Real Estate Shocks and Corporate Investment in China

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Real Estate Shocks, the Bank Lending Channel, and Corporate Investment

When real estate prices increase:

- Firms with more land holdings benefit from increased collateral values, receive more financing and invest more – *collateral channel* (Chaney, Sraer, and Thesmar, 2012)
- Banks adjust lending in response to increase in real estate prices.
 - May spillover positively, or may move capital away from non-mortgage lending (*crowding-out channel*). (Chakraborty, Goldstein, MacKinlay, 2016)

A New Twist: the Speculation Channel

- Paper shows that firms may take additional loans and buy real estate themselves, even when not related to core business.
 - In response, reduce the proportional amount of non-land investment and other productive uses of capital (e.g., patents)
 - Points to a misallocation ***within*** the firm, not just ***across*** firms, as with the crowding-out channel.
- Is a very important consideration, as the positive side effect of increased real estate prices (*collateral channel*) may just be firms directing money directly back into the real estate market and forgoing core business activity.

Comment 1: Understanding Any Biases

One pervasive issue: increasing real estate prices may be capturing changing local economic conditions more generally.

- Higher housing prices, better investment opportunities.
 - For collateral channel results (Table 2), should control for the level of real estate prices and other economic conditions in a location generally.
 - Already do this for speculation channel tables and doesn't really change the results.
 - Also reassured by the fact that the IV gives similar results.

For speculation and crowding-out channels, this bias would go against finding results for non-land investment.

Comment 1: Understanding Any Biases

An increase in real estate prices could also capture cost of production changes:

- Specifically, increase in land values captures increase in land cost as an input, but also correlated with increased wages and other costs.
- Firms in high price markets may cut non-land investment demand compared to firms in low price markets as a result.
- Fact that price change variable loads negatively for total amount of non-land investment (Table 3) but not for the proportion of non-land investment (Table 4) may point to this.

Would generate negative results for investment of non-landholding firms especially, as they have no offsetting collateral effects.

Comment 1: Additional Analysis

Add industrial land prices, local wages, and other costs as additional controls when looking at commercial land price increases.

Could rely on geographical separation:

- Look at subsample of non-landholding firms where lending bank branch is not in same area, or majority of branches not in same area.
- Look at non-landholding firms with multiple lenders. Are loan amounts different depending on price appreciations at different banks?

Comment 2: Do Banks Speculate?

Gan (2007) argues that Japanese banks had substantial real estate exposure through both loans and direct land holdings.

U.S. banks in general didn't have substantial direct land holdings during the U.S. housing boom.

What is the case in China?

- If banks themselves are buying up land, adds interesting dimension to the speculation channel.
- Would be worth looking at the financial firms that the paper currently excludes.

Comment 3: Do Firms Come Out Ahead?

Although not focus of paper, do landholding firms maximize value by speculation?

- Use increases in land value or observed land sales to give some estimate of increase in firm value.
- Would these gains offset TFP losses for these firms?
- Would further clarify the misallocation of capital across firms and within firms.

Other Questions

- What is the nature of the Chinese firm?
 - How often are industrial firms more like diversified conglomerates?
 - Implications for how much firms are moving away from core business.
- Would like more clarification on residential versus commercial real estate prices.
 - Are they essentially the same?
 - Would matter for the housing purchase restriction analysis.
- When and how do land purchases show up in net fixed assets from an accounting standpoint?
- The boom in real estate prices is driven by capital flowing into residential lending, commercial mortgage lending. Is one more dominant than the other?

Conclusion

- The speculation channel is clearly important to understand the allocation of capital.
- Raises two points:
 - The traditional collateral channel may not be as beneficial as we thought.
 - Papers should look more finely within capital expenditures and across different measures of firm activity.