

# TWO SIDES TO A STORY

## FOREIGN INVESTORS

It's an emotive subject that can get quite heated, but what's the truth about foreign investment and its impact on the Australian property industry? API dives headfirst into the debate. **ANGELA YOUNG**

**D**epending on what you're reading, or where, foreign investors are either ruining the property game for everyone or they're propping up the industry.

Media commentary on the subject has been particularly rife over the past 12 months, with certain elements of the press screaming that first homebuyers are being priced out of the market, while other sections of the media dismiss all criticism of the subject and extol only its virtues.

So, what's the truth? Is foreign investment in Australia all bad or all good or, like so many things, is it less black and white than that?

One thing that's generally not being contested by anyone is that investment from Asia, and China in particular, has increased fairly significantly over the past three years or so. But the subject of foreign investment covers all nationalities, which is where one of the flaws in this argument begins to raise its head.

### ■ DECEPTIVE APPEARANCES

Propell Valuers national research manager Linda Phillip points out that Asian buyers, and specifically Chinese, are often the focus of public disquiet due largely to their visibility at home auctions, particularly in cities such as Sydney.

"The reaction tends to be paranoid rather than factual," she says.

Open Wealth's Matthew Lewison backs this up.

"As soon as you see someone of Asian appearance at an auction you think, 'They're going to be giving everyone a run for their money,'" he says. "It's expectation now and you think their money's come from overseas. Particularly in Melbourne and Sydney where there's a very multicultural community, every generation there are going to be more people of Asian appearance living here. They might have come over last

generation and their children have married a Caucasian... I wonder if in 15 years' time when those Australians go to an auction, people are going to mistake them for an overseas bidder."

Juwa.com founder Simon Henry concurs.

"If you go back a couple of years," he says, "the majority of foreign investors in Australia were from the US, the UK and New Zealand, but you couldn't go to an auction and 'see' an American. I think genetics play a big part [in the perception]."

"We have an awful lot of Chinese who are Australian citizens buying property, so I think there's a bit of a backlash because people think everyone's coming from China whereas, in reality, Australia's home to an awful lot of Chinese Australian citizens."

So, disregarding any xenophobic hysteria that "the Chinese are stealing all our homes!" based purely on the appearance of bidders at auction, how do the numbers on foreign investors stack up?

According to a National Australia Bank survey, roughly one in six new or yet-to-be-built properties was purchased by a foreign investor in the third quarter of 2014.

Figures from CoreLogic RP Data put the market value of the whole property market in Australia at approximately

**"I think there's a bit of a backlash because people think everyone's coming from China."**

**MATTHEW LEWISON**



\$5.4 trillion, consisting of roughly 8.6 million homes. According to data from the Treasury, in the 2012-2013 year 11,700 foreign investment in residential real estate proposals were approved, worth \$15.81 billion. Data provided for the 2013-2014 year (which is only for the nine months to March 31, 2014), shows 16,000 approvals worth \$24.13 billion.

Interestingly, developments of 100 new dwellings or more require only a single Foreign Investment Review Board (FIRB) approval to sell up to 100 per cent of the properties involved to foreign buyers (and those individuals aren't required to obtain individual approval themselves). It's factors like this that lead to accusations the FIRB is ineffective and that there's 'no accurate or timely data' tracking foreign investment in residential real estate in Australia.

### ■ WHERE FROM AND WHERE TO?

If we examine foreign investment in property from its source we see that while the US was generally the top provider of investment between 2007 and 2012, China has since scooped the number one spot, with Canada, the US, Singapore and the UK following on, in that order.

Within our own shores, New South Wales, Victoria and Queensland attract the lion's share of foreign real estate investment, with NSW scooping more than 38 per cent of the total value (of FIRB approvals in 2013-2014) and Victoria taking 22 per cent.

Of the approvals in 2013-2014, more than three quarters were for brand new rather than established properties.

With plenty of figures under our belt, we're now ready to take a look at the positives and negatives, and see which is the more powerful argument when it comes to foreign investment in Australian residential real estate.



### THE CONS

Beyond the screaming headlines, what are the logical arguments for defining foreign investors as a negative for the Australian property industry?

Possibly the most significant factor is the impact they have on house prices. Although debate continues to rage on just how much influence they have, there's little doubt that sheer extra numbers help prices to rise, and that's without taking into account the issue of overseas buyers paying too high a price.

Assistant Governor of the Reserve Bank of Australia (RBA) Dr Christopher Kent sums it up well: "If you imagine an auction on a weekend where you throw in an extra buyer who's willing to pay a little bit more than everyone else there, if that buyer happens to be foreign, maybe as a temporary resident, and they're buying the single place that they're able to get approval for, it's hard to deny that it would push up the price."

CEO of NSW Starr Partners estate agents Douglas Driscoll says: "While investment from overseas buyers may help stimulate the economy, we need to be mindful that we already have an undersupply in housing and there's no shortage of locals wanting to buy."

"Many foreign investors are buying off-the-plan developments in bulk, often purchasing up to five properties at a time," he continues, saying that debate over the number of properties bought by this group could reach a climax in mid-2015.

### CLARIFICATIONS

#### What is... the FIRB?

The Foreign Investment Review Board is a non-statutory advisory body that was set up in 1976 with the aim of advising the Australian Treasurer and Federal Government on the country's foreign investment policy and the administration of that policy. The board currently comprises Brian Wilson, Anna Budulis, Michael D'Ascenzo, Patrick Seckler and Rob Donnelly.

Its role is to examine proposed investments in Australia subject to the policy, the Foreign Acquisitions and Takeovers Act 1975 and supporting legislation and make recommendations to the Treasurer; foster an awareness and understanding, both in Australia and abroad, of the policy and the Act; provide guidance to foreign investors and their representatives; check for compliance and advise the Treasurer on the policy and related matters.

#### ... the Report On Foreign Investment In Residential Real Estate?

This is the report produced in November 2014 by the House of Representatives standing committee on economics and was commissioned by Treasurer Joe Hockey to examine what benefits for residential property foreign investment brings, and whether such investment can be said to be increasing the supply of new housing as well as bringing benefits to industries such as the building sector.

"Introducing boundaries, such as limiting the number of properties an overseas investor can acquire, or requiring developers to sell a percentage of their stock to Australian residents, I believe, will help provide more opportunities for local buyers."

### ■ FIRST-HAND EXPERIENCE

Melbourne-based buyers' agent Cate Bakos has seen first-hand the issue of overseas buyers altering the residential property landscape.

"In my home town of Melbourne," she says, "overseas investor demand in the middle segments of the east is over-represented and auction clearance results, median house price growth and the differential between the housing and unit market are obvious signals that this part of the market's quite tough for local buyers to compete in."

"I've experienced many situations where bidding against overseas buyers for land in the tightly held suburbs has been fruitless on my part. In several instances, overseas buyers have raised their hands high into the air and kept them there... no bidding tactics even tried."

"I have many local buyers who steer away from house street numbers featuring an eight. Those in the glossy and outer east know better than to compete."

"The overwhelming local buyer sentiment relates to their disgruntlement at the inaccessibility of houses in areas that were once-upon-a-time a home option for them, the inherent push they're feeling to venture out further or explore new areas altogether, and the overwhelming fear that home ownership is completely threatened for them by the apparent surge in offshore investor activity."

"I'd argue that while we can enjoy a buoyant market and an increase in our own property values, the changes associated with increased offshore investor activity (particularly the

explosion of high-density developments in areas that don't support them) is a negative for our market and our lifestyle."

That explosion in high-density developments is an area of concern for others in the property game, too, including Metropole Property Investment Strategists' Michael Yardney.

The wealth creation expert sees long-term issues with foreign investment.

"Currently there's an oversupply of apartments, particularly in the CBDs of Melbourne and Brisbane," he explains, "yet foreign developers are still busy building more towers to fulfil the demand of their overseas clients, despite the fact that vacancy rates in these locations are rising.

"Many of the inner-city apartments being built are small, of a poor standard and likely to become the slums of the future.

"Some of the buildings have a high (almost 100 per cent) predominance of investor-owners rather than owner-occupiers, which is likely to create competition for tenants at a time when the particular demographic renting these properties is diminishing."

Simply put, he says, the oversupply of properties will stifle capital and rental growth.

"The high prices for new properties being bought by overseas investors who aren't familiar with our markets are enticing some inexperienced local investors to also buy into these apartment buildings, setting themselves up for disappointment in the future," he adds.

Bakos sees the same problem.

"Due to the FIRB ruling requiring most overseas buyers to purchase brand new property," she says, "we're witnessing many high-density developments that have an imbalance of owner-occupier to investor-owners, offer limited infrastructure to support the number of tenants populating the area, and add to the higher vacancy rate issue we're currently facing in most of our capital cities.

"Worse still, median value price hikes for houses in the popular overseas-investor areas have been driven up so dramatically in some areas that new local owners could be quite vulnerable if laws were to change and overseas demand was to suddenly drop off."

#### ■ MEASURING IMPACT

Lewisson stops short of declaring foreign investment a problem: "There's definitely a new impact, from the number of overseas buyers, that wasn't there previously but... I don't think you can give a blanket statement to say it's negative across the board for all property buyers," he says. "It's a negative in certain locations where they're active, but that doesn't extend to the broader market."

The fact that overseas buyers are only really looking at certain segments is, of course, part of the problem. Lewisson

#### RULES AND REGULATIONS

##### What are the rules governing foreign investment in Australia?

The best place to head for that answer is the Federal Government.

##### The regulations

According to the Treasury, a foreign person can buy residential real estate in Australia, but there are restrictions for existing homes. "A non-resident foreign investor is generally prohibited from purchasing an existing home. A temporary resident (who has a visa of more than 12 months) can purchase one existing home to live in for the duration of their visa, but must sell within three months of leaving Australia at the expiration of their visa."

When it comes to what type of residence, "All foreign investors can purchase new dwellings but all purchases must be approved – in advance of purchase – by the Foreign Investment Review Board (FIRB)", the idea being that the building of new housing stock is encouraged.

Other regulations (as they currently stand) include:

- All foreign persons can purchase vacant residential land for development and new dwellings (with applications usually only being approved on the condition that construction begin within 24 months).
- All foreign persons can seek approval to redevelop an established dwelling, though those applications are generally only approved when the existing property is found to be derelict or uninhabitable.

##### The penalties

- Failure to comply with a final or divestment order from the Treasurer can result in a court proceeding to enforce the orders and can result in a fine of up to \$85,000 for an individual (\$425,000 for a company), imprisonment for a maximum of two years, or both.
- Penalties apply only to the foreign investor – they don't affect any third party, such as a real estate agent, who knowingly assisted them.

It's worth noting, however, that absolutely no enforcement activities have been issued since 2006, and only 17 divestment orders have been issued since 2003.

himself says: "The issue we've got is that it's so concentrated on Sydney and Melbourne at the moment. The types of projects that are selling are often very big ones and because they have larger numbers that they can take over to an agent in China, or even to a local agent that has a Chinese office, it's worth their while to do a big roadshow.

"Because the big projects are getting their pre-sales overseas... the downside of that is that it's all investor stock and rental stock, which means those big projects have a smaller proportion of owner-occupiers than they historically would've had."

An interesting idea put forward by Lewisson suggests that the boom Brisbane was predicted to see in 2014, and didn't,

could've been held back in part by the prevalence of foreign property investors in Sydney and Melbourne.

"It caught a lot of people by surprise that Melbourne saw such strong price growth last year," he says, "whereas Brisbane hasn't really seen any price growth in apartments.

"Part of the reason for that, I believe, is that the Melbourne market has continued (and Sydney's continued probably longer than it might have otherwise) and it's not until those markets start to slow down and volumes drop that the local investors, who are quite mobile, will then start looking at the next city for their investment purchases" – which would then, almost certainly, lead to increases in sales in other cities such as Brisbane. Lewisson has evidence to back up his belief.

"There are investment groups we've spoken to in the past that said, 'we'll only put our clients into Sydney and Melbourne because there are bigger Asian communities there and they know the people there and feel safer'. Brisbane's a bit of an unknown to them and they just stick to the safety of what they know."

The Reserve Bank of Australia's *Foreign Investment in Residential Real Estate* report remarks, "Dwelling purchases and development by foreign residents can increase the exposure of the Australian housing market to business cycles offshore."

Yardney mentions another point that crops up repeatedly – a concern with owners of properties living elsewhere.

"I also see future problems with difficulty chasing overseas

residents if they fail to pay their strata or owners corporation fees for the building's upkeep," he says.

"The poor standard of construction could mean owners' corporations run out of cash and you can see a scenario emerging where they can't maintain the building to the standards required.

"That could start a real slippery slide of other owners bailing out and a larger number of the units being on the market and prices then tumbling."

A similar scenario can unfold in any area where conditions change – for instance in mining towns – which can see foreign investors fleeing en masse, leaving local property owners vulnerable to value crashes.

#### ■ LANGUAGE BARRIERS

The rise in Asian investor numbers certainly seems to be introducing new elements into the property market – some of which are a little worrying, even discounting xenophobic worries about 'Asian-looking' people at auctions.

According to Lewisson, Asian investors are very much relationship-driven, which can lead to difficulties for them obtaining information – or at least reliable information.

"A lot of them don't speak English," he says, "so they're relying on people to tell them where to go, or give them information, and they can't do a thorough analysis of the market."

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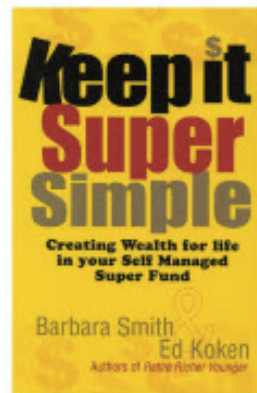
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"I've experienced many situations where bidding against overseas buyers for land in the tightly held suburbs has been fruitless on my part."

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Lewis illustrates the point: "You rarely hear a story about a US businessman coming in and paying a lot more than anyone else was prepared to pay."

This vulnerability can result in certain elements of the industry leading investors astray.

"Some of those doing well in terms of sales numbers from overseas buyers," Lewis says, "particularly for large-scale apartment projects, are having a tendency to prostitute their project in order to get some extra sales through the overseas channels, rather than trying to protect the local market." Such manoeuvres aren't rampant, he says, but are happening.

"It's something to be mindful of as a developer, needing to ensure you protect your own brand," he says.

"There are developers who are in it for the long haul and there are some who are out to make their money in the next five or seven years and they're not too worried about their legacy."

For Ben Kingsley, chair of the Property Investment Professionals of Australia and CEO of Empower Wealth, the positives of foreign investment outweigh the negatives, but care needs to be taken.

"We certainly do need to monitor any 'real' impact that might occur regarding dwelling affordability for our own population," he says. "It's not the case at the moment, but if demand for Australian property continues to grow at very strong levels for the next few years, we might need to see some changes or initiatives put in place to ensure housing remains affordable."

For others, the time for monitoring is now.

"I do believe there's more the Australian Government could do to curb ridiculous price growth and locally unsustainable competitive conditions," Bakos says. "FIRB regulations could be tighter, particularly in relation to parents' purchases for student children. Off-the-plan investments and rebates especially need closer attention, and investor caps in high-rise buildings could be reconsidered in light of our current market high-vacancy conditions."

In order to avoid excessive sales going to Melbourne or Sydney, Lewis believes "there's a need for government – federal or local – to control the manner in which we allow overseas investment to integrate into our market" adding that perhaps controls on how many sales go out through a particular new development could be introduced, in order to even things out across markets.

#### ■ FURTHER SUGGESTIONS

The Real Estate Institute of Australia, in its submission to the FIRB inquiry committee, suggested that the maximum \$85,000 penalty for non-compliance by temporary residents (i.e. people buying properties without approval, using third parties to breach the rules, etc.) didn't go far enough. Head of the committee Kelly O'Dwyer agrees, pointing out that to some buyers, this fine is simply seen as "the cost of doing business" and isn't a deterrent at all. She says that fines ought to relate to the value of the property rather than be fixed.

Concerns have also been raised about the origins of foreign buyers' finance. Despite claims from some areas of the industry that most of the finance is found in Australia, representatives from the main banks refute the idea, with Australian Bankers' Association CEO Steven Munchenberg saying: "My expectation would be a typical non-resident foreign investor into Australia is wanting to invest money from overseas into the Australian market. They're not going to be coming to us for a mortgage. They have the money." Munchenberg was backed up by ANZ deposits and mortgages general manager Brad Gravel, who told the inquiry, "... of all the residential investment coming from offshore, based on our personal experience, only a small proportion is financed by Australian institutions."

Of course, this does mean more money coming into the Australian economy.



#### THE PROS

Those with their thumbs up for foreign investors cite the clear gains derived from extra interest – and capital – being pumped into the market, as well as increased supply and competition.

Domain Group senior economist Andrew Wilson tells API: "The latest data from the FIRB indicates that the contribution of foreign buyers to housing market activity is minimal" and goes on to describe the lack of restrictions on foreign investors purchasing new property as "a positive, as foreign investment in new dwellings adds to the stock of housing."

This is the angle Kingsley also takes, saying: "I think it's a real positive for our economy, as we transition from the mining boom of the past decade or so and realign our economy back towards the mainstream economy. Foreign investment is going to play an important role in our overall gross domestic production and also in absorbing the large mining workforce transition from the post-capital expenditure peaks we've now passed."

Yardney, too, sees the positives as well as the negatives.

"The wave of new property development, particularly inner-CBD off-the-plan projects, has been good for our construction industry and our economy in the short-term."



“Foreign investors are a vital cog in the wheel of our industry.”

BEN KINGSLEY

#### SUMMARY OF THE DEBATE

PROS	CONS
A boost to the housing supply	Foreign investors will sometimes pay too much for properties they want, pushing up prices.
Crisis supply provides jobs in many areas, including construction, tourism and finance.	Ignorance and language barriers can lead to misinformation.
Increased demand can indeed boost prices, which can be a good thing for local investors.	Foreign investors can get stuck on certain areas, which might prevent the property cycle moving as it should.
Removing foreign investors could lead to higher prices as pressure on supply grows.	Can lead to an oversupply, particularly of apartments.
Brings new money into the economy	Foreign investors don't always play by the rules and current monitoring is ineffective.

#### ■ TO THE RESCUE

Lewis goes so far as to say that foreign investors actually saved the day for some developers in Australia around the time of the GFC, as they couldn't get sales locally.

"They were willing to pay the extra money for their marketing costs," he explains, "and go over there [Asia] in the hope of landing four or five sales, which would make it a worthwhile trip for them."

Along with many of the people interviewed, Lewis feels that foreign investor numbers currently are at a healthy level.

Reflecting as an "insider" of the property industry, he says: "Many people see opportunity in new."

"It brings new money to the country. If Mr Jones owns a warehouse that he's been sitting on for a few years, and he asks for \$10 million but gets \$15 million for it, that extra \$5 million gets circulated through our economy."

Property Council Victoria executive director Jennifer Cunich is pleased with the effects she's seen foreign investors have on the industry, particularly in her own state.

"They're helping lift industry buoyancy," she says, "by playing an active part in the local market." Their significance, she adds, should not be underestimated.

Tasmania is tipped for a lift, too, since Chinese President Xi Jinping paid a visit, which was splashed all over TV screens back home in November 2014.

Henry says: "Views from Tasmania on Jiwai.com saw a 114 per cent increase in the second half of the month [November] compared to the first half. Chinese real estate buyers have gone from unaware of Tasmania to curious. This could turn into a blessing for beleaguered vendors in Tassie."

According to Henry, the average budget for an Asian buyer in the Australian market is \$1.35 million.

"It's certainly not a first homebuyer type property," he says, dismissing claims that foreign investors have been pushing first-timers out of the market as unfair.

"What it really does is propel the market forward. We see a lot of net benefits... the majority of properties international buyers purchase are new builds, so you actually see an awful lot of activity in the economy at the local level – finance, accounting, tourism."

#### ■ KEEPING US GOING

Graham Wolfe, chief executive of industry policy and media for the Housing Industry Association, is sure foreign investment is a positive force.

"Foreign investment through pre-sales in multi-unit developments can be crucial to ensure that many of these

projects come to market," he says. "That obviously benefits potential domestic buyers as well as renters, through more choice and competition."

Kingsley agrees, and sees the potential for foreign investors to help us avoid a post-mining sink. "Indirectly, a lot is riding on what has been called the 'construction-lead' recovery as our national economy has slowed due to the mining downturn, plus the decision of large manufacturers to move their operations offshore where labour costs are more favourable.

"People need to understand that any foreign investment and monetary inflows goes straight to the bottom line in our economy, especially when they're using money sourced from their country, and we need to re-train and find new job opportunities for those in the manufacturing sector; construction jobs are certainly a likely option."

He goes on: "If foreign investment into residential property wasn't possible, locals would have fewer dwellings built, limiting choice and putting pressure on supply levels and therefore possibly increasing the value of property further."

"Foreign investors are a vital cog in the wheel of our industry and they, like local investors, provide a great service to those looking to rent, a service that all levels of government simply can't justify providing themselves."

Lewis makes an interesting point about other countries' attitude to foreign buyers, particularly as Australia is one of the strictest in the world when it comes to regulations.

"I think we can be very insulating in Australia, asking 'what's this doing to our market?' without actually looking at the impact on those markets overseas." Considering most countries have no restrictions on foreign investors purchasing property, including the UK, it's a fair point.

The advice from Propell Valuers makes plenty of sense, too: as foreign buyers are here to stay, domestic buyers would do well to "deal into the game and buy into the same market", particularly when you consider that price growth is likely to be stronger in those markets attracting foreign buyers.

#### ■ IT'S NOT OVER

There's no doubt this is a debate that will run and run. And the fact is, Australian property will continue to appeal to investors outside our shores, particularly in the near future as the dollar's downward run, having recently hit the sub-80 cent level, seems destined to continue.

In summing up the House Economics Committee's findings, O'Dwyer says: "As a relatively small nation, Australia will continue to rely on foreign capital to help grow our economy and provide jobs. In the case of housing, foreign investment creates more dwellings for Australians to build, buy and rent. However, Australians must have confidence that the rules, including those that apply to existing homes, are being enforced. Our enquiry revealed that, as it stands today, they could not have that confidence."

Foreign investors into the property market can have a good and a bad effect on investors – much like so many elements of property investing. If overseas buyers help to push up prices in certain areas, holders of property in those areas will be laughing all the way to their equity, while investors looking to purchase there may find their route challenged slightly.

In the words of Lewis, "you can rail against what's happening or you can accept things as inevitable, get on with business and find a way to succeed and thrive". ■